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AN EXCLUSIVE - EXECUTIVE POST - SPECIAL REPORT

“Professional Dental Practice Life-Cycle Financial Planning”

An exclusive report on dentists - their professional practice career and economic life cycle - by a leading national dental management corporate executive

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TOPIC
Dental Practice Management and Life-Cycle Financial Planning
It’s [NOT] for Dentist’s Only

EXERPT: “The challenge is that for many dentists their practice is too big and too profitable to sell to new dentists who have been, traditionally, the practice buyers. Almost fifty percent of the dentists are baby boomers pushing 50 to 55 years of age. And unfortunately, they cannot afford to retire at this point and still maintain the lifestyle they have created.

But, the temptation is there - the thought is occurring more frequently - and it is very compelling.”
Dental Practice Life-Cycle Financial Planning

It's [NOT] For Dentist's Only
By Thomas A. Knox; MBA

Accept the challenge and profit by it! Many dentists are profitable as demonstrated by the fact that they earned more money on average in the last five years, according to a survey conducted by the National Association of Health Care Consultants and internal iMBA Inc., statistics. This is significantly ahead of the rise in the consumer price index.

A statistical profile of general dentists reveals the following:

- 70.5% are solo practitioners
- 48.0 is the average age
- 37.3 hours is the average work week
- 33.5 is the average number of patients seen per week
- $165,000 is the average net income

Life is good! So what is the challenge and what is to be done about it?

The challenge is that for many dentists their practice is too big and too profitable to sell to new dentists who have been, traditionally, the practice buyers. Almost fifty percent of the dentists are baby boomers pushing 50 to 55 years of age. They cannot afford to retire at this point and still maintain the lifestyle they have created. But the temptation is there and the thought is occurring more frequently.

But what can they do? They have big practices that would sell for $500,000 - $750,000, a very healthy deposit into the retirement fund. But to whom can they sell? There are few dentists who can afford to buy them or who have the inclination and business savvy to build their own practice through acquisitions.

Those who can afford to buy them are the Dental Practice Management Companies (DPMC). If a dentist does sell to a DPMC, will they receive enough money to retire? Will the purchase agreement even allow the dentist to leave the practice initially or even slow down productivity (most will not)? And if the dentist continues to practice, what will life be like after the transaction closes and one no longer has sole control over one's business?
Dentists are faced with a professional economic life cycle that rises the first 5-7 years in practice and levels off for the next 15-20 years. There is then a peak in production for about 3-5 more years and a gradual decline into retirement. The goal is to get the annual income as high as possible as fast as possible and sustain it as long as possible or desirable. At some point, usually at retirement or just before, there is a big spike in income when the practice is sold. Since most dentists are solo, the typical sale is to another, usually younger, dentist.

But now there are important questions such as will there be a buyer when I am ready to sell? Who is it and how much will they pay me?

The question of finding a buyer - and the right price - needs careful thought. The past may not be an accurate prediction of the future. Dentists are forming groups and as they consider expansion, building may make more economic sense than buying depending on the price and condition of the practice. Tired, worn and old practices do not command premium prices. And it is hard to predict how women who now comprise as much as 58% of the students of some dental schools will respond to the notion of ownership. Yet women would be the majority of the expected buyers.

Many dentists are facing critical business issues, yet they do not fully recognize the issues, nor understand the positive and negative implications of the issues, nor do they have a decision making process in place that goes beyond the annual meeting with the accountant and tax advisor. Business is so good for dentists that they have trouble maintaining a busy clinical practice and managing the business affairs of their practices at the same time. Therein lays the risk to continued success. The critical questions dentists must answer are:

1. **Will the clinical and business performance that has made me successful up to this point continue to make me successful for the next 10 to 15 years that I want to practice?**
2. **Can I manage this business by myself?**
3. **Do I want to manage this business by myself?**

The concept of practicing in a group has been around dentistry for a long time. But group practice has not taken hold in dentistry because there was too little benefit to counter the difficulties of group practice. The trend toward joining groups increased as the marketplace got more competitive.

