Crash Craddock vs Eddie Cool: The financial ups and downs of two talented dentists

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"Most dentists have fewer years of high productivity than they realise. If they embark on a wrong business strategy, there is usually insufficient time to rectify matters and create substantial wealth from dentistry..."

Christopher Craddock, known to his dental class as 'Crash', was very ambitious. His classmate Eddie Cool, known to his class as 'Steady Eddie', or after a time simply as 'Steddie', was ambitious but in a more methodical way. Both were good students and their fellow graduates expected both to do well. Both were able to gain employment in well-run, profitable practices and gained good experience during the first few years after graduation. Both connected well with patients. Crash tended towards high-quality restorative dentistry with an element of cosmetic. Steddie was more traditional in his approach.

Buying an associateship

Crash bought an associateship with an older dentist but quickly outperformed and inevitably bought the older man out. Almost simultaneously, he purchased the premises, which were located near substantial offices on a major artery leading toward the central business district.

Steddie bought an associateship and a share of premises in a sound but not spectacular suburban practice and he too quickly outperformed his associates, eventually negotiating a split of the practice and running his own practice in a nearby suburb.

Crash lived and breathed dentistry and his wife Jane, a podiatrist, gave up her profession to help steer the practice, as well as looking after their children. Jane was even more ambitious than Crash. The practice was well-presented and while the two employed dentists were well booked, it was in reality Crash's own surgery which produced over 90% of the profit. Jane's close friend, a marketing consultant, pushed her to an elegant web design and the practice, which was well presented, looked even better on the internet. Crash and Jane were able to buy adjoining office suites and add a further dentist and hygienist. The fees were rocketing, but a close observer would have noticed that Crash was working at a frantic pace, while the new dentist and hygienist could not be coaxed into the fast lane, despite Jane's entreaties. The existing two employee dentists appeared to be in a comfort zone. Crash was so busy in his own surgery that he barely had time to do more than occasionally greet the employed dentists or hygienist. Jane set out to coach the other fee income generators. She was skilled in her presentation manner and couched her words carefully, but lofty sentences about meeting clients' expectations did not quite ring true. The other dentists sensed that her real motivation was the bottom line rather than concern about patients. She was regarded as being motivated by greed. Still the gross fees had rocketed and the profit was impressive. Jane herself did not realise that if proper cost accounting methods were applied, about 93% of the actual profit was coming from Crash's surgery. The fees being generated in the practice were now as follows:

Crash's surgery	$1,500,000
Most experienced employed dentist (Geoffrey)	$600,000
Second employed dentist (Louise)	$550,000
Third employed dentist (Andrew)	$400,000
Hygienist	$250,000
Total	**$3,300,000**

It was apparent that Crash was an outstanding clinician with great hands and that he generated confidence in patients. His fees of $1.5 million easily put him within the top two percent of Australian fee generators in their personal surgery. A close observance of his behaviour would have revealed that he was showing signs of stress, but Crash and Jane were both still of an age where they looked upon themselves as indestructible. Jane, urged on by her marketing friend, set out to clone Crash's practice by purchasing other suburban practices. She was confident that she had discovered the secret of making money via dentistry and that she could replicate what was occurring in the practice elsewhere.

Megabank rushes to lend

The medical arm of Megabank had rarely seen figures like Crash's and they rushed to lend money. Because Crash's profits were very high by dental standards, Crash and Jane were eager to upgrade their home from one worth about $1 million to one worth about $3 million. Megabank financed this along with an almost simultaneous purchase of a very expensive holiday house in a prestigious seaside location. Crash and Jane quickly ended up with $3.5 million of personal debt, on which the interest was not tax deductible.

Building a mega practice group

Jane had become used to good profits and had been focused on the gross fees. She tended to overlook the fact that in a practice with rapidly growing profit, taxation was always going to bite heavily. Jane and her marketing friend were on a mission and spoke to each other disparagingly about the blindness of dentists and how they would build a mega practice group into a high profit enterprise. Crash had misgivings, but events were taking control of his life. His own frantic style of practice meant that he had insufficient time to properly work with and supervise the other dentists in the practice, a couple of whom would have greatly benefited from taking on Crash's clinical management skills. He was generally too exhausted to pay much attention to them and they were feeling cast aside. Meanwhile Jane was on the hunt for practices and she quickly bought second, third and fourth practices financed by Megabank. Along the way, Crash and Jane had acquired and shed accountants, solicitors and advisers in quick succession, never having time to seek or comprehend proper advice. When they wanted something done, it was done quickly and decisions were taken in a haphazard manner.

