

# Buying dental practices - Pitfalls and successes

By Graham Middleton, BA, MBA



*“Having a second dentist wanting to buy your practice can relieve you from being brow beaten into accepting a price payable far below market value...”*

**J**ulie had worked in a great practice in another state but she'd decided to move states because of her partners' employment. Despite being a skilled clinician with appropriate additional training and well-developed expertise in a range of advanced dental techniques, employment in her new location was hard to come by. She accepted work in a practice whose proprietor had to take time off for health reasons. The practice was above a medical centre and it had high rental relative to fees.

Maxine, the proprietor, anticipated coming back to work and had indicated to the receptionist that she was to keep her own patients on hold for bookings. Patients booked to Julie represented Maxine's overflow and those who had been seen by the previous assistant dentist.

As time went on, it was apparent that Maxine was not likely to return to work. Her patients began to drift away. At this point, she offered to sell to Julie but her price assumed that the practice would have sufficient patients for two dentists working full time whereas so much time had elapsed that the practice was struggling to be a one-dentist practice. This was apparent to Julie working inside the practice.

The cost basis of the practice, particularly the rent, was far too high for the diminished patient pool. Julie was advised that the practice would be a very poor choice. She managed to secure work elsewhere while she looked at other opportunities.

About this time, a busy country dental practice which had had a sale on foot, advised that the buyer had pulled out for an unknown reason and asked what they should do. The practice owner was asked whether we could introduce another client to them knowing that we had previously valued the practice. Care was taken to declare the client relationship with both parties. Julie visited the practice, bonded with the vendor and purchased the practice at valuation. A year later, the practice is running smoothly; is busy and growing. No commission was involved. Clients were charged for time spent in providing services to them to bring about the transaction.

## The lesson

**D**on't buy a bad practice. No dentist should be that desperate.

## Sion's story

**S**ion was looking for a practice and knocked on many doors. He eventually found a 4-surgery practice, well located with sound fees. A period of negotiation occurred but the owner eventually advised that they were not ready to sell. We advised Sion not to burn his bridges. Rather than complain that the owner had pulled out at the last minute after much due diligence, the owner was asked politely whether they would keep Sion in

mind if they decided to sell and if Sion was still looking for a practice. We spoke to the owners' accountant and made a similar request.

Sion began looking for another practice for sale and found one. However, it was far inferior to the first one. Fortunately, the first dentists' accountant rang up and asked if Sion was still interested. It was timely as Sion had been close to purchasing the other practice. Sion is now running a first rate profitable practice with excellent fit-out in a good location. His dental future is secure.

### The lesson

Don't burn bridges!

### Michael's story

**M**ichael sought advice. He was in a partnership with low profit and very high rent relative to fees. His partner wanted to move to take up an opportunity in a regional city but Michael wondered if he bought out his partner if it would make his problem worse. In advising him, we noticed that the premises that had very high rent were due for a lease renewal and after discussions, realised that the landlord had several vacant spaces near the practice. That spelled bargaining power. The practice also had significant unused space. Michael was advised to hire a real estate negotiator. As a result, the rent per square metre was substantially reduced and the surplus space handed back to the landlord. Michael took a long-term lease and while the rent was still expensive by dental practice standards, it was far below what it was.

Michael bought out his partner and was advised to increase fees across the practice to market rate and to rearrange the dental book to steer the best patients to his own surgery.

Michael's profit has dramatically increased. He is now fully funding superannuation payments and his family financial situation has changed dramatically. He is far more confident in his decision making, his presentation to patients and concerning his long term future.

### The lesson

**S**ometimes there is a very good practice inside one which at initial perusal of financials appears to be a dog.

### Yusof's stitch up

**Y**usof bought a practice off a couple of well-known wheeler-dealers who had only owned it for a very short period.

Prior to the wheeler-dealers, it had been owned by a well thought of dentist who had employed an experienced assistant dentist. The wheeler-dealers had negotiated to purchase at a good price (to them), made a few cosmetic changes and resold to Yusof at a much higher price, having persuaded him of the practice's great potential.

Soon after the purchase, his experienced assistant dentist left and the practice then had no dentists with a lengthy relationship with any of his patients. The fee base fell to about half that of its peak. Yusof had had inadequate advice prior to the purchase and had no basis for legal recourse.

Harsh as it may seem, Yusof was advised that he had to forget what had been represented to him and concentrate his and his staff's efforts, particularly his receptionist, on rebuilding the practice by:

1. Ensuring that its physical presentation was as good as they could make it by utilising an interior decorator; and
2. Concentrating on the personal relationships with patients, ranging from the meet and greet at the front desk through to the way Yusof and an assistant dentist greeted patients and their chairside manners. The mantra was that every patient had to have a good experience.

Subsequently, the practice has passed rock bottom and is slowly rebuilding. Yusof is hundreds of thousands of dollars down in his original purchase but he is facing up realistically to the challenge. In time, it will rebuild to a good practice.

### The lesson

**Y**usof received very poor advice when purchasing. The accountant who advised him claimed to have had significant experience working with dentists but did not recognise the obvious pitfalls or ask enough relevant questions and implicitly endorsed a purchase at a price well above what the practice was worth. Yusof received good advice too late to save him from being "stitched up" but is now on a sound long-term practice recovery path. He can do nothing about the fact that he paid \$500,000 more than the practice was worth, but he can control how he conducts the practice, now and in the future.

