

My Dental

CPA

Purchasing a Dental Practice

This is not intended to be an all-inclusive checklist of everything you need to do when purchasing a dental practice. It is designed to guide you through the items we recommend when working with clients. We will defer to attorneys on a lot of the information that needs to be in the letter of intent (LOI) or the purchase agreement.

Reasons to Purchase vs. Creating a Startup

- Immediate cash flow.
- Built-in patient base that you can continue to grow.
 - *The practice broker should walk you through the best transition strategy, which should involve the selling dentist writing a letter to introduce you to the patient base.*
- Less risk, although I have never seen a startup not succeed.
- Staff in place
 - *I say this, but it is not uncommon to see some staff turnover after a purchase.*
- Established procedures.

What You Should Have Before Starting the Purchase

- Relationship with a CPA.
 - *We recommend developing these relationships shortly after or during dental school.*
 - ♦ Dental chat rooms, including Facebook groups, and referrals from dental friends are very helpful.
 - *While it's very helpful for the CPA to have a knowledge of dental practices, they do not have to be dental-specific. It is extremely important that they are a CPA with a heavy service business focus.*

First Steps: Financial, Legal, and Business Tasks

Financial

Develop a relationship with a dental broker who works a lot with practice purchases.

- Most of the time, dental brokers can provide 100% financing and initial operating capital needed for the purchase of the practice. Three banks that have very strong dental practice clients are:
 - *Provide*
 - *Huntington*
 - *Bank of America*

- ♦ I recommend developing this relationship now, even though much of the information you may need to make a final decision will not be available until you find a practice to purchase.
- When deciding which bank to choose, compare the following:
 - *Interest Rates*
 - *Term of loan (5 to 15 years)*
 - *Amount of operating capital that will be furnished*
 - *Period of interest only while you adjust to the new practice*
 - *Prepayment penalty*

Legal

Find a dental attorney to represent you.

- It is very important that you have an attorney who specializes in dentistry and will be able to write a buy/sell agreement that incorporates the nuances of buying a dental practice. The dental attorney, along with your CPA and your broker (if you use one), will help guide you through the process.

Business

Set up an LLC or PLLC. If you already have an entity (Corp or LLC) taxed as an S-corporation, you can use the existing entity.

- At this point, have your attorney set up an LLC or PLLC, depending on the state you live in, with the Secretary of State.
- Apply for a Federal Employer Identification Number (FEIN) for the new entity.
- Have your attorney or CPA make an S-Election.

Second Step: Shopping for a Practice

Now that you can get financing and have a relationship with an attorney, it is time to start shopping for a practice.

- When looking at practices, remember that the seller is often the founder of the practice and may see the practice as an extension of themselves. It is important to be respectful of that.
- When shopping, it is important to consider if your current employer knows that you are looking for a practice. If they do not know, you may limit your search to working with a broker, your CPA, or your attorney.
 - **Brokers:** *Reaching out to dental brokers is often the best way to find practices for sale. They will have already done the due diligence on the practice and will have a nicely assembled package for you to review with your CPA. They will also help you communicate with the seller.*
 - **Your professional team:** *Do not hesitate to reach out to your CPA and attorney to see if they know of practices for sale. We review practices regularly for potential purchasers and typically know of at least a couple for sale.*
 - **Dental supply representative:** *Your dental supply representative is in dental offices every day and will often know about practices for sale before others do. I think most dentists do not utilize all the services provided by a good dental supply professional.*

Practice Considerations

- Location and area demographics
 - *This is probably the most important consideration, since it will determine the area you will live in.*

- Oftentimes, rural practices have higher profits with less revenue than metropolitan practices.
- Ask yourself, “Is the area a growing area that will allow me to achieve the goals of the practice?”
- Revenue size
 - Lots of clients prefer practices in the \$1M to \$1.2M range, essentially purchasing a full practice.
 - I prefer practices in the \$600k to \$800k range in a good area with a potential for growth. You have a good base of a practice but can add value by growing the revenue and patient base.
- Payor Mix
 - Fee for service is great, and you get paid more for what you do, although most practices are in network with at least some insurance companies.
- Employees
 - It is helpful to keep most of the employees for at least for a year, but many times the employees are older, are related to the selling doctor, or have strong connections with the selling doctor. I think this is important to look into before doing due diligence on a practice you are considering.

