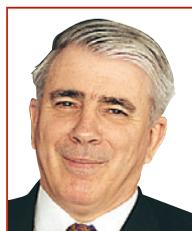


# Dental buys, sells and start-ups: Brickbats and bouquets

By Graham Middleton, BA, MBA



*“Dentists frequently misunderstand the amount of fit-out cost buried in the floor and walls of their practice and the benefit of taking ownership of their own premises. This can lead to expensive misjudgements...”*

**S**elling a high-end practice to a corporate: Freddie has long been in the top five percent of dentists by production of fees in his own surgery. He was one of the earliest dentists to heavily engage in implants and had long invested in developing his own skills in a variety of areas. He also had a significant degree of charisma and was recognised as a “top of the town” dentist. Freddie sold to a dental corporate for a figure north of \$2 million, plus a deferred element paid over three years provided that he meets achievable targets. As any dentist with the skills and personality to replicate Freddie already owns a successful practice, his was a practice which would have fetched less in the normal market, because he would have had to wind himself down and build up the remainder of his practice to make it saleable.

## Prediction

**I**t is likely that after Freddie completes his contract and eventually moves on, the high-end part of the practice will leak away and other high-end practices will replace his spot in the market. In reality, the only dentists who can match Freddie’s attributes are already conducting successful practices.

## High rents and absence destroys value

**C**ynthia owned a practice upstairs from a large medical facility with a high rent relative to its fees. The practice had two chairs but in practice, was about a 1.5-dentist operation.

Cynthia had an injury which removed her from the practice and she instructed her receptionist to defer patients, hoping to get back to work.

As time dragged on and deferrals continued, patients went to other dentists because they were not allowed an appointment with the employed dentist working the other chair.

A belated attempt to sell the practice to her assistant dentist confronted the problem of high rent and a much-reduced patient base. In effect, more than half the practice had disappeared over a period of nine months.

Inevitably, the high rent costs relative to a diminishing fee base meant that the practice was operating at a loss and Cynthia’s assistant dentist declined to buy it. Effectively, the practice had gone from being saleable to an unsaleable, loss-making operation with a diminished fee base which won’t return.

### Buying a CBD associateship

**D**aniel has a CBD associateship with Clive, who is ten years younger. Daniel's fees are about \$500,000 and Clive's about \$850,000. There are three chairs. Each own their own fees and Clive has a part-time dentist who uses the third chair. Daniel wishes to sell.

Given the difficulty of marketing for new patients in the CBD, other than to an existing patient base, Clive should buy Daniel out and employ a dentist of his choice. Since Clive will eventually wish to sell in about ten years' time, his practice will be worth considerably more if he buys Daniel out and offers the whole practice for sale in the future.

### Buying off a CBD boss

**T**eresa works for an older dentist in a CBD practice. She does \$450,000 of fees but has considerable ability and capacity to do more. Her boss, Thomas, is eccentric and untidy in his paperwork. However, he produces \$650,000 of fees per year, even though he under-charges.

Teresa should buy if the price is reasonable, have Thomas work for her part-time for a limited period and introduce a young dentist two to three days per week while doing more work herself.

### School mates' challenging future associateship

**T**im and Ellie were at dental school together about six years ago. Tim works in three practices which add up to five full days per week and he's keen to run his own practice. Ellie works in two other practices for a total of four and a half days per week. They have been frustrated trying to buy practices and decided to buy premises with appropriate zoning and set up a practice as associates. Each face tricky questions as to which element of their current work to give up so that their new venture will have a dental presence at least five days per week, even if they are only half days initially. They are yet to find that it's going to take a considerable time to build a dental presence in the new practice, so they each need to retain a significant portion of their existing work to pay the expenses while they build up

their new long-term practice. The days are long gone when dentists could simply squat and wait for patients to flood in. Tim and Ellie will build a practice at a glacial pace despite having a good website and investing in other marketing initiatives.

If they're prepared to put in a few years of investing their time and subsidising the new practice from their earnings elsewhere, they will achieve their goal.

