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Top Pitfalls to Avoid When Purchasing a Dental Practice

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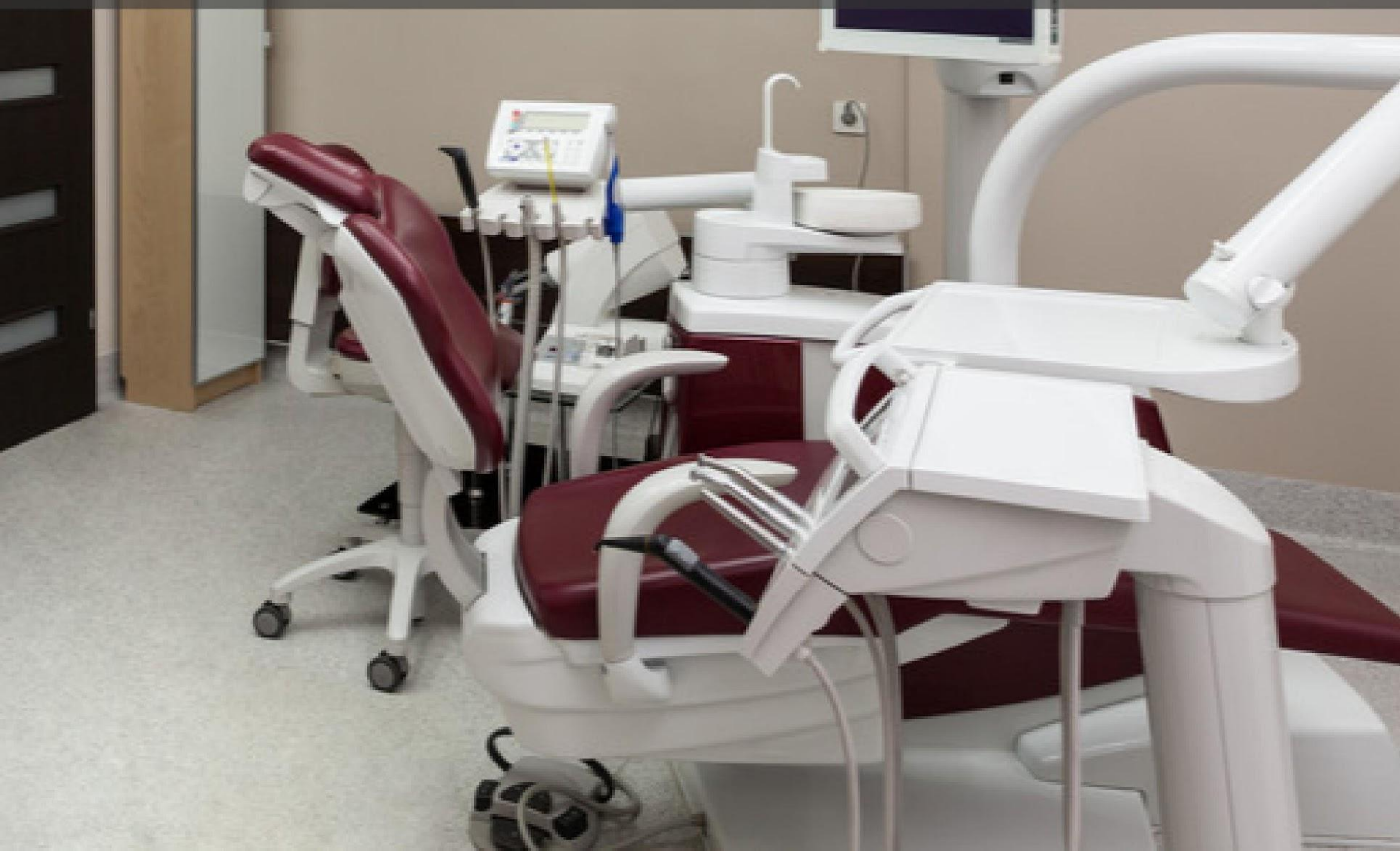

Building a dental practice from scratch requires a lot of hard work and it can take months or even years until you see a profit. Furthermore, existing practices that want to expand their market or market share often find that acquiring new patients organically can be extremely time-consuming and expensive.

