



The Benefits of Using a Qualified Practice Sale Broker

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ABSTRACT A qualified practice sale broker can be useful for facilitating the process of transitioning a dental practice from one dentist to another. This article addresses many of the various factors involved in the sales process and the issues that often arise that can be avoided by being well-informed and/or working with a professional such as a practice sales broker.

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The first step toward finding a qualified practice sales broker is to determine what is important and exactly what outcomes one would like from the process. Some important criteria one may consider include the following items:

Professional credentials. There is nothing more important than education, knowledge, and credentials when selecting a broker. Therefore, investigate the credentials and educational background of the potential broker and choose someone who is qualified, well-educated, and experienced.

Single representation. A practice sale broker should only represent one side of the transaction, either the buyer or the seller. There are numerous legal cases setting forth this principle many of them

stating simply that brokers best serve only one master.

Referrals from other dentists. Referrals from other dentists satisfied with their practice sale broker are a great way to estimate the effectiveness and experience of a broker you are considering hiring and must be one of the considerations given the highest weight by a doctor selecting a broker.

Geographic area of focus. Choose a broker who is familiar with the area where your practice is located. This is important because the broker can better appraise the worth of property in the area and has a better chance of knowing people and having connections in the area, which could lead to the more rapid sale of one's practice. A dentist should generally use a practice sale broker whose sole area of focus is their general geographic vicinity.

Deciding Major Issues

This section addresses some of the most important issues that arise in the transition process. Anticipating and being informed about these issues is important to a smooth and successful transition.

Six major topics are addressed here that include the process of determining an appropriate sales price, creating desirable transaction terms, tackling the negotiation process, analyzing the appropriate type of sale, considering the tax consequences of the sale, and securing a fast sale and closing. Each section is accompanied by tips that are followed by anecdotes of the consequences of being uninformed.

DETERMINING AN APPROPRIATE SALES PRICE

Retiring dentists tend to undervalue their dental practices, which is usually one of their most valuable assets. This may be because a retiring dentist's equipment may be older and fully depreciated, because a doctor does not appropriately understand the value of his or her many years of long work, or for a variety of other reasons. Therefore, an experienced broker can be useful in determining an appropriate sales price because he or she has seen hundreds of transactions and knows how to factor in the numerous variables that go into determining value. This allows a retiring dentist to maximize his or her profit, and usually allows the buyer to obtain 100 percent financing on his or her purchase.

Tip No. 1: Know Your Worth

CASE STUDY

A dentist had been in a partnership with his best friend from dental school for more than 35 years. They had a good working relationship, and when his friend died, the dentist bought out his deceased partner's share of the business from

the estate, according to the terms and conditions of their buy-out agreement. The valuation formula was low, but still reasonable for a partnership buy-out. The surviving dentist increased his workdays from two to four days per week, and this schedule continued for several years after his partner passed away. He began to receive inquiries about a potential sale from new graduates, and using the formula

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from the partnership buy-out agreement, the dentist started to negotiate a sale with two recent graduates. Fortunately, the doctor enlisted the assistance of a practice sale broker to appraise the practice. He soon learned that he had undervalued the practice by approximately 50 percent. Even with that knowledge, however, the doctor still did not really believe his business was worth "that much." The practice was listed and closed within 30 days for more than double what the doctor originally thought his business was worth and the dentist was glad he retained an experienced professional.

CREATING DESIRABLE TRANSACTION TERMS

There are many transaction terms to consider in a dental practice sale and the terms outlines can make a significant overall difference. The best practice transition contracts spell out precisely both parties' understanding and agreement. Tax consequences, covenants, retreat-

ment issues, and trade secret definitions are just a few of the issues that can be precisely determined by a professional broker. A reputable broker with appropriate credentials is very knowledgeable about specific contractual language, the terms and conditions of sale, and is able to properly advise the selling dentist.

Tip No. 2: Get it in Writing

CASE LAW EXAMPLE

Failure to establish specific and detailed transaction terms often leads to the need for legal resolution. The case of James E. Gernert, MD, et al. vs. Duane Hartleip, MD, et al. (L.A. Superior Central, BC 126513) provides an interesting example as to what happens when there is a lack of specificity in practice sale contracts. Dr. Hartleip sold his urology practice to Dr. Gernert in preparation for retirement. The deal turned ugly after the transaction closed. Dr. Gernert alleged that Dr. Hartleip breached the covenant not to compete, stole patients, defamed him, and unfairly competed against him in a nearby area. Dr. Gernert further alleged that Dr. Hartleip had promised to retire. However, the sales contract failed to mention most of the issues the parties found themselves facing.

On the face of the contract, Dr. Hartleip allegedly complied with all of the terms and conditions, however, according to Dr. Gernert, none of the promises were kept and the "spirit" of the contract was breached. The court rendered a defense verdict in favor of Dr. Hartleip, with an allowance for attorney's fees. The court essentially found that the written words of the document prevailed and no verbal evidence was admitted for consideration. The court found that particularly between two educated parties of equal bargaining power, a "deal was a deal" and the contract.