Historically, group practice arrangements have been driven primarily by the transition of ownership from the senior dentist to the junior dentist. However, there are many new drivers to form groups:

- **Provide a wider array of services to patients and to buyers of dental offerings**
- **Offer more convenient hours of service for patients by sharing the burden of working evenings and weekends.**
- **Share the investment required to provide state-of-the-art technology.**
- **Share the investment required to promote the practice in the marketplace.**
- **Develop and use the quality assurance & utilization review protocols required by buyers.**
- **Negotiate with health plans, managed care companies and other who want to buy a financing and care delivery system in one package.**
- **Acquire the management expertise needed to run a growing and increasingly complex business.**
Many of the items listed are changes in the marketplace. The need for greater management expertise has spawned the growth of Physician Practice Management Companies (PPMCs).

In the early to mid 1990’s, those companies managing medical groups broke new ground and found favor on Wall Street and Main Street. These early companies represented general and medical professionals as well as dentistry. The DPMC’s were considered a single specialty management company. Lots of money had been made, at least on paper, by a very small, select group of people who created an industry from ground zero.

Then disaster happened in 1998. The bubble burst and the market value of the stock of the PPMC’s, as a sector, dropped like a rock. The DPMC’s fell but not as dramatically as the PPMC’s. With stunned amazement people began to examine a number of questions: Was this expected or was everyone caught by surprise? Did anyone think that stocks selling at 60 and 70 times earnings were sustainable? Are people just mad that what was predicted really did happen and some spent the money before they actually received it? Or did we miss the fundamentals of success and bet on the wrong horse?

Currently, the world appears to be a bit more challenging. Is the PPMC sector dead or in a coma? Are they a failed concept or is there an opportunity to rethink, reorganize and properly match expectations of Wall Street and Main Street? Are those companies who manage single specialty different than those who manage multi-specialty? There is a strong argument to make that the latter opportunity is before us and that there is a role for a single specialty PPMC to play in the long term growth and development of practices whether they are medical, specialty, dentistry, podiatry, chiropractic, or even veterinary practices.

There is a major assumption behind this conclusion and that is: Most practices need a business partner and greater access to capital because the complexity of the business of health care and the resources required to sustain success will only be greater.

To date many practices have tolerated administration as an evil necessity. The environment calls for, even demands, a greater breadth and depth of executive and management talent. Clinical skills and business skills must be brought together and treated as equal and necessary parts of a successful business.

Two critical questions: Can the dentist accept this premise? Can the dentist perform the management function?

The answer is that with the commitment of enough time and training, probably. But to make it work, the business time must go up and the clinical time down. Most dentists want to practice dentistry, not management. If management is ignored, it can be the weak link of the practice.

This does not mean that every practice will need to be sold to a management company. Even in markets with heavy managed care penetration and dominant management companies there will be room for those who have the fortitude and savvy to continue operating their own business.
Realizing Value in the Dental Practice

There is an art to converting one’s business into cash at the time of sale. Some are masters at this process, making a career of building and selling businesses while most are amateurs taking a turn once in a lifetime near the end of their working career.

For many this is not even an opportunity to think about at all because they are not owners of the business. They are just valued employees who contribute mightily to the ultimate value of the business but do not receive the ultimate rewards.

Many dentists frequently make this decision, to be an owner or not, in an unconscious way. They decide the profession they want to practice; they work very hard to meet the entrance requirements to the school they want to attend; they work their butts off to learn academically what the profession is about (which includes virtually no education or training in the “business” or “economics” of the profession); and they generally borrow huge sums of money to finance their education and living expenses during the training process. They graduate, get licensed, get their first “job”, get married and begin to live a professional life cycle and a personal life cycle that parallel each other, but do not match each other.

About the time they get settled in their “job” as an employee they have an opportunity to become a “shareholder” or owner of the business. They choose to become an employee because at the start of their career, they do not have the capital to start a practice from scratch. The economics of the business force many initially into an employee status rather than an owner status. Ownership requires a capital investment frequently in excess of six figures. About the same time they have started to pay off school debt they acquire a mortgage for their house and the expenses of starting and raising a family.