Warning signs

A closer observer might have realised that Crash was exhausted at the end of every day and when he was confronted with a question from an adviser or accountant in the odd minute or two between patients, he tended to give incomplete answers. Jane always blamed the advisers or accountants and they changed several times. Accountants noticed that emails on financial matters contained gaps and incomplete sentences. They seemed to have been written in haste and sometimes requests for information went unanswered. Emails from Jane did not always gel with emails from Crash. The general feeling was 'if that ship is going to sink, I hope it won't be on my watch'.

Borrow the client's watch to tell the time

Jane, in particular, was ruthless when it came to moving on from any hint of advice that was critical of anything that she proposed doing. Inevitably they arrived at the door of a major national and international accounting firm, 'Big Firm'. A Big Firm partner had dazzled them with stories of how various businesses had grown at fantastic rates; presumably because of Big Firm's involvement. In actual fact, Big Firm dealt with hardly any dentists and the only dentist known by the partner who dazzled Jane was the one who drilled her teeth. Big Firm's clients were mainly businesses turning over many millions of dollars. Big Firm's trappings were impressive and they certainly impressed Crash and Jane; Jane in particular. The Big Firm partner was astute enough to realise that Jane was driving Crash's business affairs and that while she sensed that she had too shallow an understanding, she also sensed the potential for big firm to make substantial fees; fees far in excess of what previous advisers and accountants had charged them. Big Firm's internal mantra was <i>'borrow the new client's watch, then tell them the time'.</i> Big Firm was careful to draw out Jane and Crash's ambitions and where they would like to take the practice. The information was then represented to Crash and Jane with a bit of embellishment and examples of quite dissimilar businesses whose owners had achieved spectacular success. Jane's instant reaction was that Big Firm was wonderful. It seemed to have all the answers. The Big Firm partner was skilful at feeding back information to clients in ways which endorsed the clients' own thoughts and plans, but suggested that Big Firm was the vehicle to take them to their destination. Big Firm actually didn't have any reliable benchmarking data on dentists and didn't notice the misdistribution of fees in the practice. To Big Firm, dentists were all alike. They looked upon them as technicians who drilled people's teeth and were unaware of the vast differences across the profession. The Big Firm partner smelled a rich vein of ongoing activity and consulting fees. She promised Jane and Crash that Big Firm had all of their business answers, because it was in the big league.

If Crash and Jane had looked closely, they might have realised that of the dental corporates, the one which had the best results had grown carefully from an inauspicious beginning in a regional city and had carefully controlled its expansion and limited its debt.

Steddie expands

Out in the suburbs, Steddie, after separating his associateship, initially set up in rented premises which were less than ideal. However, he looked carefully for a suitable site on which to develop practice premises. Steddie was involved in a local theatre group and was written up in the local press for his leading roles in amateur Shakespearian productions. He became known locally as 'the Shakespearian dentist'. His wife Mamie shared a love of Shakespeare and of music. People naturally warmed to both of them. Steddie's fees grew readily and he had taken on an employed dentist. He and the practice received lots of referrals.

It took several years but eventually they found a suitable site with a derelict building on which they planned modern dental premises with three surgeries. The design was functional but not lavish and was in keeping with the surrounding area. There was space for a fourth, which was plumbed and wired but not equipped and Steddie used it as an office. He too built a practice around himself, but he also inspired his full-time assistant to stretch her talents. A third dentist was part-time. Steddie realised that he was the major fee and profit generator, but Natalie, the second dentist, produced a reasonable margin. Mike, the part-time third dentist, appeared to lack some drive to extend himself and was happy to work a two and a half day week. However Mike fitted in well.

Mamie had involved herself in the design and building of the premises and while Steddie had continued to practice from rented premises, Mamie had taken on the job of supervising the new premises project. She had a talent for getting good results. Her personal skills were such that subcontractors seemed to be willing to reduce their quotes. Somehow she managed to bring the project to completion ahead of normal time, whilst maintaining the respect of the builders and various subcontractors. From purchase of the site to the opening of the new premises took a couple of years but Steddie's practice continued to grow in rental premises and patients were pleased that the new premises were being built.

