EPSTEIN PRACTICE BROKERAGE LLC

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Busting Practice Transition Myths

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MYTH: Practices are typically valued at and sold for 100% of collections.

FACT: While it is currently a sellers' market in most of the country, dental practices typically sell for 60%-80% of the most recent year's annual revenue. However, rule of thumb valuations solely considering annual revenue are just that, a rule of thumb. You should be skeptical of any practice broker who attempts to establish an asking price for your practice based solely upon one factor or another. A formal and accurate valuation that takes all aspects of a practice – annual revenue, net cash flow, type of patient base and dentistry, location, quality of equipment and facility, etc. – into consideration is a necessity. Occasionally, a practice will sell for 100% of revenue if it's located in a highly desirable market and all other factors are in excellent condition; updated facility with 5+ ops in a high visibility location, FFS patient base, low overhead, etc. Otherwise, the practice value will most likely fall in the normal range discussed above.

Hopefully, by dispelling these myths, we have given you some valuable, real world insight into several factors involved with a practice sale so that you can make an educated decision when the time comes to plan your practice transition.

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The Dental Transition NEWSLETTER

In this issue

Preparing Your Practice for a Sale

As practice brokers, we often receive a call the day a dentist decides to sell their practice. In some cases, this phone call is the first time the practice owner has given serious consideration to the value and marketability of their office. Unfortunately, the doctor's lack of foresight and planning has resulted in making choices (or failing to make choices) that resulted in a substantial adverse impact on the value and/or marketability of the practice in the years leading up to the sale. Nobody enjoys telling someone their "baby is ugly" but that is sometimes the position in which we find ourselves due to a lack of proper transition planning on the seller's part.

With the Baby Boomer generation reaching retirement age, a large wave of sellers will be taking their practices to market over the next five years. With a substantial increase in the inventory of practice acquisition opportunities, it's imperative to take the following steps to stand out from the pack and ensure that your office is as valuable and marketable as possible when the time comes to begin looking for a buyer:

1. Keep your foot on the gas. Your revenue level is one of the key factors impacting practice value, as the value of most dental practices falls in the range of 60%-80% of annual revenue for the most recent year. Revenue trends are also an important indicator of the overall health of your office. If you are planning to cut your work schedule, consider hiring a part-time associate doctor or accelerating the date of your practice sale.

2. Monitor and control your overhead. Profitability is a prerequisite for value, as net cash flow (revenue minus overhead) is the single most important driver of practice value in the minds of buyers, their advisors, and lenders. Are your major overhead expenses in line with the following benchmarks?

Staff Salaries/Benefits	*25%-30% of Revenue*
Occupancy Costs (Rent/Utilities)	*6%-10% of Revenue*
Dental Supplies	*5%-6% of Revenue*
Lab Fees	*6%-10% of Revenue*
Advertising/Marketing	*2%-5% of Revenue*

We all know that overhead only seems to increase over time. If practice revenue is declining while overhead is increasing during the years leading up to a sale, it will undoubtedly cause massive erosion in the net cash flow and value/marketability of your practice.

3. Consider updating your office décor and equipment. The appearance of the office and age and quality of the equipment/technology is increasingly becoming a hot button among buyers. Is the appearance of your office congruent with the quality of your dentistry? Buyers and patients often believe this is the case. Therefore, if your time horizon for selling is more than three years away, it is wise to consider investing in digital radiography, updating/upgrading your computers, server, and practice management software, going paperless, and reupholstering your

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Preparing Your Practice for a Sale

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patient chairs. If a practice sale is in the nearer future, you should forego any major equipment purchases but consider updating the aesthetic of your office (new paint, change carpet to laminate wood flooring, update furnishings/décor, etc.). Enhancing the "curb appeal" of your practice can go a long way in improving its marketability.

4. Evaluate and raise your fee schedule as needed. Your fee schedule plays a vital role in the profitability of your practice. Raising your fee schedule on an annual basis will help to combat rising overhead costs and allow you to maintain/increase the net cash flow of your practice.

5. Clean up accounts receivable & credit balances. Many practices have a large balance of > 90 days accounts receivable due to uncollectable balances that have not been written off. It is important to clean up your accounts receivable and credit balances prior to beginning the transition process to avoid giving buyers the impression that your practice has an issue with collections.

6. Reduce discretionary write-offs on practice tax returns. In the years leading up to a practice sale, it is wise to instruct your accountant to reduce aggressive tax write-offs (such as running personal expenses through your practice financials) so that potential buyers and their advisors can easily determine the true overhead and profitability of your practice.

7. If you have an associate doctor, make sure you have an associate agreement with a non-compete in place. If you are planning to sell your practice to your associate, it may be time to establish a formal agreement regarding the future sale date and price for the practice.

