

Australian Dental Practice - Article – Jan/Feb 2003

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Buying and Selling the Specialty General Dental Practice

George was a dedicated dentist who had been running his own practice for about 30 years. During that time he had developed a deep professional interest in advanced techniques. His practice included a substantial orthodontic component and he attended several courses in orthodontics both in Australia and overseas to refine his skills. Specialist orthodontists may not have agreed but, George had reason to believe that he was pretty good in the orthodontics area.

George's crown and bridgework was also excellent and he had been one of the few dentists to go thoroughly into the area of treatment of sleep disorders. In his earlier years, he had spent a lot of time and expense on skilling himself, often to the detriment of his practice.

As George developed the special side of his practice, his declining interest meant that he passed on the traditional elements of his practice to Fred an employed dentist. Fred's workload in the practice gradually built up to the point that he was full time. Fred had an agreeable personality and generated quite a lot of personal referrals. However, as Fred became busier, he had reached a comfort zone whereby his remuneration based on the standard formula was sufficient to meet his needs. Fred was working four slightly extended days per week and utilising his three day long weekend to pursue his personal hobby of fly fishing. Fred's spouse had a reasonable income and they were content with their lifestyle. He was happy to refer back to George those patients in need of advanced treatment. Many would say that the relationship between the proprietor George and the employee Fred was almost ideal in a dental practice.

Realising that he couldn't persuade Fred to work any more hours, George introduced Mandy, a hygienist, to the practice. It seemed that George was lucky with staff. Mandy clicked with him and George was gradually able to build her role in the practice from one day to three and a half days per week. Mandy also enjoyed doing practice administration which George hated and he managed to increase her workload to a five day week with one and a half days devoted to the administration tasks.

Looked at closely, the actual situation was that George made good profits in his own surgery. He broke even on the hygiene components of Mandy's work and was content to pay her for the administration work. The profit in Fred's surgery was about five cents in the dollar of fees after Fred's salary and all overhead expenses had been met. However, George was happy in the practice and he had helped it evolve into one in which he was able to do work largely of his personal choice. Overall the fees looked like this:

- George working a nine session week, spending four weeks each year on training courses and enjoying a four weeks holiday, but generating \$550,000 of fees in his own surgery.
- Mandy working a five day week with 30 percent of her time spent in practice administration. Mandy generated about \$130,000 of fees per annum.
- Fred working four extended days per week and generating \$300,000 per year.

Overall, the practice grossed \$980,000 and was by most standards a well respected practice. In George's terms it was a successful practice. However, George like many dentists was limited in his terms of reference of comparison.

As George approached the age at which he contemplated retirement, his mind was repeatedly switched to succession planning. Quite a few people had praised his practice over the years and George asked his accountant what he thought it was worth. George's accountant like most accountants had only ever dealt with a couple of dentists. He looked up a reference on small business valuation which carried examples of prices applying to newsagents, Victorian Tattsлото agencies and postal agencies. Based on that criteria, the practice appeared to be worth \$800,000. George's accountant did not understand the internal workings of the dental profession. In particular he had no conceptional idea as to the amount of George's fee base, which was transferable to another dentist.

Armed with a report from his accountant, George approached Fred and offered to sell him fifty percent of the practice for \$400,000. Fred may not have been the most businesslike dentist in town, but he realised that:

1. The price was absurd.
2. He had no interest in pursuing the skill levels necessary to takeover a component of specialty treatment plan fees.
3. He didn't think that Mandy did enough.
4. He mentioned to his wife that he thought George had acquired delusions of grandeur.

As a result, Fred did not display any interest in George's offer.

George now reasoned that he had met lots of top dentists at the various courses that he had attended and he advertised the practice for sale.

To his surprise, none of the dentists who inspected the practice, believed that they could takeover his specialty fee base and nobody seemed to take his asking price seriously. He had not realised that selling a portion of his practice was going to be so difficult. He began to realise that there were areas of his practice which made transfer of the economic benefit to another dentist quite difficult.

At this point, George fell ill. Initially it was thought that he would only be absent for a week or two, and his patients were rescheduled. Unfortunately the illness took a turn for the worse.

Meanwhile back at the practice, Fred and Mandy each did what they could to assist with Fred filling up his working week by giving up his day off and Mandy generating as many oral hygiene appointments as possible. Together with George's spouse they toyed with the idea of getting a locum, but George's patients were heavily bonded and it was very difficult to get a locum with the appropriate skills. An increasing number of George's patients had to be referred on to specialists.