### Old dental school friends click in future associateship

**T**ristan worked for a health fund but had built up an extensive list of patients who routinely asked for him and refused to be treated by other dentists. The health fund made the mistake of transferring him from a practice in the CBD to a suburban practice and cut off the patient base which was loyal to him.

Tristan was able to buy into an associateship with a classmate from dental school, buying out the older dental associateship in that practice. Many of Tristan's patients at the health fund tracked him down on the internet and made appointments. This, together with the fee base he purchased, means that Tristan is heavily booked and thriving.

### Rich kid - poor dentist

**J**ohnnie had rich parents who bought him an associateship and premises, but he had too little interest in dentistry and his work was below the standard of other high quality dentists in his area. As a result, patients have drifted. His associate has moved out to run his own practice free of the negative vibes coming from Johnnie.

Johnnie has his very expensive European luxury car parked in the practice car park and is oblivious to whether he appears too opulent to patients. Unfortunately, dentistry is a distraction to his lifestyle and his practice has acted as a benefit to other practices in the area who have picked up patients from him.

### Immigrant dentist with a tough path

**E**leanor is an immigrant dentist from South Africa. She does good work

but has very little money, having arrived with hardly anything except her clothes. She's still a little slow in her dentistry and needs to develop her skillset. She realises that her chairside manner needs to improve and is working on it. Her much older boss offered to sell her his practice but for Eleanor it was a step too soon. She is a hard worker and over time will build a solid fee base and reduce her and her husband's home loan. In time, she'll be able to buy a practice.

### Accountant's poor judgement leads to associateship disaster

**J**ulian had a long-term associate, Sam, who wanted to sell. Sam offered to sell his associateship to Julian at a realistic price. Julian's accountant advised him not to buy, saying something along the lines of "You're busy enough in your own surgery already, why do you want to look after another part of the practice?"

After a time, Sam lowered his price and subsequently advised Julian that he was about to sell to a foreign buyer, but he was offering Julian a last chance to step in and buy. Julian's accountant again advised him not to buy. As a consequence, Julian found himself with an associate whose social skills and attitudes quickly alienated the practice staff and began driving patients away.

In desperation, Julian sourced new premises and fitted them out at substantial expense. He then moved his practice away from his new associate and reflected upon the significant damage done to his practice in the meantime. He wished that he had ignored poor accounting advice, bought out Sam and then introduced a dentist of his own choosing to the practice.

### Lesson #1

**U**nless they have many dental clients, accountants are apt to give poor business advice concerning dental practice business decisions. Source your business advice carefully.

### Lesson #2

**D**on't let an incompatible dentist near your practice.

### Inability to step up

**A**my worked for a high-performing dentist. He wanted to sell and retire and despite having the inside running, Amy could not bring herself to step up and buy the practice. As a result, the practice was sold to a dentist who brought in his spouse and diverted all new patients to his and his spouse's surgeries, gradually squeezing Amy's presence in the practice from full-time to two and a half days per week.

#### The lesson

**D**entists who aren't able to step up to opportunity risk getting pushed aside.

#### Expensive premises mistake

**O**livia had a sound practice and worked four and a half days in her surgery, employing an assistant dentist for three days per week and a hygienist for two and a half days. Practice fees were about \$1,150,000. She was nearing the end of her second-last lease period and her landlord offered her the alternative of exercising her right for the final renewal for three years or buying the premises. His asking price was reasonable in relation to the rent. Unfortunately, Olivia took advice from a real estate agent who advised her not to buy the premises but rather to gear into several residential rental units in order to "get more financial leverage". She rejected the buy offer in respect of the premises and geared into the residential units, all of which turned out to have disappointing outcomes after purchase. Meanwhile, the dental premises were sold to an investor who realised that with the end of Olivia's lease approaching, he could demand a significantly higher rent. Olivia then found herself in a situation of having to choose between paying a much higher rent or sourcing new premises to buy or rent and undertaking a very expensive dental fit-out in order to house her practice. Eventually, she decided that in order to avoid the fit-out cost, she would pay a rent which was 50% more than she had been paying. She now regretted taking advice from a real estate agent.

Furthermore, as her rent was now well above market, when it eventually came time to sell her practice, the additional rent meant that she received a significantly lower price for the practice.