TACKLING THE NEGOTIATION PROCESS

A thorough understanding of the main transaction points and the importance of bargaining are necessary to achieve the best transaction. An experienced broker with appropriate credentials can competently negotiate the various aspects of the transaction, factoring in specific items, and knowing when and what to give and take. The covenants set forth in the agreement are particularly important, whether there is merely a covenant not to compete, or additionally a covenant not to solicit, a covenant not to treat, and a covenant not to hire employees, requires sophisticated negotiation skills and may make or break the transaction.

Tip No. 3: Negotiate and Document

CASE LAW EXAMPLE

The case of Wallace, MD, vs. Cooperman, MD, decided in Los Angeles Superior Court on Dec. 11, 1995, illustrated the importance of adequately negotiating and documenting a practice sales transaction. Dr. Wallace purchased Dr. Cooperman's ophthalmology practice in 1989. Dr. Wallace subsequently sued Dr. Cooperman stating the practice was misrepresented as being more profitable than it was in reality.

Dr. Cooperman contended that Dr. Wallace's lack of success was due to increased competition from HMOs, that Dr. Wallace failed to advertise the practice and develop relationships with referring doctors, and that Dr. Wallace's personality had alienated the patients. After a lengthy jury trial, the court agreed with Dr. Cooperman. The parties should have completely negotiated and put in writing all the terms and conditions of their agreement. Therefore, complications like these can be eliminated and provide both the seller and buyer with peace of mind with the help

of the services of a professional broker who has experienced negotiation skills and expertise in formulating contracts.

DETERMINE THE APPROPRIATE TYPE OF SALE

Practice transitions come in various forms. For example, it may involve a phased transition, a partnership leading to full buy-in, a straight sale, or a combination of these things. An

THE TAX CONSEQUENCES

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experienced broker can be useful for evaluating a doctor's needs and desires and determining the best type of transition for that particular doctor.

Tip No. 4: Specialization is Key

CASE STUDY

A doctor retained a transition firm based outside of California to handle his transition. He paid a relatively large upfront cost for an appraisal and then another upfront cost for a "standard" contract. The doctor found himself a potential buyer, that person started employment as an associate, which led to a partnership and then a full buy-out. The doctor soon found out the firm was not versed in California law, that the covenant not to compete sections were not in accordance with California law, and there were numerous problems with the contract.

He then decided to hire an expe-

rienced broker and found out that his practice was undervalued for the California market by about \$175,000 and that the document created by the transition firm he had hired, which he paid thousand of dollars for was basically worthless. It was an expensive lesson to learn but the sale was eventually consummated on terms and at a price the doctor was very happy with once he had the assistance of a professional broker who specializes in such transactions.

CONSIDERATION OF TAX CONSEQUENCES OF THE SALE

The tax consequences of a sales transaction are extremely important to a selling and purchasing dentist. The allocation of the sales price determines the actual net for the seller and tax depreciation and amortization schedule for the buyer. Generally, the amount of the sales price allocated to goodwill is taxed to the seller at the capital gains rate and the rest of the sales price is taxed at the seller's ordinary income rate, generally at least double that capital gains rate.

Although the buyer can fully amortize and depreciate an asset purchase, the allocation schedule determines the speed at which those deductions can occur. Other tax consequences also must be considered, including a doctor's plan to purchase another practice and utilize a 1031 exchange, or a doctor's ability to sell stock rather than assets of his practice.

Tip No. 5: Pay Attention to Taxable Entities

CASE STUDY

A doctor spent most of his career in an outlying area developing a successful dental practice. After his children moved out of the house, the doctor and

his wife decided to relocate to a beach city and find a small practice to work a couple days a week and ease happily into retirement. The doctor successfully entered escrow with his longstanding practice and made an offer to purchase his dream beach practice. The doctor's representatives failed to mention the benefits the doctor would derive from a 1031 exchange. Three-hundred thousand dollars was allocated to that equipment and that amount was taxable ordinary income to the doctor. The doctor could have exchanged with the amount allocated to equipment

for his Southern California purchase and avoided that current tax burden if he had been properly represented.

SECURING A SPEEDING SALE AND CLOSING

Time is an important factor in selling a dental practice, especially in the event of a death, disability, or illness. An experienced broker has an extensive and detailed database of buyers. This database is generally obtained by a broker's contact and participation with dental schools, dental meetings, through speaking, which gives the broker access to new graduates and buyers.

Tip No. 6: Watch Out for the Details

CASE STUDY

A dentist developed a very successful practice over the past 30 years. Collections exceeded \$1.5 million per year and the practice was broad-based and attracted about 35 new patients per month. The doctor was nearing retirement age and he began to receive unsolicited phone calls and mailings from practice sale brokers and recent graduates. He was a savvy businessman and decided that since he had numerous potential offerees, he would handle the transaction himself with the assistance from a local attorney. The transaction went relatively smoothly, although it took about six months. About a year after the closing and after attending a convention and talking to several of his friends, the doctor realized he had included his accounts receivable in the sales price, which had steadily crept up after his decision to sell. This one item cost the doctor approximately \$200,000.

Celebrate Your Transition

Transitioning a dental practice is a multifaceted and intricate process, so having the right knowledge and information is crucial. The use of a qualified practice sales broker with the appropriate credentials and knowledge can help ensure a smooth transaction and lend peace of mind that all goals were met and bases were covered in the process. ■■■■

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