After a further six weeks it became apparent that George's illness was getting worse and even under best case scenarios was unlikely that he would return to work in the near future, if at all. By now a lot of patients were aware of his absence and all orthodontic patients had been referred on for completion of treatment plans. Many patients decided to attend other practices recommended by friends.

Fred had lifted his output but found that about \$8,000 of fees per week were about his personal comfort level.

After an initial period, Mandy's oral hygiene appointments began to decline as George was no longer present to generate internal referrals.

Louisa, George's dedicated chairside nurse had initially taken leave and had been relieving Fred's nurse while she took a couple of weeks leave. Finally, she had had to be retrenched.

At peak intensity the practice had employed two receptionists, one of whom also assisted with infection control procedures. However, the patient load had now dwindled. Each of the receptionists had co-operated by taking some accumulated leave. Perhaps fortuitously one was now offered another job and she reasoned that she should take it as her old job seemed to be in danger of disappearing.

Mandy too, realised that her job was being squeezed and she shifted to a three day week doing approximately two days of oral hygiene appointments and one day of practice administration. She filled in the other two days in another practice. It transpired that the other practice had a significant need and they suggested that Mandy could work up to a full-time patient load if she wished. Mandy confided to Fred that she was contemplating this change.

At this point, George's medical specialist advised him that he was never going to work again. George's family arranged for a practice broker to list the practice for sale; again. The broker looked at the last couple of years fees and suggested sale of a package of goodwill and equipment for \$400,000. Simultaneously the family offered the practice to Fred. Fred was now being

offered the whole of the practice for the same price that he had previously been offered the half. However, Fred reasoned that:

- George's personal goodwill had largely evaporated. Many of George's loyal patients hearing that he was no longer practicing, had gone to another dentist recommended by close friends or relatives. In particular, those patients who had had complex speciality treatment plans had been referred on, or alternatively Fred had been unable to satisfy their needs.
- Mandy's patient base had collapsed and Mandy was about to leave the practice.
- In reality, the practice had reduced to a one dentist traditional type practice centred on Fred supported by one nurse and one receptionist.
- Although functional, most of the equipment was well worn. At most, Fred needed one fully equipped surgery and a limited second surgery to cope with the occasional emergency. Fred had never been attuned to the type of dentistry required to running two busy surgeries, two nurses and a heavy schedule.
- The rent of the premises was now high relative to the maintainable Fees.

Fred advised the family politely that \$400,000 was too much. Over the next few weeks it became apparent that the practice broker had overstated the appeal of the practice. In actual fact, the word had passed along the dental grapevine that the practice was no longer the one that had generated \$980,000 of fees. To make matters worse, potential buyers were now not too sure what the current recoverable fee base really was.

Catch 22

Most potential buyers realised that in order to quickly provide patients for themselves they would have to sack Fred, but in sacking Fred, legal niceties aside, they would also have to run the risk, that a significant portion of the remaining goodwill of the patients was attached to him. They needed Fred's active co-operation to ensure that they maintained as many of the fees as possible. Faced with the Catch 22 situation, they moved on.

Eventually Fred found an experienced dental financial adviser and after a period of quiet negotiation, purchased the practice for a realistic price.

Some Lessons

1. For those who run specialty practices, the very features of the practice which gives them high income and personal satisfaction, are the aspects which are hardest to pass along to a potential purchaser. In other words, the transferable economic benefit may be restricted.
2. Often the most saleable practices are the traditional practices in which given an orderly handover, any competent dentist of reasonable experience should be able to takeover and maintain. Indeed, some practices have a certain amount of hidden gold in that many of their patients may have been under serviced during an older dentists last few years of practice.
3. Valuing businesses, (any type of business) is a specialist activity. In most industries there is an accounting firm which specialises in that industry and which has much better knowledge than generally available. Accountants who value practices on a one off basis are usually way off the mark.
4. Practice brokers are not good at valuing practices. It's the old real estate syndrome of quoting a high price to the seller and hoping to knock them down to meet a buyer. Additionally, dentists should be wary of the two-card trick of having a broker value the practice and an equipment supplier separately value the dental equipment. The practice needs to be valued holistically starting with the financials then updating for current changes. Proper attention to depreciation, leasing or hire purchase charges will appropriately capitalise the value of the equipment into the practice.
5. If there is an employed dentist in the practice who has worked there long-term and has a substantial relationship with the patient base, transferring that person's workload to a new proprietor is tricky. In extreme circumstances, there may be issues of unfair dismissal, "constructive dismissal", or redundancy payment involved.

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