The move into the new premises went well and their numerous patients and friends from local theatre and music circles were pleased at their achievement.

Two gun shearers

Steddie was the gun shearer in his practice just as Crash was in his. Whereas Crash was driving himself at a frantic pace, Steddie, who did about 65% of the fees of Crash (a not inconsiderable achievement), was usually smiling at the end of the day.

Steddie and Mamie upgraded their home too, but their debt was far less than that of Crash and Jane and within a relatively short time, their only borrowings were business related. They were content to use rented accommodation when they went on holiday. Crash and Jane's mansion by the sea was in reality only used for a small amount of the available time. Since it wasn't rented, the interest on the borrowings was not tax deductible and had a much greater impact on their finances than they had realised when they rushed to buy it.

There were also worrying signs of a decline in the real estate market. Houses in their prestigious suburb were having trouble meeting reserve at auctions. Some were passed in and some were withdrawn from sale. It was now highly unlikely that they could have sold either their house or their beach property at anything like the price that they had paid.

Methodical approach

Steddie was content to build his practice in the one location and he went about it in a methodical way. He had maintained the ability to manage his staff. Mamie had the wisdom and tact to be discreet about her influence in the practice and hardly ever visited the practice during work hours. She did a significant amount of work behind the scenes, comparing dental pricing through surrounding suburbs and ensuring that any written material that the practice put out was tactful and discreet. When she met the staff at the practice's Christmas night out, she was personally interested in them and their partners.

Crash losing sight of reality

Crash and Jane didn't realise it, but Crash was rapidly losing sight of what was occurring in the surgeries of his employed clinical staff at his headquarter location and he had almost no contact with those at the recently purchased practice sites. Jane and her marketing buddy had been too keen to buy the additional practices and in particular had bought the third and fourth practice before they had time to bed down the staff and procedures in the second. Jane's biggest problem was that she had assumed that there were many dentists like Crash who could work at his pace and produce his quality of work. She rapidly learned that dentists of that calibre had long been running their own practices and that dentists of average ability but good presentation skills, who were capable of working without clinical supervision, were also hard to find. She had difficulty in recruiting the right type of dentist to fill their new practices. Many dentists had discussed employment with them and of those who had a profile which suggested that they might be good dental employees, most after speaking to Jane and looking at the practices decided to take up employment elsewhere. Yet to Jane the ability for her to buy those practices in a market where good practices were hard to acquire had seemed to be too good to be true. The truth was that they were able to make the purchases because she had paid well above their market value.

Steddie runs one practice well

Meanwhile, Steddie and Mamie had no intention of acquiring additional dental practices. They were content to run one practice well, in good premises and to build and maintain a reliable clientele, which grew steadily. Patients had the confidence in the practice to refer their friends.

Each of the three additional practices acquired by Crash and Jane were of about a one and a half dentist size, with the outgoing dentist employed to work part-time for them for six months to facilitate handover. It was not possible for Crash to work in any of those practices since he was now generating $1.8 million of fees from parallel surgeries at their original practice.

Had a cost accountant gone around the entirety of their practices, he would have found that:

- There was an enormous profit margin in the two surgeries that Crash operated;
- A couple of the dentists at the headquarter location produced a reasonable profit margin, one of about 13% of fees and the second of about 8% of fees. The other dentist and hygienist at that location would, if properly accounted for, been found to be at best breaking even;

- The first of their three newer practices, since it had come online a couple of months ahead of the other two, had benefited from the marketing effort, but was struggling to pay its expenses and the interest bill related to its purchase. This practice was barely breaking even. The vendor dentist was developing a distaste for Jane's management style and had decided to move on at the end of his contractual obligations, which ended six months after purchase.
- The second of the newer practices had staffing problems from the beginning and for several months the only dentist was the vendor dentist who was working three days per week and not prepared to work more. He could see that the practice was falling apart, but it wasn't his duty to recruit other dentists. When she visited the practices, Jane was not interested in listening to advice that he offered and he ceased making any response to her comments. Whilst eventually Jane found a dentist to fill a second surgery and in due course a dentist to replace the vendor, a significant wastage of the good client base of this practice had occurred. Clients attracted by marketing did not have the same long-term loyalty and many left because the dentists recruited were not up to the expected standard.
- The third practice that they had purchased was a disaster from day one. The vendor dentist went through the motions of working a three day week for a period of six months. His employed dentist quickly realised that there was no future working for what was, in effect, a mini corporate and departed. The good receptionist quickly became tired of apologising to existing patients for being unable to fit them into appointments. She realised that the practice was falling apart and she too departed for employment in a well-conducted practice. The second dentist's experienced chairside nurse departed at the same time as he. The practice began racking up a substantial monthly loss.