As they reach the mid-point of their careers, their earnings go up, they are finally “getting ahead” financially at home and then another opportunity at ownership arises when the senior partner of the practice decides to retire. Their analysis indicates his shares are valued very high and they realize that the business needs a capital infusion to replace a roof, the carpeting, the heating system, etc.

The potential buyer also believes the business needs a new information system. If they pay too much for the practice and the privilege of ownership they will not have enough capital to improve and grow the business in order to realize an appropriate return on their investment. This is a scenario played out all over the country. Paying too much initially does not allow one to realize value over time; not investing in the future growth of the business does not allow one to create and realize value over time. A trap is set that has no apparent way out.

A basic problem is that the average dentist focuses too much on “annual income” and not “wealth”. Wealth in this case is defined as the value of the practice. Income and wealth are not the same things. Dentists, like most physicians, are in a personal service business. They generate cash flow only if they are busy seeing patients. The real value of any personal service business is its ability to generate sustainable cash flow in the future. In other words, value is determined by what one can earn with this asset tomorrow and not by how much was made yesterday.
How should the ownership of such a business be approached? One may suggest that we need a change in view about ownership and value creation. It will no longer work to have groups form with a small number of owners.

Ownership, with all of its rights and responsibilities, must be readily available to a significant number (50%) of those practicing in a group. The owners must focus on creating value in the business and not on how high an individual owner’s annual income can. The “business” of the practice requires a constant feeding of dollars to assure it remains competitive, has proper equipment, retains competent staff and is physically and emotionally appealing to the patient and buyer of health care services. The business needs to be fed capital in order to grow, or at a minimum, maintain its value.

How is this approach different from current practice? It calls for dentists to begin thinking about the value of the business at the start of their careers and reduce their fixation on annual income. What is the business worth today is more important than how much am I making today. A long-term perspective is required, not a short term one.

If you make this change in perspective and behavior is made, you will be in a position to realize one of the greatest rewards of building a business: the ability to sell it and turn paper value into cash. For many this is a dream come true scenario. But to make it reality, you will need more than good luck and impeccable timing.

To capitalize on the opportunity to sell your business, and to get the highest possible value, you will need to prepare for this critical transaction. You will need to analyze each component of your business, determine the critical success factors that make your business valuable, now and in the future, and whether or not you have the will and the capability to build the value of your business all by yourself. If you can--do it! If you truly believe that you can build, manage and finance your business alone, do not seek business partners. The more owners involved, the more complicated life gets. Keep your goals clear and your organizational life as simple as possible.

But if you cannot build your business by yourself, if you do not have all of the knowledge, skills, abilities, capital and time, then think through very carefully what you need from a business partner and who can best deliver what you need.

You should take on a partner only when you need new, different or better knowledge, skills and abilities or money brought into your business and it is critical that the potential business partner demonstrate an ownership perspective and behavior to the rest of the organization. Partners need to have complimentary reasons to be in the partnership for the long haul to make these associations meaningful and as successful as possible.

The idea is to do everything possible to strengthen your position, making your business the most attractive to prospective buyers. Remember, your business is worth only what someone is willing to pay you for it. Your expectations or needs do not count at this point. What can you do to maximize the value of your business?
Crafting a Business Plan

As suggested earlier in this treatise, you must be able to articulate to yourself and to others what you want to do with your business and how it is going to be done. Implementation of that plan is required if you want to maximize value and make your business attractive to a potential buyer. You must know your patients, products, competitors, market trends and cost structure inside out and backwards. You have to know the variables that impact value and manage them appropriately. You must study your financial projections as much as you study your dental records.

Beyond this traditional plan, you need a personal plan to know yourself well. The key yet deceptively simple questions to this plan are:

1. Where am I now?
2. Where do I want to be five years from now?
3. How do I get there?
4. Can I duplicate this level of success for the next five years doing what I have been doing for the past five years?
5. Is the value of my business more this year than last year?
6. Do I need a business partner to accomplish my goals and objectives?

The business plan is a tool designed to help you hold yourself accountable by focusing on the right measures of success. Remember, you get what you measure!