### June buys strategically

**F**ortunately, June, who had been looking for a practice, was able to be connected with a dentist we knew who was selling her practice. The vendor and her accountant set a relatively realistic price but the practice had been growing steadily. It was well situated in modern premises and was in an area of strong growth. We advised June that, whilst she appeared to be paying perhaps 10-15% above value, in a couple of years' time that would appear to have been a sound purchase.

While practices in growth corridors won't realise their full potential for ten or more years as many new homeowners have been rendered cash poor by their acquisitions, in time, the demand will grow strongly. However, in June's case, there are pockets of long-established housing within the practices catchment area sufficient to provide reasonable short-term growth. June was also able to purchase the premises with a high quality fit-out of only 3-4 years ago and can look forward to building a practice in secure premises long term. Her future dental career is secure.

### The lesson

1. It can be a sound strategy to buy above market value but care needs to be taken;
2. However, be wary of practice brokers.

In some cases, their motivation is to achieve quick sales of often inferior practices to earn a quick commission and their advice can be tainted. Many of the practices they have listed are dogs. In reality, most of the dentists that we know purchased practices off somebody that they knew previously and nearly all of the best practices transfer in that manner.

In June's case no broker was involved and the practice came to her via her relationship with her Synstrat advisers and their relationship with a dentist offering a practice for sale. No commission was paid, only charges for time spent.

### Two buyers

**G**uiseppe - "Joe" to his mates - had been the long term owner of a suburban dental practice. Joe worked one surgery and an assistant dentist the other; both full time. The premises had been built by Joe's father, a builder and contained a spare surgery and space for a 4th.

Joe's assistant dentist, Sunil, had asked to buy the practice but offered a ridiculously low price. Joe rejected the offer but granted his assistant a last right of refusal. Meanwhile, we were able to introduce another dentist who was looking to pay a market price and made a firm offer. In keeping with his word, Joe advised Sunil of the price and she asked for time to reconsider, even though that price was more than twice the price she previously said that she was prepared to pay.

Sunil's accountant jumped up and down and demanded to know how the price was arrived at. He was told "It's simple, that is the price another buyer is prepared to pay". Unfortunately the second buyer who had made a genuine offer was unexpectedly pushed aside, given that Sunil's initial offer had been so far below market price as to suggest that she was not prepared to buy at market. It seems that that was a try on gambit.

### The lesson

To get a fair price it is sometimes necessary to have multiple buyers.

### Multiple buyers - Take two

Rex employed two other dentists, one of whom was "Sunny", who had worked in a practice for over ten years and the other, Toni, for three years. Rex had health issues forcing him to consider early retirement and eventually advised he had to sell. Sunny had always appeared to be the heir apparent. The practice was a sound three-dentist practice in well-fitted-out premises with a long-term lease at reasonable rent. It was clearly an attractive purchase. However, when advised of a fair market price, Sunny claimed to have had advice from his accountant that the practice was only worth about one third of that amount. That advice was plainly absurd. Sunny was told to go out and check prices with brokers and "get real if he wanted to buy the practice". Sunny kept quoting his accountant who was unknown in dental circles and stalled negotiations. At this point, Toni stepped forward and announced that he was prepared to buy the practice.

Rex sealed the deal with Toni. Sunny will come to realise that his accountant cost him the opportunity to buy the best dental practice he was ever likely to be able to acquire.

### The lesson

Most accountants spend their time completing tax returns and very few have significant, if any, knowledge of dental practices. Informed advice is critical.

Having a second dentist wanting to buy the practice relieved Rex from being brow beaten into accepting a price payable far below market value.

### Freddy V Thomas

Freddy is employed in a practice where he does 90% of the treatment. The owner, Thomas, who has a second practice in another suburb, does the other 10%. The practice is housed in an aging building with a tired fit-out, but the building is on a site which has leapt in value because of the attractiveness of the suburb.

Thomas wants to redevelop the site within the next year or two and he proposed to sell Freddy the practice. However, Thomas obtained advice concerning the practice value from an accountant who purports to know a lot about dental practice. That accountant did not take account of the fact that no long-term lease was available and the premises and its fit-out were very tired. The reality is that if Freddy buys, he faces a major expense in fitting out premises elsewhere and relocating the practice. The accountant who valued for Thomas valued the practice at a similar figure to what practices in well-fitted-out modern premises with long-term leases were fetching.

As a result, Thomas was asking a price that Freddy will not pay because Freddy knows that if he buys the practice, he is going to have to pay for a substantial fit-out and relocation. In reality, the practice is worth possibly half what Thomas is asking; at most.

Unless Thomas accepts reality and sells at a price which will allow Freddy to buy, then fit our premises elsewhere and move the practice, he is stuck not being able to redevelop the site. The possible outcomes do not look good being:

- Freddy will get sick of waiting and negotiating and take up dental employment elsewhere; or
- Buy a practice elsewhere; or
- Set-up his own practice.

### The lessons

1. Be careful who you take practice valuation advice from; and
2. A win/win situation will require a practice being offered to Freddy at a price which recognises that he is going to have to pay a substantial amount to re-establish the practice in fitted-out premises elsewhere.

### Disclaimer

*While each of the examples given in this article are based on actual events, names and some details have been altered. Any association with actual dentists is therefore accidental.*

### About the author

*Graham Middleton personally has been advising dentists on strategic, practice management, valuation and conflict resolution processes for 29 years, the last 22 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.*