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Let's Make a Deal: A Dentist's Guide to Buying and Selling a Practice

Here's some practical advice for buyers and sellers that will enable you to avoid mistakes and increase your chance of success

Although the purchase or sale of a dental practice is a business transaction, it involves more than money. Seller's emotions run deep. The sale signifies the end of an exciting and rewarding career. For many doctors, there may be a loss of identity. For others, they face their own mortality for the first time. Most sellers experience a feeling of separation and loss as they leave behind both staff and patients.

Buyers can experience anxiety, if not sheer terror. Buying a practice is exhilarating as well as intimidating. Exhilarating since it is a new beginning and a change in lifestyle. Intimidating because it is an awesome responsibility and a long term professional and financial commitment. It takes courage, vision, self confidence and desire to buy a practice. Success requires dedication and hard work.

Accept the emotions you feel. Sellers embrace the sale with enthusiasm and you will avoid post-sale depression. Buyers be honest and realistic regarding your fears and you will avoid pre-sale anxiety.

Although buyers and sellers may appear to have an adversarial relationship, they would like to avoid mistakes and conclude the sale. If the parties follow these principles, they will increase their chance of success.

Get Professional Help. Retain a professional practice appraiser, an accountant, an attorney and any other professionals experienced in practice valuation and sale. The purchase or sale of a dental practice is complicated transaction. A professional appraiser can help you determine the value of the practice, an accountant can answer tax questions and an attorney can prepare a letter of intent and purchase and sale contract. These professionals will provide the buyer and seller advice that will enable them to steer clear of potential problems and make the right professional and personal decisions.

Check out the Catchment Area. Normally, the buyer will conduct a market analysis of the catchment area. However, if the seller conducts the analysis before he offers the practice for sale, marketing the practice is much easier.

A market analysis is a study of the primary and secondary catchment area of the practice. It marks the population; lists the communities; sets forth demographics, i.e., age, education, occupation, income and speaks to the outlook for the local or regional economy.
The analysis should also describe office location, i.e. access and egress, parking, public transportation and the adjacent neighborhood. A good market analysis also should indicate the number of dentists who practice in the primary and secondary areas.

ADVICE FOR SELLERS

Get Professional Help. I can not emphasize this enough.

Plan for the Future. Work hard. Maintain an active, viable practice. Continue to market your practice and acquire new patients. Take care of your equipment and invest in new technology. Keep abreast of developments in continuing education. Manage the day-to-day operation of your practice efficiently and productively. Reduce excesses and improve the use of human, financial and physical resources. Participate in managed care.

Finally, safeguard the values of your practice. Pursue quality and recognize it is the key factor in determining value, marketing the practice, and concluding the sale.

Establish a Realistic Market Value. Engage a professional to establish the purchase price or value of your practice. Render a written practice appraisal. Paint a picture of the practice and let the buyer know where it has been, where it is, and where it is going. Describe the catchment area and office location. Discuss your clinical focus, payor profile and service mix. Talk about case management, technique, personnel. Provide a financial history of the business. A professional practice appraisal will make the difference in selling your practice and maximizing the sale price.

Be Honest. Make full disclosure. Don't hide problems. Buyers eventually learn the truth.

Tie Up Loose Ends. Put your business in order before you offer your practice for sale. Clean up your practice. Poor records, lawsuits, undisclosed borrowings, tax liens or other unfinished business turns off buyers. Obtain proper title to the assets. Pay past due bills or back taxes. Complete all government reports. Bring your financial statement up to date.

Be Patient. Unless the sale of your practice is urgent, wait for a buyer who is professionally and financially qualified to purchase the practice. Don't panic. If you have a quality practice that is realistically valued, you will sell it and receive a fair price.

Work Hard During the Transition Period. Transfer your professional goodwill to the buyer. Work with the buyer to help him retain the patients of record. Introduce the buyer to your patients as well as your professional referents. Facilitate staff transition.

ADVICE FOR BUYERS.

Get Professional Help. The purchase of a dental practice is complicated. Get help.

Gather Information. In order to differentiate disease or confirm diagnosis, a dentist must take a case history of the patient and conduct an examination. The purchase of a dental practice is no different. In order to decide whether or not to purchase a particular practice, a buyer must gather facts and figures.

Ask the seller for a copy of the practice appraisal. Read it carefully. Ask for supporting documents such as federal income tax returns, interim financial reports and any leases or other contracts that are binding on the practice. Gather information on the primary catchment area. Conduct a market analysis.

