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Practice Management Information for Implant Dentists

De-Mystifying the Complex World of Dental Practice Purchases and Sales: New Strategies to Accomplish Your Goals (Part 1 of 3 Part Series)

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The *process by which you find a buyer* to whom you sell your dental practice or, conversely, the *steps you take to acquire a dental practice* can be *challenging, complex, and time-consuming*. Your finding the “perfect practice” to purchase or the “right buyer” to whom to sell demands (i) an understanding of the chronology of steps to be completed in this process and (ii) a recognition of the significant *economic, tax, and liability consequences* to you for years to come resulting from such a purchase or sale.

Dental practice purchases and sales are *fraught with peril* in the form of (i) undisclosed equipment liens, (ii) office leases with limited rights by a seller to transfer the lease to the purchasing dentist, (iii) uncompleted or failed dentistry to be performed or redone by the seller or buyer, (iv) accounts receivable to remain owned by the seller or to be collected by the buyer, and (v) restrictions on the seller’s right to practice dentistry, solicit staff, or treat patients subsequent to any transfer of the practice to a buyer. *This 3-part article serves as a compass to help you to navigate into safe harbors and to avoid the precarious shoals and hidden dangers of dental practice purchase and sale transactions.*

Part 1 briefly summarizes which advisors to engage and those *necessary* steps to follow when purchasing or selling your dental practice. Part 2 identifies the *related entities* (such as a dental corporation) which need to be created or the *related legal documents* (such as your office lease and office employee manual) which need to be prudently prepared, analyzed, and signed in addition to your practice purchase and sale agreement. Part 3 explains the *essential* (albeit often over-looked) *terms* and conditions to be drafted in your practice purchase and sale agreement.

1. *Identifying key participating parties.* The critical prerequisite which you must remember is that each of the advisors counseling you *must have dental transaction expertise*. In much the same way that you would not engage a general practitioner to perform an extraordinarily complex surgery requiring an oral and maxillofacial surgeon, neither should you engage any attorney, accountant, practice broker, lender, or consultant to assist you in a dental transaction whose expertise is not focused *solely* on the dental field. Moreover, especially in the area of dental acquisitions or sales, your attorney’s experience

should be in *dental transactions* and *not*, for example, in *unrelated dental matters* such as dental malpractice defense, dental licensing, or Denti-Cal litigation. While these areas certainly involve advising dentists, none of them involves *the unique and required knowledge of dental practice purchase and sale transactions*.

Your utilization of the following advisors *will save you substantial time and money and reduce your stress* because of their respective specializations in those areas in which you seek their assistance:

- Recognized *dental lenders* (such as current ADA or CDA endorsed lenders Matsco and Bank of America) are able to provide you with loan approval within days of your submitting required paperwork. They have *more expedited and liberal funding policies* than conventional banks or lenders who do not specialize in making dental loans.
- Recognized *dental CPAs* are intimately familiar with appropriate percentages for a dental practice's financial criteria such as its net operating income, staff salaries, lab expenses, and office rent expense. More importantly, a dental CPA will also understand appropriate amounts to be allocated to your practice's goodwill, covenant not to compete, and other assets so that you can accomplish the maximum amount of tax savings appropriate for you.
- Recognized *dental practice brokers* serve an invaluable function of bringing together pre-qualified buyers with ready, willing, and able-to-sell owners of dental practices. Such brokers have a wealth of information describing the dental practice which meets the specifications previously communicated to them by the prospective buyer. In California, while dental practice brokers must be licensed with the state's Department of Real Estate, no other qualifications or licenses are required. Most brokers inform you that any written description or profile of the seller's practice has *not* been based on their own independent investigation but is the result of data merely having been provided to them by the seller. Accordingly, information about significant matters (such as the practice's income, expenses, number of total patients, number of active patients, age and condition of the equipment, percentage of the practice allocated among cash, insurance, PPO, capitation, or medi-cal patients, the percentage of the practice devoted to restorative procedures and specialty procedures, and the sources of new patients) *must also be independently verified by you and your advisors*. *The broker does not warrant the accuracy of any of the information provided to you* because the broker has not performed any "due diligence" to determine the accuracy of the seller's data or the truthfulness of the seller's representations.

Be aware that *some* dental practice brokers also receive compensation or “points” from lenders for directing, referring, or submitting the buyer’s loan to them for funding. While the selling dentist is normally charged a fee of ten percent (10%) of the purchase price by the broker as a fee for the broker’s services, neither the buyer nor the seller is aware of the “points” paid by the lender to the broker for the broker’s directing the buyer to the lender or procuring a loan for the buyer. Accordingly, if the dental practice broker is assisting you in obtaining financing, the broker should (i) explain why the lender recommended or chosen by the broker is the best funding source for you or (ii) shop multiple prospective lenders before you make a final decision regarding which dental lender to use. *In either situation you should inquire from both the lender and the broker whether the broker is receiving any compensation for the referral.* Some dental accountants and attorneys also receive a fee for their referrals; therefore, also request those advisors to confirm in writing any compensation paid to them by your dental lender.