Third Step: Due Diligence

Your CPA should be heavily involved in the due diligence phase. It is not uncommon for me to look at four or more practices for a dentist looking to purchase—do not rush or settle.

- Minimum financial data we would like to see from each practice:
 - 3 years of business tax returns
 - ♦ Look at top line revenue trend over this period.
 - Flat or slight growth is good.
 - If it spikes up or down, make sure you understand the reason. Some dentists will perform unnecessary dentistry before the sale to drive up the revenue numbers.
 - 3 years of business financials
 - Collection by procedure
 - Collections by provider
 - Payor mix
 - Receivables report to determine collections
- Have an equipment representative evaluate the equipment.
- Determine employee pay and length of service.
- Meet with the seller and make sure you are like-minded.
- Determine if the office is paperless.
- There are numerous items and other checklists out there that are more complete. One is "Practice Success Series of Dentists—Acquiring A Dental Practice.”

Fourth Step: Make an Offer

If you’ve found a practice worth purchasing, it’s time to work out an offer.

- Price—Working with your CPA, business broker, and attorney, determine the price you would be willing to pay.
- Letter of Intent—This is your formal offer to the seller of the practice and will contain most of the terms of the sales.

- *2 types of transactions*
 - ♦ **Stock/Membership Units**—Here you would purchase the stock of the existing entity. We do not recommend this type of transaction for most purchasers, although there have been occasions where we used this type because of very favorable payor schedules or lease terms. This type is also more common when purchasing a practice from a related party, like a father, since tax law can make an asset purchase more difficult in such a case.
 - ♦ **Asset Purchase**—This is 90%+ of all the transactions we are involved with. You purchase the assets of the practice. Typically, the assets are divided into 2 primary categories:
 - *Hard assets, such as equipment and supplies. You want as much of the purchase price allocated to these assets as possible.*
 - *Goodwill and intangible assets. These assets must be amortized (expensed) over a 15-year period on a straight-line basis. We try to allocate less of the purchase price to goodwill, but it is typically around 80% of the purchase price.*
- *I defer to your attorney what should be in the letter of intent but do like to see the following, in addition to the obvious:*
 - ♦ Asset allocation (above)
 - ♦ Terms of continued employment for the seller
 - ♦ Whether or not receivables are being purchased
- Note that this is a negotiation, and so it may go back and forth a couple of times before you reach a final agreement.
- One consideration is whether to purchase accounts receivable. Typically, it takes time for the new practice to be set up with insurance companies and you will often bill under the previous practice. Keeping track of receivables if they are not purchased can be burdensome. We suggest having an outside party help with this process and if it is an insurance-based practice, helping negotiate better reimbursements.

Fifth Step: The Agreement

If you have an agreement, it's time to get busy.

- Your attorney should start working on an Asset Purchase Agreement (APA) based on the terms of the LOI.
- Provide financials to the bank to start underwriting.
- Coordinate with the seller about communication with patients and employees.
 - *Some sellers may not want anyone to know until the final agreement is signed.*
 - *Have a patient letter ready to go out to existing patients.*
- Contract with someone who can help negotiate with PPOs, if needed, and with credentialing.
- Contact your insurance agent about the appropriate insurance needs.
 - *You will probably need life insurance as a requirement of the loan.*

Congratulations, You Are Now a Practice Owner! Let the Fun Begin.

I am a big advocate of not making any big changes when you first purchase a business. You want it to feel the same to the staff and patients.

Now you are a business owner before you are a dentist. It is time to think like a business owner (Be a Business Owner First).

- Understand where you want to be in three years and start making decisions that will take you there. There is a time you have to make decisions for today but always be thinking, “How does this work with my three-year plan?”
- Be an active business owner, not a passive one. Drive your business toward where you want it to go with your vision.