### Lesson #1

**D**entists frequently misunderstand the amount of fit-out cost buried in the floor and walls of their practice and the benefit of taking ownership of their own premises. This can lead to expensive misjudgements.

### Lesson #2

**D**ental premises are much better investments than residential rental units.

#### Buying and wrecking a great practice

**A** dentist with a substantial three-dentist plus hygienist practice in a large regional city was approaching retirement, decided to sell and offered his practice at valuation to a buyer who also purchased the premises. The buyer was asked whether they needed assistance with business strategy, practice benchmarking, etc, but made it known that he knew his own mind. Nor did he want a handover from the vendor. He was quite aggressive in his approach and the vendor was particularly happy not to have to work for him for a handover period, preferring to fine-tune his boat and get his fishing tackle out instead.

Within a short time, chairside assistants and reception staff were all seeking employment in other practices, as were the assistant dentist and hygienist. Within a year, the practice was down to a single dentist, the owner, working two surgeries and carrying the burden of significant loan repayments. Word had spread around the city that he was not a nice person and referrals to his practice had evaporated. A number of other dentists in surrounding practices were particularly happy, having shared in the windfall of patients changing practices and acquiring good staff when they had a vacancy.

### Lesson #1

**N**o amount of clinical skill will compensate for boorish and aggressive behaviour, nor will good staff tolerate it.

### Lesson #2

**T**he best staff leave first, because they are readily employable elsewhere.

### Lesson #3

**B**ad news travels faster than good news, and patient referrals can dry up surprisingly quickly.

#### Blowing up a good associateship

**H**enry, an ageing associate, and Michael, a dentist still in his prime, had practised together for many years and employed two other dentists. Henry, with Michael's agreement, offered to sell his associateship to Gregory, the more experienced of the employee dentists, at a fair price. Gregory indicated he would buy and everything went smoothly, but at the last moment he demanded that Henry reduce his price. Henry was too committed to retirement plans and caved in. Gregory stepped up to the associateship, Henry retired and a new employee dentist entered the practice.

Subsequently, Gregory started demanding of Michael that he allow him to manage the whole practice and sell him his interest in that part of the practice conducted by their employed assistant dentist.

Advice to Michael indicated that he would find the remainder of his practice worthless if he acceded to Gregory's demands. Not only would Gregory control the other dentists in the practice, he would also control the front desk and all new referrals to the practice. It was apparent that Gregory was getting advice from somebody with little understanding as to how practices worked, who simply believed that he could force his way through aggressive tactics.

Michael was also wary because of Gregory's treatment of Henry, who Michael had worked with and respected for many years. Michael refused a series of unreasonable demands from Gregory until ultimately Gregory demanded, through lawyers, a break-up of the associateship. That forced a negotiation. Acting on advice, Michael refused to move from the premises or to give up the practice name or telephone number, which he had used for many years. His position was that these elements were integral to his practice and if Gregory wished to move on, then it was up to Gregory to do his own marketing.

Gregory had made a rash decision to buy premises nearby; premises which required a lot of renovation and together with dental fit-out, meant a huge debt. Having

committed himself, he found himself being drawn towards his new premises by the inevitable consequences of the golden chains attached to the bank loans attached to his new premises and fit-out. He now found himself negotiating from a position of significant financial weakness. He and his lawyers were stared down.

As a result, Michael bought Gregory's interest in what had been their joint premises at valuation. Michael retained the business name, telephone number, the practice website and the majority of staff. Subsequently, new patient referrals continued to Michael's practice almost as though Gregory had never left. Gregory's new patient referrals were negligible for a considerable period of time and he found himself under huge financial pressure.

### Lesson #1

**B**e careful who you listen to when taking business strategy advice concerning a dental practice or dental associateship.

### Lesson #2

**D**on't commit yourself to expensive new premises and fit-out on the assumption that you will be able to force a suitable outcome in negotiations with your existing associate.

### Forget apartments, buy your dental premises

**T**revor worked for a dentist who had two practice locations. At a certain point, his employer found himself stretched financially and found that running practices in two locations created a lot more pressure on him. As a result, he sold the lesser of the two practices to Trevor, who was employed at that location. The particular premises were rented.