- Recognized *dental consultants* are important advisors if you are contemplating selling or purchasing a practice. Dental consultants assist buyers prior to and subsequent to their acquisition by analyzing the practice (e.g., the staff’s efficiency and competency, office procedures, and patient financial policies). *They serve as a “second pair of eyes” to the buyer.* Some have the experience to validate the broker’s valuation of the practice and analyze the practice data provided by the seller. Unlike the broker who owes fiduciary and legal obligations to the seller and whose commission is paid by the seller, the dental consultant is an advisor who (i) is paid by the party engaging the consultant, (ii) provides independent objective advice, and (iii) should have no vested interest in the outcome of the purchase and sale transaction. Their compensation can be either an hourly fee or a fixed amount based upon the scope of the services rendered. *The seller’s use of a dental consultant is also prudent* because the consultant can evaluate the practice and make recommendations regarding patent or latent deficiencies adversely impacting its value or marketability.

Your securing the right dental attorney, dental CPA, dental consultant, dental broker, or dental lender need not be a difficult ordeal. *There is no substitute for your advisor’s having numerous years of experience* and referrals from clients willing to extol their advisor’s skills in helping consummate their dental practice transactions.

2. Proper mind set. Recognize and acknowledge in advance that your dental practice purchase or sale can be a stressful experience. This will assist you in coping with the complexity and anxiety associated with the event. When people’s futures are being affected by parties such as landlords, lenders, CPAs, and attorneys, heightened anxiety or acrimony are frequent and real outcomes. A

significant part of a person's life (*if you are the seller*) is ending at the time of the practice sale. Such event can often be met with obvious reluctance and remorse by the seller shortly before the date of transfer is to occur. A significant part of a person's future (*if you are the buyer*) is being determined by the buyer's consultant, landlord, lender, CPA, and attorney during the negotiation process.

3. *Not all participants in the purchase and sale process cooperate.* A seller's landlord, for example, has no compelling reason to act expeditiously to meet your deadline for completing your transaction. Why? The landlord's lease provides for an ongoing rent obligation whether such responsibility is continued by the seller or assumed by the buyer.

Not all participants in the purchase and sale process have your best interests in mind. Some desire to complete the transaction irrespective of the wisdom of your practice being purchased or sold. For example, some dental lenders' representatives want to fund the loan irrespective of the buyer's possible incompatibility with the prospective practice. Also, some dental practice brokers are motivated to generate their sales commission regardless of a possible lack of success the buyer may have in the new practice or the buyer's actual ability to pay a promissory note taken back by the selling dentist.

Dentists have little experience in dental practice purchases and sales. You rarely engage in these activities as a regular course of business. Accordingly, you do not know what is the "custom and usage" in these types of transactions regarding significant business matters involving money, risk, and liability. Therefore, *create a sample checklist* (such as the one below) to serve as a roadmap in determining whether the proper protocol by which you are selling or purchasing your dental practice is being followed and, therefore, acceptable for you to continue as a participant.

- a. Set forth in writing certain criteria and timelines within which the events are to be achieved (e.g., loan approval, attorney's approval of purchase and sale agreements).
- b. Remind yourself that you will *not* continue with the transaction if your criteria are *not* reasonably and substantially met.
- c. Be cognizant of the fact that *some advisors* (whether inadvertently or intentionally) *give advice to you outside the scope of their license, experience, or expertise.*
- d. *Allocate reasonable time* for you and your advisors to accomplish your goals within the *timelines previously established by you* (and *not* by any timelines artificially established by *participants who get paid* a commission when the transaction is consummated).

e. *Remember - there is no substitute for experience and excellence.* It will be *less time consuming and costly* for you to retain dental specialist advisors who are *superb* (and *not average*) in their counseling of you than it will be to engage an advisor who appears to be less costly and without the years of specialized focus and experience.

Next issue: In part 2 of this article you will learn (as the prospective buyer or seller) of the preliminary significant legal documents you will be signing to protect yourself during the practice purchase and sale process. Letters of intent, deposit receipts, and dental nondisclosure and confidentiality agreements are critically important documents uniformly signed by serious dental practice buyers and sellers (i) to make sure that there occurs no unauthorized disclosure of a seller's practice profitability or a buyer's financial condition and (ii) to preclude either party in the transaction from subsequently trying to renegotiate any of the "deal points" previously addressed in the letter of intent or deposit receipt (e.g., the purchase price, ownership of accounts receivable, or the scope of the seller's covenant not to compete).

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