Focus on Profits; not Revenues

Shift the focus of your business and financial plan from saving taxes to increasing profits. Many dentists will milk their business by allocating revenues to a wide range of fringe benefits. Their goal is to reduce profitability and thus limit taxes. Paying taxes is good because it means your business is profitable. We are not suggesting that you pay more taxes than you are required to pay but driving fancy cars and wearing expensive watches means you are consuming income now and not building future wealth. Trying to avoid paying taxes may seem like a wise strategy, but it can be an anchor when the owners seek to sell because the potential buyers want to see profits.

For example, if your business will sell for a multiple of five times earnings, each incremental dollar of profits would produce five dollars of capital gains when the company is sold. That is a huge payoff for focusing on the right variable and exercising financial discipline. The point is your tax return should not be your business plan. Such a focus may cause you to miss critical market opportunities that will allow you to sustain a successful business and increase its value.

Actively Managing you Practice Assets

Every dentists should, on at least an annual basis, take a new look at how he/she manages dental practice assets. What assets do I own? How can I make these assets more productive? Take steps to eliminate unproductive equipment and space. Sell off unproductive real estate, or find someone that will put it to good use and produce a new cash flow for you. Such moves will enable you to extract more cash from the business while you own it and allow you to focus on growing the value of your core business.
Real estate is always an interesting issue for a dental practice. To own or lease the space is the proverbial question. A more important and all encompassing question is: How much capital do I have and how can I best put it to work? Is my business changing such that I need to put cash into other assets in order to maintain profitability?

For example, how prepared are you to conduct some of your day to day business functions via the Internet (eligibility, claims submission, payments, etc.). If you cannot function in cyberspace, owning your own building may not make a difference. How much do I spend on market research to learn why my patients come to this practice and stay with this practice? Information is becoming a far more valuable asset. What am I doing and how much am I spending to gain more of this asset and use it to make my business more profitable?

**Actively Groom your Successor**

This is a particularly sensitive issue for dentists. The vast majority of dentists practice solo or with one or two associates. As stated before, the real value of personal service business is to generate future cash flow and profits. Any business, no matter how small, needs leadership. The value of your business is enhanced if there is continuity. Should you die, choose to retire or move to a second career or become disabled, your best approach is to teach your second-in-command everything you know about your business. This can be extremely hard to do, especially if you are the only owner. But the approach should provide two benefits:

1. **The interaction will offer you another perspective about running your practice**
2. **It assures buyers that a capable successor is in place to assume control and will continue managing a successful business.**

Why is this discussion important and how does it relate to a DPMC? The answer is fundamentals:

1. **Where am I now?**
2. **Where do I want to be in the future?**
3. **Do I need a business partner to accomplish my goals and objectives?**

If you believe you need a business partner, then a DPMC may be one tool you wish to use. But what makes a dental practice management company the right tool?

**Change Abounds in the Marketplace**

The health care industry has been a level five-whitewater rapids for the past 5 to 10 years and it will continue to be for the next 5 to 10 years. The toll of operating in this kind of environment is beginning to show up and will continue to do so. Examples are bankruptcies, loss of market value, mergers in which the identity of one entity disappears, loss of market share, reduced profitability, high turnover of staff, etc.

All initiatives in the marketplace, whether successful or not, are aimed at two fundamental issues:

- **How to make the business perform better operationally and financially.**
- **How to manage market forces pushing providers to work more efficiently and effectively.**
The second issue is driving the first. The changes required to keep a dental practice sustainable and profitable are about the marketplace. The fact that the marketplace views dental, or any other medical services, as valuable but wants to buy them and pay for them differently than they have in the past should not be taken as a personal attack on your character or professional capabilities.

It is just business. Accept, no embrace, the fact that buyers want to hold you accountable, as a professional providing a personal service, and you will be ready to build a sustainable and profitable business for the next decade. Deny this fact and you put your business at considerable risk.

The marketplace has experienced a very wide swing regarding practice management companies. One minute they are the darlings of Wall Street and the next minute they are a failed strategy. Since when is bringing better management to dentistry a failed strategy?

The recent activities on Wall Street lead one to conclude that Wall Street will back companies that are increasing the revenue and profitability of individual practices in a plausible fashion. There is a place for DPMC’s but their focus must be a strategy that makes sense. It is very important for the dentist/business owner to understand that a relationship with a DPMC is about more than just how much money can you get for your practice at the time of the initial transaction. It is about the core values of why you would affiliate with a DPMC in the first place. The answer should come from your business plan.