Subsequently, Trevor indicated to his adviser that he and his father were about to take a free trip to the Gold Coast as a developer was providing them with plane fares to look at some apartments he had for sale. He was advised to forget the Gold Coast apartments, as it followed such a regular cycle of boom and bust that overwhelmingly, investors buying apartments had come to regret their decision and found them virtually unsaleable on the secondary market.

He was advised that the key assets of a dental practitioner were his home, his practice, practice premises and super-annuation fund. In due course, Trevor acquired his own dental premises, had them fitted out in an attractive style and found his practice profitability increased markedly. Many years later, he is in a very healthy financial position. Meanwhile, there have been many tales of woe concerning those who have invested in Gold Coast real estate.

### The lesson

**F**or virtually any dentist, the best two property investments they can make are:

1. Their long-term home.
2. Their dental premises.

### Incompatible associateships

**C**harles was a high-end dentist who employed an assistant dentist, Sophie, plus an hygienist. In Charles's mind, Sophie and the hygienist existed to service those patients who were not in need of the high-end services he provided. Charles was a very good dentist, with fast hands and a high production rate. He produced about 65% of the fees of the practice, Sophie about 25% and the hygienist 10%.

Sophie was keen to buy in and Charles sold her an associateship which consisted of her fees and a pro rata share of the hygiene fees. Unfortunately they were incompatible and while Charles had imagined little change in the operation of the practice, which had been quite successful previously, Sophie exercised her right to involve herself intricately in its operation, to a point at which her consistent quibbling of even small decisions irritated Charles, who was more a big-picture person. His view was that he was there to concentrate on dentistry and preferred to delegate a significant amount of administrative detail. Sophie was naturally a micro-manager. Her regular queries and need for regular discussions were an irritating distraction to Charles and also irritated practice staff. Charles's defensive mechanism was to speak to her as little as possible, which tended to make matters worse. In truth both were at fault and the relationship grew ever more strained.

Sophie made the error of consulting a solicitor, who immediately wrote a letter to Charles which suggested he was trampling on Sophie's rights and which broke down any residual trust. The solicitor's letter was far too aggressive and Charles could not resist the impulse to write back to Sophie's solicitor in equally offensive terms.

Their accountants and advisers counselled a cooling-off period, but Sophie's lawyer, seeing the opportunity to earn significant fees, poo-pooed this suggestion, instead proposing that the matter go off to a legal mediation. The legal mediator he had in mind had mediated quite a few family law property settlements, but had never dealt with a dentist associateship dispute. Charles's advisers told him to sit tight and resist the temptation to engage a lawyer.

In due course Sophie's lawyer found himself firing blank bullets, as Charles now refused to engage in dialogue. In due course, Charles's advisers pointed out to Sophie's lawyer that despite all the huffing and puffing, the only possible solutions were either that Sophie would sell back her associateship to Charles or, alternatively, she could source her own premises elsewhere and leave, taking with her the records of those patients she had treated. Eventually Sophie sold her associateship back to Charles.

### The lesson

**I**t is unusual for lawyers to solve associateship disputes, but they can inflame a situation further. Suggestions of court action tend to be hollow because judges don't see much public interest in two dentists squabbling. Such matters tend to keep falling to the bottom of court lists.

### The practice manager who almost destroyed a practice

**R**oger was an older dentist who had owned a practice for many years and employed Susan, who was much younger but quite capable, as a full-time dentist. A third older dentist worked part-time.

Roger had also employed as practice manager Sylvie, who had started as his

chairside assistant and graduated to the position of manager. Sylvie had proved to be extremely manipulative and managed to arrange the practice in such a way that she herself did little actual work. As a result, the non-professional staff cost in the practice was far too high relative to fees and practice benchmarks. Rather than being a fixer, Sylvie had become a cost centre.

