Don't Wait!

Plan Today!

Five Alternative Exit Strategies

by John F. McDonnell

Over the years while attending state and national dental conventions, I will run into dentists I have known for years and during our conversations they tell me that they will be ready to sell their practices in five years and will call me at that time so I can help them.

I see these same dentists every year at conventions and each year they tell me that they will be ready to sell in another five years. Sometimes 10 years have gone by before they finally contact me. Each year I encourage them to plan their transition now and not wait. Many of these dentists are friends of mine and will eventually contact me to help them. If you are planning to exit your practice within one, five, 10 or 20 years, the time to plan is today.

Benefits of planning today for your exit strategy:

1. You will have the peace of mind of knowing that your exit strategy and retirement from dentistry is planned. This means that you, your family, staff and patients will all benefit.
2. Having a plan assures that you are more likely to sell the practice at its peak and not when it is in decline.
3. Planning now gives you an opportunity to have higher earnings during the years between the start of the plan and your exit.
4. Implementing a plan allows your staff and patients to have a clear path to remain with the practice as they will be taken care of and work with your heir apparent.
5. Having a plan assures that you will pass on the legacy of your long-term practice to a worthy successor.
6. A plan gives you a form of insurance in the event that a death or disability was to occur.
7. Planning ahead allows you to explore multiple alternatives for the transition of your practice.

Planning now is a form of insurance to protect one of your most important and most valuable assets. Here are five alternatives:

Option 1: Sell the Practice and Leave

Selling the practice and leaving is still the most common of practice sales in our industry. With this option the seller normally leaves immediately following the sale or within a three- to six-month period. The reason for leaving so soon is that many of the solo practices do not have enough patients or a space large enough to have two full-time dentists in the office simultaneously. As the buyer needs to pay the overhead of the practice, themselves and the bank loan for the practice purchase, there is nothing left for the seller.

Benefits and reasons:

1. The dentist is ready to retire and not practice any longer.
2. The dentist has health issues and has to retire and turn over their patients to the new buyer.

3. The seller avoids having to commit to a new long-term lease as the buyer will be the one to sign the new lease.
4. The senior dentist has other interests, hobbies or businesses.
5. In most cases the seller receives 100 percent of the sale price at the closing.
6. In most cases, in addition to the sale price, the seller receives the accounts receivable.
7. Currently the seller can take the 15 percent capital gains tax rate.

Option 2: Sell the Practice and Stay on After the Sale

What if you could sell your practice and stay on after the sale continuing to enjoy performing dentistry and earning a fair compensation for two to 10 years? When we interview dentists who are preparing their exit strategy, the common theme we hear is that they still enjoy doing the dentistry, taking CE courses and seeing the patients, but they do not like running the business, dealing with insurance companies and handling staff issues.

Benefits and reasons:

1. Dentist is tired of being a business owner and manager 24/7, 365 days a year.
2. He or she has the peace of mind of completing an exit strategy while still able to practice dentistry.
3. We find that dentists in their 30s to 50s who have good practices but due to a large debt service and high monthly bank payments find it stressful that their earnings are not as high as expected.
4. Owners with a full-time associate realize that they can switch roles with the associate and stay on after the sale.
5. Some baby boomers have a set goal of selling their practices after reaching age 55 and this strategy allows them to sell now but continue earning income after the sale to increase their investments and offset the losses they might have due to the recent economic downturn.

Option 3: Delayed Sale of the Practice

This option is becoming more popular as it allows the seller to stay in control of the practice, maximizes earnings and gives an opportunity to sell the practice at its peak. This option requires the office space to be large enough for at least two full-time dentists. It also requires the practice to either have enough patients and work for two full-time dentists or have the potential of patients to be served. If not, the practice will need to have a proactive marketing plan for new patients so that the two dentists can be productive full time.

This option is similar to the sell and leave strategy in that there is a signed asset purchase agreement with a specific target date for the practice sale. There is an associate with an employment agreement for the period of time between joining the practice and the targeted sale date. This time period is normally one to five years depending on the needs of both the seller and the future buyer associate. At the end of the one to five year period the associate purchases the practice by borrowing 100 percent of the sale price to be paid to the seller on the prearranged target date for the closing. A methodology is agreed upon in the beginning to calculate the sale price at the time of the closing and is part of the mutually beneficial agreement signed at the start of the process. This agreement includes a three- to six-month time period during which both the host dentist and associate can ter-

continued on page 98

continued from page 97

minate the delayed sale purchase agreement without any penalty in case they do not work well together.