To be successful, the DPMC’s must focus on the core values of why dentists are affiliating with them. Dentists are looking for business partners that will build value. Dentists need and want more than cash. They need an ongoing relationship that has aligned incentives to succeed, that is, be more profitable. Dentists need increased efficiency and a way to tap into new markets and services for revenue and ways to contain if not reduce expenses.

As dentists evaluate their business needs, they need to be very careful about who they talk to about selling their practice and what the potential buyer has to offer. Is it just money or is there a level of experience and expertise that the business partner must bring to the arrangement? What happens after the closing and the “courting” process ends? Do both parties bring knowledge, skills and abilities to the relationship every day to increase the value of the business?

The business partner needs to be more than just a one-time financial bonus for the dentists. Know your own business needs and expectations and then determine the potential business partner’s ability to meet them. Judge each partner separately and not the industry. Each DPMC is unique and has the ability to be a success. But your challenge is to find the one that can bring the most success (profitability) to your business.

**Increasing Demand for Accountability**

Being accountable for the services you provide is becoming one of the driving forces behind the need for consolidation of a dentist’s practice and the need for greater depth and breadth of management knowledge, skills and abilities.
A decade ago, The National Association of Dental Plans Foundation announced the basis of an accreditation system aimed at boosting the stock of managed dental plans with employers, other payers and consumers. The industry itself is building the blocks of a quality-based performance system “aimed at coralling widely divergent operating and quality practices into a common standard.” The accreditation system includes 35 standards relating to quality, utilization management, credentialing, member’s rights and responsibilities and dental records. This proposed system represents a “high-water mark for the dental industry”. The system would create a benchmark for payers, consumers and others to compare plans on quality, and would increase the comfort level and knowledge of dental care purchasers about what they are buying.

Many employers are looking for ways to upgrade their dental plans without increasing spending. The dental profession is way behind the curve in defining and measuring quality compared to the medical profession.

For example, it has no widely accepted diagnostic codes; few widely accepted and validated parameters of care and few outcome studies. Employers have no way of tracking whether their enrollees are improving oral health and whether they are satisfied. The employers are after demonstrable outcomes. To meet this demand the dental plans are measuring employee satisfaction, credentialing their participating dentists, conducting office audits and trying to verify treatments. As a broader stream of patients is directed to a smaller number of dentists, employers want assurances about the dentists. This means dentists will be monitored to assure patients are treated appropriately. This translates into a movement toward “evidence-based care which involves evaluating a patient’s genetic risk factors toward dental disease”. The goal is to maintain a patient in a state of dental wellness.

Some organizations are determining which patients are at risk for cavities and periodontal disease so they can apply more resources to patients who really need it. They are also attempting to determine those dentists whose practice patterns naturally focus on this approach to care. This approach allows the organization to select a provider network that can produce the most “value” for an employer. This takes a pretty sophisticated approach and electronic database. How prepared is your practice to deal with these issues?

1. Do you know enough about these issues to respond to a request for service?
2. To negotiate a contract?
3. To determine whether or not to perform such functions yourself?
4. To know if current performance will even allow you to get an invitation to the party?

These are the emerging business issues that must be managed now and over time. Where do dentists find the knowledge, skills and abilities they need to manage these?

Financial Capital – The Driver of Deals

Dental groups and dental networks form the core of any managed dental care system. But many of the dental practices are financially vulnerable to the changing world in which they must practice. Most groups retain no earnings and have little if any reserves. Yet the demand for capital - recognized or not - has never been greater despite the current sub-prime mortgage induced liquidity crunch of 2007-08.
Capital is needed to buy out senior partners, install clinical information systems, restructure and strengthen operating systems, to consolidate or expand practices, to achieve economies of scale in clinic administration, vendor contracting and to finance investments in the software of managed care methods of utilization and quality management.