Practice owner Roger was a nice person who had a few health issues. He had been reluctant to confront Sylvie, who could become quite aggressive. Roger indicated to Susan that he would like her to purchase into the practice. Susan, who had the experience of being brushed aside by Sylvie on too many occasions when she had made reasonable requests, felt that Sylvie had too much dominance over Roger and she was reluctant to buy into the practice while Sylvie was in a managerial position. Eventually Roger, urged on by his wife, took advice. They were advised that:

1. The non professional staff component of the practice as a percentage of gross fees was far above average and in fact, the difference between the cost in Roger's practice and the average cost percentage approximately matched Sylvie's salary and superannuation package!
2. There were a myriad of dental practices of approximately similar size which functioned efficiently without a practice manager; the owners themselves administered these practices, sometimes with the assistance of a part-time bookkeeper, while some did the books themselves; and
3. In some practices a receptionist had the courtesy title of practice manager, but functioned as a receptionist.

It became obvious that for the practice to get out of its rut and for Susan to buy in, Sylvie had to go. In due course, Sylvie was made redundant without replacement. Susan bought an associateship from Roger and, as per their associateship agreement, they shared the management of the practice. They also found that the other staff of the practice responded enthusiastically and some patients, who had been treated quite rudely by Sylvie, mentioned to staff how pleased they were she was no longer present.

### The lesson

**T**oo often, practice managers are profit and practice destroyers. In the vast majority of practices, the dental owners make all of the actual management decisions, perhaps with a little assistance from part-time bookkeepers and external advisers.

### Persistence pays off

**W**illie had done well at dental school and was good enough to be recommended to the owner of a good practice by his mentor in dental school.

He took on employment in the practice and continued to develop his clinical skills, producing a good income worked out on a percentage base. However, the owner of the practice was many years away from retirement and not prepared to sell an associateship.

At seven years out of dental school, Willie started seriously looking for a practice to buy, tracking down older dentists and politely presenting himself as a dentist who could look after their patients in a manner they would wish post their retirement.

He found a dentist with a four-chair practice, of which three chairs were fully utilised and the other partially utilised. Apart from the owner, there were a combination of part-time dentists and hygienists in the practice, none of whom was a likely buyer, but a couple of which produced good fees and had a sound local following.

The owner of the practice, who was beginning to contemplate retirement, had not yet made up their mind about passing that personal Rubicon.

After a period of polite negotiation and discussion between Willie and the practice owner and between their respective advisers, a deal began to take shape, but the practice owner eventually decided they were not yet able to sell. Willie felt hugely disappointed, but his adviser told him to:

1. Keep on looking for an opportunity to buy a practice; and
2. Be polite to the owner of the practice who had pulled out of the deal at the last moment and ask them politely if you could be considered with a first offer if they changed their mind.

Willie was contemplating purchasing a significantly inferior practice when his financial adviser received a telephone call from the previous practice owner's accountant, indicating that they now wanted to retire and asking whether Willie was still looking for a practice to buy. A deal was done and Willie is now the owner and lead dentist in a sound, well-established four-operatory practice.

### The lesson

Persistence and politeness pays off.

### An ignorant accountant cuts off an opportunity

**T**ony had a good practice with two full-time assistant dentists, but he had personal health issues. His personal health concerns eventually forced him to contemplate selling the practice well before normal retirement age. The practice was professionally valued to market and Tony offered it to the senior of his assistant dentists, Jimmy, who had previously expressed an interest. Jimmy took the financials and the valuation to his accountant.

The accountant advised Jimmy that the practice was only worth a fraction of the valuation and for some reason, his client believed him without checking further. In actual fact, practices of similar size, profitability and cost base and located in similar suburbs, had been selling readily for three times the figure the accountant advised.

Jillian, the other assistant dentist, recognised an opportunity and asked Tony whether she could buy the practice. Tony sold the practice to her and subsequently she did well. Jimmy will come to regret listening to an accountant with zero knowledge of dental practices.

### The lesson

**I**n every profession and every industry there are a few accountants and advisers with a lot of experience of dealing with the industry or profession concerned and who have a good idea as to practice value. There are a multitude of other accountants who claim to be business advisers but whose only experience of dentistry is an

occasional visit to have their teeth drilled. Many of these accountants give advice which is dangerously wrong.