8. Consult your financial advisor and tax accountant. How much money do you need to retire? How much retirement savings do you currently have on hand? What are the tax consequences associated with the practice sale?

9. Be realistic regarding the time it will take to sell your practice. Practices typically sell much faster in metropolitan areas (3-6 months) versus rural areas (1-2 years or more).

10. Meet with an experienced practice broker or transition consultant to discuss transition strategies and have a practice valuation completed in advance of the sale. A practice valuation can serve as a valuable tool in identifying areas where you can increase the value of your office in the years leading up to the sale.

By planning ahead and taking the above steps, you can rest easy knowing that you will be in the position to maximize the value of your practice when it's time to begin the transition process.

What Our Clients Have To Say About Us Matters

"Mark Epstein did an outstanding job for me. Not too long after we met, Mark had a buyer for me. All went very smoothly. Mark answered all my questions along the way. I received an excellent price for my practice and would highly recommend Mark to anyone planning to sell their practice."
– Irving Gerstman, DDS, New York, NY

"My greatest fear after making the decision to sell my practice after a 40 year career was not finding the right person. I didn't just want it to be a business deal. Epstein Practice Brokerage had the volume of potential buyers to be able to help me find the right person. I could not be happier. My staff and patients are equally as pleased."
– Michael Goldberg, DDS, Midland Park, NJ

Busting Practice Transition Myths

Over the years, we have heard many myths regarding practice transitions that doctors mistakenly accept as facts. We feel that it's our responsibility to dispel the following urban legends so you can make smart decisions when planning your practice transition.

MYTH: The practice will lose 30% of the patient base immediately following the sale.

FACT: While it's true that practices will lose "some" patients following a sale, the amount of patient attrition is typically far less than 30%. Assuming the buyer is a good fit for the practice and the transition is handled properly, the typical attrition rate is closer to 5%-10% of the patient base. Many of the departing patients are typically friends and family members of the selling doctor who don't live near the office. While these patients may decide to find a new dentist closer to home following the sale, they are typically replaced by the friends and family of the new practice owner.

MYTH: The seller needs to continue working in the practice for at least 3-6 months following the sale in order for the transition to be successful.

FACT: Each situation and practice is unique. However, a large number of our transitions are structured as "walk away" sales where the seller does not step foot in the office following the closing date. Even with that type of transition structure, patient attrition is minimal so long as the buyer is a good fit for the practice and does not make any abrupt changes to the office. It's also important to note that it takes a significant shift in the mentality of the selling doctor (from an owner to an associate) in order for the seller's continued presence in the office post-closing to have a positive impact on the transition. If the seller has the right mindset, staying on following the sale can help with patient and staff retention, especially in a fee-for-service practice where the selling doctor has a magnetic personality. On the other hand, a seller who is reluctant to relinquish control of the practice to the new owner can have a negative impact on the transition. On average, the typical practice transition involves the seller sticking around for 4-6 weeks post-closing to ensure a smooth transition of ownership and maximize patient retention.

MYTH: My associate doctor is going to buy the practice.

FACT: This sounds like a great idea in theory; however, the ADA estimates that 75% of associate buy-ins fail prior to fruition. Oftentimes, these relationships fail due to an incongruence in practice philosophy, lack of busyness, timing (the seller is not ready to sell when the buyer is ready to buy or vice versa), or a differing opinion regarding the value of the practice – just to name a few. If you are planning to sell your practice to your associate doctor, it's important to have an employment agreement (with a non-compete) in place and to formally agree on the principle terms of the sale (closing date and method of determining the price) early on in the relationship.

MYTH: The landlord will release me from liability under the lease upon the sale of my practice.

FACT: The vast majority of the time, the landlord will require the original tenant to remain liable for the lease until the expiration of the current lease term. Therefore, unless your lease explicitly states that the landlord is required to release you from liability upon assignment, you will likely be required to remain liable for the lease until the expiration of the current lease term. If you will be negotiating a new lease or lease extension prior to the sale of your practice, it's imperative for you (and your advisors) to pay attention to the assignment provisions. If possible, you should attempt to negotiate a clause that requires the landlord to release you from liability upon assignment of the lease.

MYTH: The Seller will need to finance all or part of the practice purchase price.

FACT: There are several nationwide dental lenders and numerous local/regional banks that provide 100% conventional financing for dental practice acquisitions. Seller notes are typically only required in situations where there is a perceived risk that the bank is trying to mitigate, such as a buyer's lack of experience/production history, a declining revenue trend, the seller owning another practice nearby, or the seller asking for a premium price for the practice. If you are selling real estate in conjunction with the sale of your practice, it is relatively common for the buyer to ask the seller to hold a note for 15%-20% of the real estate purchase price since most banks do not provide 100% financing on real estate.

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