Benefits and reasons:

1. The seller can remain in control of the practice longer. Some dentists prefer to be in control and do not want to have a partner.
2. The seller can maximize his or her income in the final years of practice. Because the associate is going to be the future owner, his or her commitment to the practice and the performance are at a higher level. The practice normally will grow during the period before the targeted sale date and the earnings are higher during that period.
3. Because the value is based upon the most recent year's performance (with consideration to the buyer for his or her contribution to the growth of the practice) the seller is likely to receive a higher sale price at the closing then the foundational value at the beginning of the process.
4. The buyer has a chance to get to know the patients in the practice, the staff and the office systems. By the time the delayed sale is implemented, a smooth transition should occur.
5. Because the practice has two full-time dentists at the targeted delayed sale date, the seller has the option of remaining with the practice after the sale and becoming the associate of the practice.
6. The seller has the peace of mind of knowing that the associate has committed to the delayed sale thereby avoiding failed associates coming and going As the sale agreement is signed in the beginning this keeps the associate there.
7. The seller has the chance to pass on the legacy of patients and staff to this chosen heir apparent who has already been with the practice for a time period before the targeted closing date.

Option 4: Equity Buy-in Buy-out (Partnership)

Over the last 30 years, approximately 25 percent of all dental practices have chosen to be partnerships. This percentage has not fluctuated more than two percent over those years.

This option requires a space and practice large enough for at least two full-time dentists. The number of years needed to justify this option for the senior dentist is five to 20 years from the retirement of the host seller. If a dentist has practiced solo for more than 30 years and is in his or her 60s, we do not feel this option is viable at that stage of practice.

This option is particularly applicable to an owner who currently has a good associate in place or is in the process of choosing a new associate. This strategy is for the owner who wants the peace of mind of having the heir apparent under contract with a plan for the equity buy-in buy-out partnership in place. Often good people (owners and associates) say they will discuss a transition plan in the future and the future never comes. And without a win-win plan they normally fail in their attempt to have a partnership. We suggest that the discussion happen early on and that agreements for the partnership be signed by all in the beginning. This will insure the successful process of a buy-in buy-out partnership strategy.

Benefits and reasons:

1. This option gives the seller the peace of mind of having the heir apparent on board and a transition plan underway.
2. This option allows the owner to have a future partner with whom to share the burden of managing the practice.
3. The owner has a trusted equity partner in the office.
4. As the equity partner is normally younger, the practice will be attractive to young couples with children thus lowering the average age of the patients.
5. Often the new partner might do some specialty procedures that are traditionally referred out of the practice. That work/income and can now remain in the practice.

Option 5: Merge-in Merge-out

When a dentist practices in a home office or does not want to sign a new long-term lease in a professional building, the merge-out strategy is a good option. The practice can be merged into a larger practice close by and the selling dentist can move with the patients for a period of time earning compensation after the sale. When the selling dentist can come with the patients for a period of time this assures the buyer that the patients will come to the practice.

Assuming that the selling dentist's office is large enough for two full-time dentists or more then the merge-in strategy can be implemented. If a young dentist in the area has a smaller office space or a following of patients, he or she can purchase the seller's practice and merge the patients and practice into the larger space. This again might allow the seller to remain in the practice to continue to see patients.

The merge-in merge-out option allow the seller to get the maximum practice sale value. When merging the practices many of the expenses are lower while the earnings in the joined practice are positive so a positive cash flow for the buyer should result as well.

Benefits and reasons:

1. The problem of the home office practice sale is solved by the merge-out option. This allows the seller to market the house sale to a larger buyer pool then just dentists. In most states home offices are very difficult to sell.

continued on page 100

continued from page 98

2. This strategy solves the problem of a senior dentist who is faced with signing a long-term lease for the office space.
3. This option allows the seller to receive the Fair Market Value price for the practice when they agree to move with patients to the new office for a period of time.
4. This strategy allows the seller to stay as an employee dentist post-sale for a period of time earning compensation.

Less than five percent of dentists have a plan for their exit strategy. The good news is that whether you plan to exit in one to 20 years, you can still have a plan and have time to implement it. The longer the time between the start of the plan and the exit, the more time you have to explore the five alternative strategies. However, even if you need to sell in the near future, planning ahead is always the best course of action.

Suggested steps to take to plan your exit strategy today:

1. Choose a transition organization that specializes in practice transitions 24/7 365 days a year and does not have other products and services to sell.
2. Have your practice valued by a qualified, experienced transition specialty organization in the dental industry. This foundational valuation will inform your choices with the five alternatives.
3. Choose a dental CPA to work along with the transition speciality organization as part of your advisory team.
4. Have a written financial plan completed by a qualified planner and have it monitored on a yearly basis.
5. Decide what you want to do about your exit strategy your timetable. Plan your transition now, including how long you want to remain in practice after the sale.

You have the choice. Plan your exit strategy *today!* ■

Author's Bio

John F. McDonnell, as president and founder of ADS McNor Group has served dentists for more than 40 years in the area of practice transitions in Maryland, Virginia, DC and Pennsylvania. Three generations of his family have worked with dentists in these states for more than 60 years. He is the former president of ADS, the largest dental practice brokerage company in the United States. He has lectured locally and nationally on the topic of dental practice transition. Mr. McDonnell is an expert in assisting dentists in joining and leaving dental practices as well as facilitating all types of transitions. He can be reached at johnfm@adstransitions.com or 888-419-5590 x410.