Where do practitioners find the capital they need? There are three primary sources:

1. Earnings
2. Debt
3. Equity

Most of the practices do not retain earnings and build a cash reserve. The organizational structures and tax laws have not facilitated this, but more importantly, dentists have not applied a mindset of saving to invest in the business and grow its value. It has been more a situation of take as much cash from the business as I can each year (how high is my income rather than how much is my practice worth). There may be a subtle difference but the long-term consequences of these two approaches are significant.

To date, the ability to borrow money for the practice has typically been driven more by the individual dentist’s financial position than the business’s financial position. To be successful in an environment of constrained revenue and unconstrained consumer expectations, the business’s financial position needs to be separated from the owners. The business needs to stand on its own financial merits. The banking community is already recognizing this.

Equity capital is now available to dental practices in the form of venture capital, investment bankers and equity partners. They recognize the need for capital in dental practices and are rushing to bring financial resources and entrepreneurial zeal to a highly fragmented industry of small personal service businesses. They seek profits through the traditional strategy of enhancing revenues while reducing costs but are using methods adapted to the new managed care marketplace. They are targeting specific payer mixes and targeting specific patient groups. They seek contracts that fit their strategy for operations and profitability. They seek volume of a particular kind and at a particular price rather than wait for it to walk through the front door.

At this point you may be asking yourself, why do I need capital and why do I need to get tied up with a business partner? Dental practices need capital for these reasons:

1. Unfunded Liabilities
2. Growth
3. Operations

As dentists begin to join groups, and this trend is growing, they need to pay attention to the ownership governance and capital structure of the business. There are many lessons to be learned from medical colleagues who have been through this already. The lack of retained earnings is problematic when it is time to buy out senior shareholders or to acquire professional management, or to replace old and worn equipment or to invest in information systems. Every business has a capital appetite that needs to be fed regularly. Delaying investments does not make the problem go away; it only makes it more difficult to deal with.
Growing the practice requires capital whether the growth is adding other dentists to the practice or acquiring other practices or even organizing a network to gain access to managed care contracts. Each strategy requires a level of initial and usually sustained capital investment. The growth of new services or new sources of revenue requires the same level of commitment.

Investing in future operations is perhaps the most important use of capital but the area that gets the least attention. This may also be the hardest area to evaluate in terms of “money well spent.” Because operating systems are invisible, or behind the scenes the investment is designed to improve the efficiency and quality of the manner in which the services are provided.

Today, only about 40% of the dental practices are able to submit claims electronically. That number may be irrelevant unless in the future you will be required to submit claims electronically in order to see the patient. When will that happen? How much will it cost to install the capability? How much will it cost to train the staff? How much will it cost to operate and maintain this system? How much will it cost if you do not do this?

There is a host of operating expenses that can be attacked. How much does it cost to deposit checks manually? How much does it cost to have the cash transferred electronically? As you begin to manage your payer mix, you need to build or buy competencies in financial risk assessment, network development, contracting, utilization monitoring, quality management, etc.

You may be saying to yourself: Tell me again why I need to worry about these issues? Why can't I just keep practicing the way I have? There are a number of trends that lead one to conclude that what allowed you to be successful up to this point, may not allow you to continue to be as successful in the future. Not all dentists will be impacted by these trends equally. Some may decide to trade freedom for income by selling for control of their business. The point is that trends create the need for business decisions, not clinical decisions, to either change what you are doing or continue what you are doing. Ignoring trends is also a decision and one that can prove fatal.

Dentists’ real net incomes have increased during the 10-year period 1986 to 1995. The increase was 30.7% or 2.7% annually. And, the last decade exhibited even fast growth. Using real per capital income as a benchmark, it was found that the purchasing power of dentists as a group had increased more rapidly than the purchasing power of the overall US population.

Dentistry, like other professions and industries, is affected by the economy. Inflation, interest rates and other factors, such as the penetration of dental managed care plans, will, in part, determine whether and to what extent dentistry’s upward earnings trend will continue. The critical question is: can this enviable economic trend continue and to what degree? I would offer a strong caution against reaching an absolute yes in response to that question. While growth of revenue, hours worked and increase in operating expenses all appear to be set in the dentists’ favor, what could change that equilibrium? The answer is managed dental care plans. The nature of how you gain access to patients and the price you will be paid for those services is changing.
We know from the 1999 Dental HMO/PPO Industry Profile that network based dental benefits (dental HMO’s and PPO’s) are the fastest growing segment of the dental market with dental PPO’s growing the fastest. There has been significant growth in the total dental benefits market. The total dental benefits market is estimated at 147 million people, or about 55% of the US population (at year-end). The total dental benefits market has been expanding about 4-7% annually for the past decade. As more people are covered by these types of plans, the number of full fee-for-service patients available to your practice is going down. That increases your challenge to sustain profitability because of your ability to attract and keep full fee-for-service patients in your practice.