On the other hand, while buying an existing practice is generally more expensive up front, you will most often be buying the existing customer base and can usually expect a cash flow from day one. For these reasons and more, buying an existing dental practice is often a better option.

That said, it is not uncommon for those who are new to the experience to purchase an existing dental practice and then realize, several months down the line, that they paid too much or made certain critical errors during the purchasing process. To prevent this from happening to you, here is a list of several pitfalls to avoid when purchasing a dental practice:

Not Drafting a Comprehensive Purchase Agreement

After negotiating the purchases of your dental practice, you need to reduce everything that you and the seller have agreed upon to writing in the form of a comprehensive purchase agreement.

A purchase agreement is a legally binding contract that facilitates the sale of a business from one party to another.

Your purchase agreement must list all of the terms that you and the seller have agreed upon and everything that is specifically included (or excluded) in the purchase of the practice.

A purchase agreement is the most important document you will need to prepare when purchasing a dental practice. Every comprehensive purchase agreement will contain the following clauses:

- **Goodwill** - goodwill is the term used to describe the intangible aspects of the practice that go into making it a recognized and successful business (its reputation, patient base, location, etc.). Goodwill should be assigned a dollar value and included in the purchase agreement.

- **Contingencies** - your purchase agreement must provide you with a way out of the contract if certain contingencies, such as entering into a satisfactory lease with the landlord or obtaining a loan for the purchase, are not met.

- **Non-compete** - a buyer who is purchasing the assets of a successful practice will not want the seller to start a competing practice after closing. Therefore, the buyer must ensure that the agreement contains a clause stating that the seller agrees not to compete as the owner, director, shareholder, partner, employee, consultant, or otherwise with the buyer in a specific territory for a specified period of time.

- **Confidentiality and Non-disclosure** - the purchaser may be asked to sign a document stating that sensitive information shared about the practice during the purchasing process will be kept confidential.

- **Representations and Warranties** - your purchase agreement must include a declaration that certain statements made about the practice by the seller regarding issues, such as the practice's income and expenses and whether or not there have been any criminal, civil, or regulatory claims against the practice, are completely true and correct.

- **Defects** - This clause must outline the rights and obligations of the parties with regard to defects in services that have already been provided. In other words, who will be responsible for correcting defective dentistry?

Not Incorporating Your Practice

There are many good reasons to incorporate your dental practice, such as tax flexibility and professional credibility. But, perhaps the most important reason to incorporate when purchasing an existing practice is personal asset protection. While incorporating will add extra costs and complexities to the purchasing process, it will also mitigate your overall exposure to lawsuits arising out of the purchase of the practice.

If you purchase the practice as a sole proprietor and someone brings a successful lawsuit against the practice, your personal assets could be at risk. In the worst-case scenario, you could lose everything.

But, if your practice is structured as a corporation or LLC, and properly managed, you will have additional protection to ensure that your personal assets will be treated as separate from your business assets and will not be attached to satisfy any debt or lawsuit arising out of your practice.

Not Doing Your Due Diligence

There are many things that need to be considered when buying a dental practice. Before you buy, you need to find out as much as you can about the practice.

Do you really know what you are buying? Remember, once you have purchased the practice, it will be too late.

Here's a list of items you and your team (your accountant, lawyer, etc.) should review during the due diligence period of the purchasing process:

- The practice's clinical records, profit and loss statements, balance sheets, and tax returns for the past three or more years.
- The practice's ongoing contracts, utility bills, and other expenses of the business.
- The practice's reputation in the community and with suppliers;
- The seller's reason for selling; and
- The practice's potential for expansion
- The practice’s current staff, how much each is paid, and whether they intend to stay on with the practice after you acquire it.
- Details regarding tools, equipment, and fixtures in terms of what is owed on any of these, whether they are in good working condition, and their lifespan so that you can ascertain when the next capital expenditure may be.

- The practice's trademarks, business name, and intellectual property to ensure that they are properly registered, that they will pass through to you upon settlement, and that there will be no issues or litigation regarding any of the practice's intellectual property.

- Existing contracts with suppliers, staff, and any organizational clients to ensure that they don't contain any clauses that can cause you harm.

- Any partnership or joint venture agreements with third parties to ensure that they can be assigned to you along with the purchase and to ensure that you will not be taking on any onerous obligations agreed to by the seller.