### Accountant turns buyer off

**B**enedict had previously sold a practice in another suburb and he moved to a suburb outside the agreed exclusion distance to establish a new practice. He found the search for a suitable premises a little bit more difficult than he'd imagined and ended up buying a building in a suburb with a working class population, albeit only a few kilometres away from suburbs with a high socioeconomic demographic.

He fitted out his premises to a glamorous standard which was out of keeping with his location. He smugly thought that many patients would follow him from his old location, but ultimately was disappointed. However, he heavily promoted the new practice with fancy leaflet drops in the surrounding suburbs, but had limited success.

Word was already getting around that those who had an appointment with him were subjected to fairly aggressive selling tactics for top-end dental options. It took several years for Benedict to work out that he was unlikely to repeat the success he'd had elsewhere, albeit that his practice was profitable if one ignored the true economic rent of the premises. Realising that he had little possibility of significantly improving his financial outcomes, Benedict decided it was time to sell his practice and move on once more.

He confidently offered it to the most senior of his two assistant dentists, who consulted the author. Benedict's accountant jumped into the negotiations and pushed heavily for a sale, claiming the practice was a magnificent purchase with huge potential. However, the figures including the required rent on the premises suggested that at the price offered, it was a very poor purchase option and pressure from Benedict's accountant merely made her suspicious. The assistant dentist, Suzanna, despite being hard-sold by Benedict and his accountant, decided on advice not to purchase but instead acquired premises in a far better location about 5km away. Had they not pushed so hard, she would have been content to

remain employed in the practice indefinitely. Her set-up was acceptable because she had no exclusion requirements in her employment contract, and indeed Benedict didn't believe that a dentist employed by him would take the initiative to establish themselves elsewhere.

The new location was surrounded by a significantly better socioeconomic population than was Benedict's practice. Suzanna had scrupulously obeyed the rules and not taken any patient lists with her when she left Benedict's employment, but quickly found that many patients had tracked her down, having preferred her to treat them rather than Benedict, who had turned almost every appointment into a hard sell. Suzanna found herself treating many of the patients who had previously been treated by her at Benedict's practice, and those patients often referred their friends who had been Benedict's patients! Now about eight years later, Suzanna has a good two-dentist practice. Her premises have appreciated significantly in value because of their location and she and her spouse have upgraded their home.

After Suzanna left, Benedict kept trying to sell his practice and eventually sold to

an interstate dentist who subsequently found, to his horror, that after purchase, the fees were way below those disclosed in the previous year's financials and who was repeatedly told by remaining patients of the negative impact Benedict had had on them.

The rent was far too high in relation to the fees of the practice housed within. Furthermore, the new owner found that promoting the practice was largely a waste of money because it had acquired a bad reputation in the area. Most people who received advertising equated it with the previous reputation of the practice. After struggling for a couple of years, the practice was closed.

### Lesson #1

**P**ersonal hubris does not make a good practice or a good investment.

### Lesson #2

**A**s well as the normal accounting due diligence, it is vital when buying a practice to check the recent patient book and practice fee bankings.

### About the author

*Graham Middleton personally has been advising dentists on strategic, practice management, valuation and conflict resolution processes for 27 years, the last 20 as a founding partner and director of Synstrat Management Pty Ltd and Synstrat Accounting Pty Ltd. He was once a regular army officer, and later Director Human Resources Manager, Attorney General's Department of Victoria. He is considered an expert on dental practice valuation and practice performance benchmarking. He has spent many years advising dentists in respect of their business and financial strategy and measuring their practice and financial performance. He is the author of Synstrat Dental Stories, the Synstrat Guide to Practice Management, 50 Rules for Success as a Dentist and Buying & Selling General & Specialist Dental Practices. He is a long-term contributor to the Australasian Dental Practice magazine. The Synstrat Group is an independent data-based organisation providing management, benchmarking, valuation, financial and accounting services to the dental profession. Synstrat Management Pty Ltd is a Licensed financial services company. Both Synstrat companies are owned by the same directors who work within the Synstrat Group. For more info, call (03) 9843-7777, Fax: (03) 9843-7799, email dental@synstrat.com.au or see www.synstrat.com.au.*

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