When you consider the payer source for those covered by dental benefits it is clear that commercial groups dominate. However, there is a significant amount of growth recently in Medicare and Medicaid coverage. Do you know how much of your current revenue comes from each of these sources and what the current trends are? Can you project the trends in order to analyze financial impact? How much of each category of business do you want to serve?

We know that employers pay the majority of the dental benefit costs. Which employers use these plans? What is their future? Is your practice dependent on a single company or single industry? If there were to be a material change in benefits, how would you handle that change in the short run? What business would you replace it with? Can you schedule patients to optimize your profitability given many payment sources and payment rates? Are you prepared to negotiate contracts and prices? Are you prepared to take risk contracts?

The growth of PPO’s has been greater than HMO’s. Are you ready clinically, operationally and financially to accept capitation payments? How will you handle specialty care? Can you demonstrate accountability for your performance that meets the expectations of the buyers of dental care?

At least at this point, all dentists do not face the same challenges to the same degree. Seventy five percent of the dental HMO enrollees are concentrated in 10 states. The dental HMO’s are concentrated in direct proportion to the concentration of the general US population. The top states tend to have active markets in other forms of managed care such as large senior populations and well-developed managed Medicaid systems. Dental seems to grow in these areas because there is a population that is well-educated on managed care concepts. Seventy five percent of the dental PPO enrollment is concentrated in a minority of States. The characteristics are very similar to those in HMO’s.

Dentists and many other practitioners, such as chiropractors and podiatrists, have a unique opportunity because managed care has not penetrated their professions the way it has the traditional medical professions. There is not a lot of traditional insurance coverage much less managed care. How can these professions take advantage of the current circumstances and keep the cash paying customer base? What can they learn from the PPCM experience to date and apply it to their own circumstances? How can they demonstrate accountability that meets customer expectations?
It is clear the health care delivery system in the US has moved from one in which patients had total freedom to choose their physician and hospital to one in which the payer of these services significantly influences the choice and in some cases makes the choice. In many ways this is a story about power in the marketplace. One clear response has been for providers to organize into groups in order to gain leverage with the payers. Dentists have not organized into groups for the most part, and those that have tend to be small when compared to medical colleagues.

The DPMC’s have emerged as a means of facilitating the consolidation of dental practices. They bring professional business management, access to capital and the offer of some consideration for buying the operating assets of the practice. A DPMC is a management and business consultant, a bank, and a buyer all wrapped into one. But it still needs to be recognized as a tool that needs to be used properly by the dental group to advance its position in the marketplace and improve its profitability.

We need to remember this is a personal service business. It is about one dentist seeing one patient at a time. It is not about deals, or mergers and acquisitions, or only top line growth. It is about improving and sustaining the performance of this particular dental practice in this market. Dentists are the “means of production” in dental care. Very little happens without their direct involvement. The health plans and managed care companies cannot treat dental patients. Only the dentist can. If the DPMC tool will not help the dentist improve his profitability over time, do not use it.

**Practice Life after Closing**

When you decide to sell your practice to a DPMC there are several realities that you must come to grips with, preferably before you close the transaction. The most personal issue is what practice life is like when you have a business partner. There will be a loss of control to some degree. You will experience joint ownership, governance and management. The reality is that you are no longer the sole decision-maker. Decisions at many levels within the organization will be shared with the business partner. The decisions must now consider the impact, positive and negative, on both partners. Both must gain real benefit over time to make this type of relationship work.

