The practices that invisible DSOs value most

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THE MUTUAL GOAL of a doctor with an invisible dental support organization (IDSO) is to accelerate practice growth and profitability using the silent partner's extensive resources and the doctor's proven brand leadership and management. IDSOs now quietly own parts of thousands of practices across the country and new IDSOs are being formed every month. This is not a fad. It is accelerating. Over $300,000,000 in these transactions will be closed in the next quarter.

NOW IS THE TIME TO UNDERSTAND THE IDSO OPTION

These silent yet active dental support organizations (DSOs) are now officially operating in all 50 states. We know because we at Large Practice Sales just sold a large specialty practice that operates in the two Western states that were holding out on the idea of an IDSO. This practice achieved a value of about three times annual collections and is a microcosm of what an IDSO values most in a partner.

PRACTICE PROFILE

The practice doctors are in their early 60s, 40s, and 30s. The practice is growing both top and bottom lines at over 10% per year. The team turnover is low, the margins are high, and the patient satisfaction surveys are superior to all others in their region. The practice's new IDSO partner believes that its infrastructure and resources will enable the practice to grow even faster. The doctors are excited to offload much of the daily administrative burdens and focus more on patient care and satisfaction.

The transaction was fairly typical, with the doctors selling 70% of the practice for cash now (at favorable tax rates) and the owner doctors retaining equity in the practice and in the acquiring partner. In addition, a path was created for the associate doctors to become owners. As a group, all of the doctors have significant upside profit opportunity from the retained equity in their practice, but also a potentially larger long-term gain from the value created when the acquiring partner sells or recapitalizes in the future.

Author's note: Read previous articles about invisible dental support organizations (IDSOs) in the May and September 2019 issues of *Dental Economics*. For more than three decades, IDSOs have been quietly buying interests in dental practices of all specialties across the US. These silent partners allow doctors to cash out part of the value of their life's work today and continue growing their practices under the doctor's leadership, team, and local brand.

ORGANIZED SYSTEMS ARE CRITICAL

While higher collections and strong net profits are an important part of the value puzzle, one of the first items that a prospective IDSO partner (or any partner/buyer) will look for is the quality of the accounting and operating systems. IDSOs will functionally test a practice's systems (and your advisor) by asking for a long series of reports and data points early in the discovery process. While the requested data is relevant, equally important is its accuracy and the speed at which it can be obtained. Quality data also becomes important after a letter of intent is signed and the quality of earnings (QoE) process of due diligence commences, a critical piece in obtaining maximum value for a practice. Practices and advisors that fumble this first test are in many cases doomed to lower values.

Bottom line: Make sure your accounting is current and correct. You should be able to provide profit and loss statements within 10 days of the end of the previous month.

THE DOCTOR MATTERS

Practice profitability, growth rate, and low team turnover are all drivers of value. But without exception the highest valued practices—the ones achieving values of two, three, and even four times collections—are those with great doctors. All IDSOs make the initial assumption that the doctor is a better-than-average clinician. The key drivers of higher values are doctors with a personality, a plan, and a history of adapting to changes and driving growth, even in difficult times. High-value doctors are those who are knowledgeable about their practice metrics and the numbers that drive practice measurement and improvement.

In our Western practice case above, the founding doctors built the practice in part through acquisitions of smaller practices. They successfully recruited, trained, and retained associates. They adapted the "product mix" over the years to meet changing patient care demands with the most desirable and highest margin procedures. The practice is leading edge in its technology adoption, but not bleeding edge.

The doctors are all active in, and officers of, their state and regional associations and have created relationships with other doctors in the area. They have a written growth plan for the next five years and are personable and enjoyable people (not just doctors) with whom to socialize.

BELIEVERS IN THE FUTURE, YET COGNIZANT OF COMING CHANGE

Due to their location, this particular group is relatively insulated from an onslaught of nationally branded DSOs disrupting the market with lower fees and dominant marketing. However, the doctors can elucidate to prospective partners why and how they feel the industry is changing, and why they want to be prepared now, not later, for the inevitable consolidation and competition.

The doctors made it clear to prospective partners that their goal was not just a transaction to put millions of dollars in their pockets and slow down. Their primary goal was the defensive and offensive desire to benefit from the resources of a large, national partner to protect and accelerate growth. In the doctors' view, the beneficial partner resources include lower supplies costs, better and less expensive team benefits, leverage in payer negotiations, and most importantly, professional marketing. As a bonus, they hope to reduce time spent on administrative minutiae and human resources and recruiting issues. The doctors are also intrigued by the potential upside of their equity ownership in their IDSO partner.

AN INTERESTING TWIST ON PRACTICE REAL ESTATE

In many large, more profitable dental practices, the doctors own the real estate. A fancy, expensive office is not required to get a blockbuster value, and IDSOs do not typically buy practice real estate. In the example above, the doctors owned part and leased part of their offices. However, IDSO practice transactions result in doctors with two options for their properties, both of them good.

The first is that the new partners enter into a long-term lease on the real estate, ensuring the doctors have a reliable income stream, indexed for inflation, from a AAA credit quality national tenant for many years into the future.

In the second option, the real estate is now more valuable to an outside investor due to the credit quality of the new tenant. In many transactions, it is arranged to concurrently sell the practice real estate to an investor. In this case, we negotiated the lease to meet the standard terms desired by real estate investment trusts in the event the doctors decide to monetize the properties in the future. This one often-forgotten piece of a transaction potentially adds seven figures of additional value for doctors, on top of their extraordinary practice value today.

SUMMARY

Partnering with an IDSO is not for every doctor. But for those who believe the industry is changing and could benefit from a silent partner, a guaranteed future exit, and millions in cash now, it is worth understanding the potential value of your practice to an IDSO today. Why not? DE

Editor's note: Want to stay in the loop about DSO trends and strategies for growing multiple practices? Subscribe to *Group Practice and DSO Digest*, a monthly newsletter from *Dental Economics*, at dentaleconomics.com/subscribe.

CHIP FICHTNER is the founder of Large Practice Sales, which specializes in invisible DSO transactions for large practices of all specialties. The company has completed more than $100 million of transactions in the last six months. Learn more at largepracticesales.com.