Crash slides towards a financial crisis

Crash had grown rapidly and hadn't properly factored in payroll tax, nor had he realised the extent to which a significant jump in dental profit in one year led to a hefty tax bill and a leap in PAYG tax instalments in the following year.

Interest rates had crept up a couple of notches and the payments on their home and holiday home was taking a substantial amount of their post-tax income.

Crash had borrowed heavily to acquire practices two, three and four at Jane's bidding and then had paid for expensive new fit-outs and replaced aged equipment in order that those practices could meet the presentation standards required by the head practice's website. Each of these practices had now cost far more than they could be sold for in the dental marketplace.

The overall size of their borrowings meant that they were categorised for special review inside Megabank, which marked their file as having too much risk exposure. Megabank indicated that it wanted their loans reduced.

Steddie's financials were in such good order that his bankers only gave his file the briefest of checks. Indeed, they wished that they could lend more because he was an A-list borrower.

The financial world closes in

In the early stages of their relationship, Megabank had invited Crash and Jane to various business forums where owners of businesses network. Crash was always too busy to attend, but Jane attended a few and got a buzz out of being invited to mix with such exalted company. Lately she noticed that those invitations had dried up. Steddie and Mamie hadn't needed to borrow sufficient funds to attract this higher level grooming.

Similarly, Big Firm had included them in its invitations to various business forums and again Crash had been unable to attend but Jane had been delighted to. Big Firm's business strategy networking meetings had been exhilarating, however just as Megabank's invitations dried up, so too did Big Firm's. Behind the scenes, Big Firm had asked their accountants to prepare additional information. Big Firm recognised the symptoms. By this stage Crash and Jane had found out that the actual accountants doing their work always wanted the same information as all of the other previous accountants they had dealt with and produced the results in a similar manner, but they were presented in classier folders and they came with much bigger invoices. Big Firm's charge out rates were astronomical. Crash was too busy to deal with the accounting detail, but when Jane asked for more detailed information about dentists and dental incomes she discovered that there was apparently nobody in Big Firm who actually dealt with dentists. Sheila, the Big Firm partner who had delighted Jane at first, was now always too busy to talk to her and her enquiries were diverted to Bob. Bob suggested that Crash and Jane were carrying too much debt. Whereas Jane had been expecting an innovative solution, all Bob could say was: *"I'm advising you to sell some assets quickly and reduce debt before Megabank steps in and forces you to make unpleasant decisions under duress"*.

Jane and Crash now contemplated their options:

1. They first of all made enquiries about selling their beach house. While it had cost nearly $2 million, the agents now advised that just as the housing market across the city had fallen sharply, lifestyle properties had fallen further than suburban homes. They were told if they wanted a quick sale they could expect no more than $1.3 million. After factoring in buying and selling costs, that meant a loss of $800,000 not counting the interest carrying costs.
2. Next they decided to sell practices two, three and four but were told that they had overpaid substantially for the practices prior to expending an average of $400,000 each on updating fit-out and equipment. Sale would have meant paying out leases. On average, a break-even sale for each of the practices would have required them to receive $1.1 million, but the practice valuer they consulted told them that they might get $550,000 to $600,000 for the best of the three and less for the others.
3. Finally, very reluctantly, they called in several agents for opinions as to the value of their home. It had cost almost $3 million but they were advised that in a weaker market it could probably sell for $2.3 million. After factoring in the stamp duty on acquisition and the various selling costs, they were looking at a loss of around $1 million, which happened to be the equity they had put into it from the sale of their previous home. On top of that, they had had to pay interest on a housing debt of about $2.1 million for several years.