- The technology used in the dental practice to ensure that it is suitable to the way you intend on operating the practice and the services you intend to provide and to make sure that you are not purchasing a problem that cannot be changed.

Talking Too Much

Confidentially plays an absolutely vital role in the purchase of a dental practice. Unless there are some unusual or extraordinary circumstances surrounding the sale of the practice, it's extremely important to keep the purchase of that practice as secret as possible, for as long as possible, and from as many people as possible.

Confidentiality is essential to maintaining a positive relationship with the practice's existing patients, suppliers, and employees. Should the practice's employees discover the owner's intention to sell, they may react negatively and jeopardize the practice's performance.

Likewise, the practice's patients and suppliers may become apprehensive and begin to question whether or not they should continue their relationship with the practice. Therefore, buyers are often required to sign a non-disclosure agreement (NDA) stipulating that any confidential information shared by the seller when negotiating the sale of the practice must not be shared with anyone else unless the buyer acquires that information as part of the purchase. In some cases, the seller will also be required to agree to keep any information regarding the sale of the practice as confidential as possible.

Over Negotiating

Buyers always want a great deal, whether they are buying a house, a new car, or a dental practice. But, you should be sure not to over negotiate in pursuit of that deal. By *"over negotiating"*, we mean being so aggressive with your negotiation tactics that your approach lacks fairness.

Fairness is a factor that influences the success of a negotiation, but is often overlooked. Fairness in negotiations does not mean each party meeting the other halfway, but each party being open to making whatever concessions that they can make according to their capacity to do so.

When negotiating the price of a dental practice, for example, you should ask for a *“fair”* price justified by its market value, industry standards, expert opinion, etc. If not, the seller may abandon the negotiations if he or she thinks that your offer is unfairly low or that you want more than you should for a competitively priced dental practice.

It must be emphasized that not only is the existence of fairness important, but the perception of fairness important as well. Even if you offer a price that is above the seller's bottom line, but you do so in an arrogant or deprecating manner, it's highly likely that the seller will walk away from the negotiations, even though you have met their price.

You should, therefore, make sure that you don't insult the seller. Refrain from using terms like *"you are asking way too much"* or *"it's not worth it"*. Instead, use terms like, *"I'm a buyer at this price"* or *"I'm comfortable spending this much money"*.

The bottom line is, the way you negotiate sometimes matters as much as its content. So, you should always be respectful and seek mutually agreed upon resolutions with the seller by accepting change and being willing to compromise.

Your job in the negotiation process is to engage the seller in a constructive dialogue. Once that dialog is open, the purchase price can only go down from there.

Not Establishing Firm Deadlines

A deadline is a date or time by which a task or process must be finished. Setting deadlines during business negotiations can also increase time awareness, improve organization and prioritization of activities, and inspire action.

In negotiations, deadlines often precipitate discursive exchanges and accelerate concession trading, which leads to conflicts being dissolved. In other words, deals get done in proximity to deadlines.

Deadlines also create pressure in business negotiations and provide accountability. Sometimes, a seller will leverage delaying and stalling tactics to force the buyer to give in on a particular issue of contention. However, setting a rigid, non-negotiable deadline that forces both parties to either move the negotiations forward and or walk away completely, can affect a positive outcome and get the deal done.

Failing to Work With a Professional Transition Team

Failing to work with a team of advisors and professionals that are experienced in the dental field is another pitfall to avoid when purchasing a dental practice. When acquiring any business, you will almost always need the help of an attorney and an accountant.

An attorney who is experienced in the dental field will help protect your interests comprehensively and efficiently. Likewise, a well-chosen accountant will help ensure that you are not liable for any outstanding debts or claims against the practice.

What's more, working with a business broker who specializes in dental practice transactions can be the difference between a successful transition into ownership or one that is poorly executed. There are many facets to buying a practice that you just won't know about. But a good broker can guide you through the process and make sure that all of the boxes are ticked.

Finally, it is also a good idea to establish relationships with other professionals, such as a banker, a financial planner, a dental insurance broker, and other helpful advisors. The right transition team will protect your interests, accelerate your transition, and put you in the best position to accomplish all of your business goals after the purchase has been completed.