Kick the Tires. Interview the seller. Audit the appointment book, day sheets, accounts receivable ledger and payroll records. Study the patient charts. Review reschedule procedures. Ask about patient recall and patient reactivation protocol. After you interview the seller, visit the practice again and observe the seller at work. Observe the work flow of the office. Meet the clinical as well as the administrative staff.

Go slow. If you make a mistake, you will live to regret it for a long time to come.

Buy Results. A buyer must decide whether or not to buy a particular practice and what to pay for it based on facts and not emotion. Focus on the track record of the seller rather than on your potential. Evaluate the present. Don't speculate on the future. Optimism will not enable you to make a decision; facts and figures will. Hope may spring eternal, but it does not pay the bills.

Be Reasonable. Do unto others as you would have them do unto you. If you do not have a genuine interest in the practice or can not afford it, tell the seller. If you are not a serious buyer, don't ask the seller to produce volumes of records. That is not reasonable. On the other hand, if you are serious, the seller will be happy to produce the information you need.

If the facts check out, buy the practice. If the facts don't check out, there is no sale.

Here are the answers to some FAQs:

1. How important is a non-compete clause? Is it enforceable? A restrictive covenant is a provision in a purchase and sale contract that prohibits a doctor from practicing in a prescribed area after he leaves the employ of the practice.

In most states, a non-compete clause is enforceable if it meets five tests of reasonableness: Is the covenant in the public interest; Is the covenant necessary to protect the economic interest of the practice; Is the covenant fair to the restricted employee; Is the covenant reasonable in duration; Is the covenant reasonable in distance.

Violating a restrictive covenant is risky business. Unless the covenant is specifically prohibited under the laws of your state, the seller should include a covenant in the purchase and sale contract and abide by it.

2. Should you offer an associate a purchase discount for his/her prior service? An associate doctor may help grow and manage the practice of the seller, but, in my opinion, the employer-doctor should not discount the value of the practice as a reward to the associate for honoring his contract and working hard. If the associate is a high-performance doctor, his reward is a promotion to partner.

3. Should the seller finance the purchase price of the practice? The inability of the buyer to access capital is a strong impediment to the sale. If the seller becomes a banker, he will increase the marketability of the practice, but will incur a significant credit risk.

Unless the sale of the practice is urgent, the seller should wait for a financially qualified buyer or limit the amount of the seller note to less than 25% of the purchase price. If the sale is urgent, the seller could finance up to 60% to 75% of the price but never 100%.

Qualify the borrower; support the seller note with life insurance in the amount of the debt as well as disability-income insurance with monthly benefits that are equal to the amount of the monthly note payment; secure the note with a lien on the assets of the practice. Limit the term of the seller note to seven years. A third-party guarantor will strengthen the credit.

4. The allocation of the purchase price is a tax question, not a valuation issue. The sale of a practice is not one sale, but a series of sub-sales. For tax purposes, the purchase price must be allocated to each asset sold. Gain or loss is computed and each asset is taxed individually.

In order to minimize the tax consequences of the sale, the seller should allocate as much of the purchase price as he can to assets that will be taxed at capital-gain rates and allocate minimum value to assets that will be taxed at ordinary income tax rates.

5. Purchase of stock v. purchase of assets. If the buyer purchases the capital stock of a C corporation, the purchase will be subject to any pending or potential corporate liabilities. Although the seller can indemnify the buyer for any loss, the seller can not eliminate the risk. In addition, capital stock is not depreciable. If the buyer purchases capital stock, he will lose the tax benefits of the sale.

If the seller sells the capital stock of the corporation, the corporation will pay corporate income taxes on the gain-over-basis and then the seller will pay ordinary income tax on the remainder. The combined federal marginal tax rate could be as much as 73% of the gain. The purchase of stock versus the purchase of assets is a complex legal and tax question. Speak with your accountant or attorney.

The author, David J. Shuffler, is a specialist in practice valuation, business planning for doctors and other health care professionals. A frequent author on practice valuation, Mr. Shuffler's articles have appeared in Medical Economics as well as other professional journals. He has been the guest speaker for numerous professional organizations, including hospitals and medical centers. Mr. Shuffler holds a bachelor's in economics from the Wharton School of Finance & Commerce, University of Pennsylvania.

If you have questions regarding practice valuation or buying or selling a practice, please call The Practice Valuation Group at 1-877-833-3738. Ask for David Shuffler.