Steddie's financial position continues to improve

Meanwhile Steddie and Mamie had no debt on their home. They were advised that the likely resale value of their dental practice and premises was now substantially greater than the cost of these assets. Their superannuation fund was growing nicely and the cost of interest on their business borrowings was covered many times over by their earnings. They were making additional non tax deductible contributions into their superannuation fund and they were regularly asked by their bankers whether they needed additional finance for equipment, upgrading motor vehicles or home improvements. However they were content to maintain a lifestyle which was not ostentatious and most of their practice equipment was of recent origin, having been acquired at the time of the fit-out of the premises. Steddie was capable of working faster, but had found a level which suited him whilst giving him sufficient time to mentor Natalie and Mike. There was no practice manager at Steddie's but a small team of support staff shared the administration and kept the patient book in good order. He was able to keep a quiet eye on that as well. Steddie and Mamie still involved themselves with the theatre group and were looked upon as community minded within the wider area. Patients came to their practice from a number of surrounding suburbs.

Update on Crash's Practice

Crash's practice now looked like this:

Headquarter practice fees:

Crash's surgery	$1,800,000
Geoffrey's surgery	$625,000
Louise's surgery	$570,000
Andrew's surgery	$415,000
Hygienist	$275,000
Total	**$3,685,000**

The profit was $1,283,100 but if proper cost allocations were made, $1,170,000 of this came from the dual surgeries which Crash worked personally. Crash was providing almost as much of the gross fees as the rest of the practice combined and 91% of the profit in the headquarter practice. In the past two years, despite Jane's coaxing, their employed dentists and hygienists had barely changed their output. Everything around Crash's twin surgeries moved near perfectly and he did high quality work at very high charge-out rates. He was at the absolute zenith of his clinical career.

Number two practice fees:

Senior dentist	$500,000
Second dentist (three days per week)	$300,000
Part-time hygienist	$100,000
Total	**$900,000**

After assignment of leasing costs on new equipment and fit-out, interest costs on the practice purchase and its share of the administrative and advisory overheads, this practice broke even.

Number three practice:

Senior dentist (three and a half days)	$400,000
Second dentist (two days)	$180,000
Part-time hygienist (half day)	$50,000
Total	**$630,000**

After factoring in interest and leasing costs, marketing and administrative overhead costs, this practice was losing $90,000 pa.

Number four practice:

One dentist (four days)	$455,000

After factoring interest and leasing costs, marketing costs and administrative costs, and maintaining a chairside assistant and full-time receptionist, this practice was losing $150,000 per annum.

Summary of profits:

Number one practice	$1,283,100
Number two practice	$0
Number three practice loss	($90,000)
Number four practice loss	($150,000)
Combined profit	**$1,043,100**

This was less than the profit had been on Crash's own surgery. In reality, his and Jane's strategy had created an elaborate employment network of dentists, hygienists, chairside assistants and practice receptionists, nearly all of which was unprofitable.

Crash visits his doctor

Crash was feeling the strain and he saw his doctor who sent him for tests and referred him to specialists. He was told that:

1. He needed a longish holiday; and
2. He had to reduce his workload significantly.

If he didn't take these steps, a serious breakdown in his physical and mental health was likely.

Update of Steddie's Practice

Steddie's fees now looked like this:

Steddie's surgery	$1,100,000
Natalie's surgery	$700,000
Mike's surgery (three and a half days)	$375,000
Total	**$2,175,000**

The profit looked like this:

Profit on Steddie's surgery	$762,000
Profit on Natalie's surgery	$112,000
Profit on Mike's surgery	$37,500
Total	**$911,500**

Steddie and Mamie had no personal non tax deductible debt and interest on all borrowings and chattel mortgages was included within the practice expenses. The rent paid on practice premises equated to the interest cost on the mortgage. They had a growing superannuation fund. Steddie and Mamie were in good financial shape and in good health.

The effect of personal debt on Crash

Crash and Jane had $3,500,000 of mortgage debt on their home and beach house, which was financed on a principal and interest reducing loan over 25 years at 7.5%. This required monthly payments at $25,704 or $308,448 per annum, which came out of their after tax income.

At a marginal tax and Medicare rate of 46.5%, the $308,448 of payments on this finance accounted for $576,539 of their pre-tax profit and since more than 100% of the pre-tax profit was due to Crash's extraordinary personal fee generating ability, the pressure on him was great indeed.