Letting the Location Dictate the Practice Purchase

Experts often proclaim location to be the most important factor when buying a dental practice. But, in many cases, a more balanced evaluation of a variety of factors will enable you to identify a better opportunity.

Historically, a practice's value was largely dependent on its location. A practice located in a major metropolitan center was more sought-after (and priced higher) than a practice of a similar size located in the suburbs.

While you can't overlook a practice's location in terms of things like brand visibility, ease of access for your customer base, convenience for you and your employees, and how a practice in such a location will be perceived, you shouldn't let the location of the practice alone determine whether or not you buy it.

You must also give careful consideration to the location's influence on your ability to market the practice, the level of competition you will face, the total cost of operations, the taxes you will be required to pay, and the regulations you will be required to follow.

Underestimating the Potential to Grow the Practice

A dental practice's potential to grow is its ability to gain more patients and generate more profits in the future. This can be gauged by its ability to move into new markets, offer new products and treatments, market its services more effectively, and/or to employ other measures that will grow the volume of the operation.

When purchasing a dental practice, its potential to grow is absolutely critical to a quality purchase. Can you add:

- New services?

- New clinical rooms?
- New equipment?
- New ideas?

If you cannot grow the practice that you are buying, you should ask yourself why you are interested in buying it.

Different dental practices have different or varying degrees of growth potential. So, you need to carefully evaluate each practice that you consider to ensure that you are not overlooking any value that is hidden in its potential to grow.

This means that, in addition to evaluating how the practice performed in the past, you need to assess how much you can grow the practice in the future. This can be done by:

1. Identifying any key trends affecting the dental industry;
2. Understanding what the practice's revenues and profits are projected to be, and why; and
3. Finding out what strategies the current owner has not been employing that if you were to implement would dramatically grow the practice

A good assessment of a practice's growth potential will enable you to see its true value and identify a great opportunity, when it may otherwise be overlooked.

A Seller That Isn’t Ready to Sell or Pressures you to Sell

Sometimes, it is very hard for a seller to completely let go of a dental practice that they have sacrificed blood, sweat, and tears to build. Many sellers are excited to sell their practice but also terrified to be giving up what is likely their most valuable asset.

You should steer clear of sellers who seem to be reluctant to actually let go of the dental practice they want to sell. Here are a few clues to look out for:

- The seller wants an employment contract or consulting agreement to stay involved with the practice for a number of years after the sale.

- The seller has a list of demands that may cause the transition period to drag on for an extended period of time.
- The seller wants an unreasonably large amount of money for the practice and/or to continue to receive a percentage of the net profits/earnings of the practice after the sale.
- You have no definitive handoff date - you should insist that a definitive handoff date be stated in your sales contract or purchase agreement. While this may seem a little aggressive, you must establish a binding exit date to prevent the seller from lingering.

If you are selling a dental practice, be aware that some potential buyers will try to pressure you into agreeing to the terms they want. Nevertheless, you should never feel pressured to sell your practice for anything less than you think is fair.

Some buyers will insist that their offer is only good for a very short period of time, perhaps only a day or two. But, no reasonable offer to buy comes with such a short amount of time to accept.

A serious offer to buy will begin with the interested party providing you a letter of intent or term sheet that represents the starting point for further discussions and negotiations, not the endpoint.

Contact Dental & Medical Counsel

In many ways, purchasing a dental practice is very different from purchasing other types of businesses and comes with many different types of challenges. Therefore, it is always recommended that you work with an attorney who is experienced in the sale and purchase of dental practices.

Our dental attorneys specialize in the sale and purchases of dental practices and have the right background and experience to help you navigate the steps involved and avoid any potential pitfalls in the purchasing process. To learn more about how we can assist you, call **Dental & Medical Counsel** at **925-999-8200**, or send us a message via our contact form to receive more information.

Do you have questions regarding a practice purchase?

Dental & Medical Counsel was built with doctors in mind. We understand that you already have a busy professional life full of stress, heavy workload, and constant liability. Let us help you reduce your stress levels, improve your work/life balance, and reduce your worries and concerns with legal matters.

Additionally, our comprehensive and unique approach enables the most entrepreneurial dentists, veterinarians, optometrists and physicians to achieve their personal and business goals as they create massive wealth through smart strategies with the peace of mind of knowing that their practices are compliant with all federal and state laws.

Regards,

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