Before you sign, discuss, understand and be comfortable with the decision making process. If sharing the decision making process is going to be difficult, if not impossible, do not enter into this relationship. Do not think that you can change, or ignore, the established structure of the company. It seldom, if ever works, but trying can be terribly damaging physically, emotionally and financially, not only to you but to your staff as well.

Another issue to consider is how your operations will change. Many are attracted to this business model because they want to achieve economies of scale or they get mesmerized by the size of the check handed over at the closing. Achieving economies of scale requires commitment to the same products from the same vendors. Achieving economies of scale requires a change in behavior on your part and your staff’s part. Too many want the benefit but are unwilling to make the change. You cannot have one without the other. If you cannot make the change or you cannot require your staff to make the change, do not enter into this transaction because you will be disappointed that your expectations are not met. Disappointment can lead to dissatisfaction and ultimately the break up of the relationship. Both partners need to give-in to be successful.
How you assure success after you enter into the relationship is another important issue. If you enter into a typical relationship you will receive cash, convertible notes and stock for the operating assets of your practice. Too often the items you receive are mentally, if not physically, removed from your business and then you question the performance and value of the business partner’s contribution and conclude that you are worse off now than before when you were alone and independent.

Resist the temptation to do that and re-orient your thinking. Focus on the value of the business, and not just income. It is a given that in the short run you will have less income because you will pay a management fee to the DPMC so they can put resources in place to serve your practice. The question and challenge is: How soon can you earn back the management fee?

What if it does not come back? What if your income stayed at the lower level? Is this still a good business decision? It could be. I submit you must take the resources you gain initially and put them to work for you and view them as if they are practice assets. You may in fact not have them held by the practice for tax and estate planning reasons. However, you should consider the value of the asset purchased with the cash, plus the interest earned on the notes, plus the value of the DPMC stock, plus the net income generated by your practice as the full value of your business. Now answer the question: Am I better off in this relationship with the business partner today than I was before as a solo and independent dentist?

In this relationship, the job of both partners is to increase the value of the individual practice in the specific market it serves. If done properly and effectively, the cumulative value of each practice is increased and thus the value of the DPMC is increased. Yes it is easy to write the theory down. No it is not easy to make this work. It is still very challenging to get all of the parts working together, and evaluated with the proper perspective. There are now elements contributing to the value of your business beyond just your income or even just your practice. Owning the stock of a DPMC allows you to diversify your wealth potential into other markets without having to physically be there.

Another reality to consider is that some of your internal management processes will change.

For example, your chart of accounts will be standardized with other practices. This is not done just to antagonize you or show you who is boss, but to facilitate analysis across practices to determine who has the best practice and to facilitate reporting results to investors in the DPMC whether public or private. The budget process and timetable will be done to meet the needs of the group. The list can go on and yet many of these processes are behind the scenes. But your attitude toward the changes will be reflected in the behavior of your staff and their interaction with DPMC staff. If you need absolute control over all of these issues, then do not enter into a relationship with a DPMC. It will be a living hell for everyone.

As a word of caution though, if by joining a DPMC you are required to leave your operating and information systems, etc., there is an economic issue that needs to be addressed before you close. Your own due diligence of the DPMC and what is expected should reveal this situation. Your question is: What do I need to do differently once we close our deal? And how much will it cost to comply?
Assessment

What we have experienced in the marketplace, to date, holds many lessons. Some are clearer than others and some are still emerging.

In essence, the Physician Practice Management sector, regardless of specialty, is not dead; but clearly recovering from a terrible body blow. If we focus on the fundamentals there is no reason why we cannot blend clinical skills with stronger business and management skills and improve the operational and financial performance of dental practices.

When evaluating the various DPMC’s, it is important that you understand the differences of their philosophy and strategy. As your business partner, they must have a strategy for your market. It is not enough to just string together a number of unrelated practices in several markets. Each market needs a strategy that will position you, and probably several other practices, to be attractive and profitable over the long term.

Gaining market dominance and improving your profitability as a practice is the real test of added value from the DPMC. With a proper set of expectations in place, the DPMC can be a very valuable tool to use to help build the value of your practice.

Editor's Note: The insightful reader will note the applicability of this essay to all physicians; not just dentists.
Conclusion

Your peaceful or angst-ridden thoughts and comments are appreciated at:

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