Buying or selling a dental practice? Chances are you will only go through each once in a lifetime. Those who embark on a scratch start-up may only go through the selling phase. It is strange how many “large ticket” items we may buy and sell through the years, such as cars, boats, property, and homes. However, it is likely a dentist will buy and sell a dental practice only once. This why, from the doctor’s perspective, so much ambiguity exists in the process.

The intention of this article is not to completely educate on the process, but rather clarify how the process may progress, and dispel some misconceptions regarding transitions.

It seems whenever our group is requested to become involved in a dental practice valuation and/or transition, the dentist will invariably ask, “How do you come up with the value of my practice?” This is a very fair question, which usually elicits the popular comment, “I have always heard it is based on X% of my collections.” This is what should be addressed.

While collections are an important ingredient in determining value, it cannot be the only measure. Let’s look at the following scenario:

Two dentists request a valuation. Practice “A” has gross collections of $500,000 with a net to the dentist after overhead and before taxes of $235,000. Practice “B” has collections of $900,000 and a net to the doctor after overhead and before taxes of $200,000. If we used only the popular theory that a practice is worth X% of collections, then the practice “B” valuation would be considerably more than that of practice “A.” However, practice “A” generates more personal income for the dentist.

This usually makes sense to the doctor, and the next question may be, “What drives the value of my practice?” There are four questions to ask that go into determining the value. They are:

1. “Where is the practice located?” It seems the majority of recent graduates want to live in, or close to, large metropolitan areas. They may have a significant other who has a profession that requires him or her to live in or near a larger city. This is not to suggest a dental practice in a small town is “unsellable,” but rather, to say it may take more time. The good news for those in smaller towns is we are finding there is an increased interest in them.

2. “How much money do you make?” A practitioner asks this because it tells him and his/her team of advisors what they can afford to pay for the practice. They need to know how much is left over after the overhead and debt service is paid.

3. “What is transferrable to me?” If the seller performs a large amount of endo procedures and the buyer dislikes and does not wish to do any endo, that production is not transferable to the buyer. The same may hold true for oral surgery, ortho/Invisalign, cosmetic procedures, etc.

4. “What is my secondary cost of purchase?” If the buying doctor is purchasing a “fixer-upper,” how much money is it going to take to get the practice up to standard?

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What else is considered in the valuation process?

**Goodwill**

We measure practice goodwill in two categories based on the practice history of collections and cash flow. It is important to address goodwill accurately and fairly, as it is the primary determining factor in what a buyer can afford to pay you for your practice once he/she has paid the overhead and debt service, yet still make a decent living.

**Tangible Assets**

This is the assigned value of your dental equipment, office equipment, and inventory of dental supplies.

Once our group has visited the practice and applied the business formula of “Add back and removal,” we are then able to assign a value ratio to the final numbers. These ratios are based upon demand for the practice’s geographical location and the condition of the facility and its equipment. If it is expected a buyer will have to invest a large amount of money to improve the practice soon, the ratio used will be smaller. Conversely, where a practice is in a high-demand area in an updated building with good/moderate equipment, the ratio used would be larger.

A word of caution for the seller: do not rush out, enter into a complete practice remodel, and purchase new equipment if you are planning to transition in the next year or two. Because you spend $100,000 on a new piece of equipment does not necessarily mean the value of your practice increases proportionally. Please speak not only to your accountant about this, but also a transition specialist before undertaking any large capital investments. If an investment in your practice provides added tax benefits and will increase the sale value, consider contacting your Burkhart Account Manager and Equipment Specialist. They can help lay out a long-term plan of your equipment needs. It would be wise to plan far enough ahead so you are able to recapture your expenditure before transitioning. Keep in mind, it is not uncommon for us to receive an offer from a buyer, less a portion of the cost needed to replace some older equipment or to purchase equipment, such as digital x-ray (an example of secondary cost of purchase).

Two other things you may or may not sell in your transition are the facility which houses the practice (should you own it) and the accounts receivables.

Whether you are contemplating having an associate who will become an eventual partner or a full-scale transition within the next few years, please consider contacting a transition specialist for a practice overview. In short, what this will provide are some options to consider in getting your practice in a “healthy” position when the time comes. If you are planning an associate to eventually buy-in/out, a transition specialist can help with this, as well.

When consulting with clients in an overview, we may suggest to them that if they can wait a year or two to implement some changes, these changes will have a positive impact, not only on short-term collections and cash flow, but also on the future value of their practice.

Two common responses we hear from clients upon completion of the overview are, “That makes a lot of sense. I can implement those recommendations and concepts easily,” and, “That makes a lot of sense, but I do not want to wait to sell, regardless of how it affects the value of my practice.”

Either way, the doctor has all the information to make the choice personally, and proceed as he/she sees fit.

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