The passive income practice

Author_Dr Phillip Palmer, Australia

Photos: Yuri Arcurs

_Exit planning has traditionally been a fairly simple task for dentists. The choices a dentist faced were either winding down the number of days worked, thereby gradually easing into retirement, or working until three to six months before wanting to stop, and then advertising the practice for sale. After negotiations with the buyer, dentists would sell and walk away—much like a house sale. Sometimes there would be a good handover of patients and staff, and sometimes this process would be less than ideal.

More recently, other options for exit planning have become available for practice owners. Over the last three to four years, for example, many dentists in Australia having sold their practices stayed on to work as employee dentists for the new owner. This model in particular has increased in popularity recently with corporate entities often being the buyer. Another model is deferred sale/employee with view, whereby a new dentist (Dr Junior) works for a year as an employee for Dr Senior. If all goes well, a contract is signed for the purchase of half (or even all)

the practice in some years hence. The employed dentist continues to work as an associate, and the transaction is settled after the agreed time. This technique assures Dr Senior both a buyer and extra income from Dr Junior during the years as an employee. Through the incremental percentage technique, after a similar trial period, the practice contracts are exchanged and incrementally each year a further percentage of the practice changes hands from Dr Senior to Dr Junior.

In each case, after the practice is sold, the ex-owner commonly takes the money he made from the sale, goes on a holiday and then invests whatever is left in real estate or the stock market to fund his retirement. For a practice here in Australia grossing say AUS$800,000 per year, if sold on the open market could bring up to AUS$500,000. If that entire sum were used to purchase a residential investment property, one would be lucky to net more than AUS$30,000 per year, and probably less, to fund retirement.

Another way to exit plan and fund a dentist's retirement is to establish the passive income practice, also known as the "never sell concept". Using this method, the practice is set up in such a way as to be self-managed, with little effort (1 day/month) needed from the owner when the practice is mature. The profit from the practice can be as high as 30 % after payment of all normal expenses and clinicians' wages.

If maintained as a going concern and run properly, there is no reason to expect a return from the AUS$800,000 grossing practice of less than AUS$200,000 p.a. (and still maintain an asset worth at least AUS$500,000).

Obviously, for this option to work, the practice and the staff need to be trained to be self-managed and to provide a certain level of service and communication. Basically, they would need to have a deep knowledge and understanding of the systems needed to run a practice.

Some degree (the more, the better) of management, leadership and business skills is also required by the owner, including the ability to look at and analyse the right numbers or to motivate key staff members to manage the practice and outperform through the judicious use of incentives, including well-designed bonus systems. As the owner dentist is no longer present full-time in the passive income practice, there also needs to be regular training in communication and the provision of service, i.e. clinical training.

There definitely needs to be more than one clinician. Rarely is there sufficient profit over and above the employee dentist's wage (40 % after lab) to warrant running the practice as a business with such a small staff.

There are plenty of horror stories out there, especially after the global financial crisis, of retired dentists needing to return to practice because the practice sale did not fund their retirement the way they expected it to. The never sell concept represents a new way of looking at the asset that is your practice and how it can bring you returns long after your clinical career comes to an end._

_about the author

CAD/CAM

Former dentist **Dr Phillip Palmer** is currently Director of Prime Practice and Dentist Job Search and regarded as Australia's leading expert in the business of dentistry.
He can be contacted at info@primepractice.com.au.