Along their journey, Crash and Jane had cast aside advisers who had counselled them against a too rapid expansion away from their primary site, but Jane in particular was deaf to that message and Crash was willing to let her have her way while they seemed to be in the ascendancy.

They now knew that they were under closer scrutiny at Megabank and they sensed that the Big Firm partner who had sold them its services now had little interest. She was adept at distancing herself from clients with potential problems. Bob, who was now dealing with them, counselled them in strong terms to take action before Megabank told them to. He told them horror stories of banks requiring quarterly reviews, forced asset sales and applying penalty interest rates, all of which pushed clients into a deeper quagmire.

Jane and Crash were also finding that their own relationship was becoming brittle under the financial pressures that they had brought upon themselves. They tended to blame each other for joint decisions that they hadn't properly considered.

They now went through each of their options and it became apparent that:

1. They had to sell their home at a huge loss and move to modest rented accommodation;
2. The beach house had to be tenanted with a full-time tenant to make the interest costs on it tax deductible. This meant that they could no longer use it; and

Somehow they needed to deal with the non profitable elements of their dental empire, but this was not easy as each had been bought with borrowings from Megabank, averaging $600,000 per practice, augmented with Megabank chattel mortgages of about $400,000 per practice to refit and re-equip.

The sale of their home and the renting of the beach house did have the effect of reducing financial pressure. Crash took several weeks off under doctor's orders but this was enormously expensive to their cash flow, since without him there was insufficient cash flow for their dental empire to pay all of its bills.

They economised in their personal lives, swapping their expensive cars for modest machines and Jane was forced to economise in every aspect of their family lifestyle. This was a bitter lesson to her.

Meanwhile Megabank was now requiring half yearly financials by set dates. Jane had significantly reduced the services of her marketing buddy and was contemplating how they could trim the dental empire.

Geoffrey and Louise depart

Geoffrey and Louise had recognised that there was no place for them in Crash and Jane's plans other than as employee dentists. They'd been quietly searching for a suitable practice to buy. They had at last found a practice owned by an older dentist with a good fee base whose decision to sell had been determined when he had been given notice by his employed dentist. Geoffrey and Louise figured that they'd be happier as practice owners and gave notice to Crash.

This precipitated a further crisis. Jane was able to secure a reasonable replacement for Geoffrey; Fred had had two years' clinical experience. But Fred had less fee generating capacity at this stage of his career. She was unsuccessful in finding a suitable replacement for Louise's position and filled it temporarily with locums. Under doctor's orders, Crash had substantially reduced his clinical output.

The annual fees produced in Crash's number one practice now looked like this:

Crash's surgery	$900,000
Fred's surgery	$500,000
Andrew's surgery	$425,000
Locum dentists	$400,000
Hygienist	$275,000
Total	**$2,500,000**

Fees at the location had fallen by 32.2% but the profit at location one had fallen from $1,283,100 to $640,000 or by more than 50%!

Crash and Jane were now three and a half years into the financing contracts for equipment and fit-out at practice two; the contracts at practice three had three years to run, and at practice four two years and nine months. Only practice two was breaking even, while the losses at practices three and four continued unabated.

Profit practice one	$640,000
Practice two – break even	$0
Practice three – a loss	($90,000)
Practice four – loss	($150,000)
Overall dental profit	$400,000
Less annual loss on beach house rental	($100,000)
Net profit	**$300,000**

This equated to joint after tax profit of $208,600 after dividing income evenly between Crash and Jane.

Cash flow situation much worse

Because capital repayments on loans and financing contracts were significantly greater than the interest cost, their free after tax cash flow was now negligible, yet they were now living in a rented home. They were surviving on expanding credit card debts. They had sold some personal possessions and the payments to dental suppliers were being stretched outwards. The practice receptionists began getting messages from suppliers asking Crash or Jane to ring them back. To save expenditure, all ordering was now done for minimum quantities and at the last moment. There was often a crisis in one of the practices, with supplies having to be borrowed from another location and Jane spent a lot of time running around patching holes. Their marketing expenditure had been slashed.

Practices for sale

The accounts insisted upon by Megabank and produced by Big Firm were being done at horrendous charge-out rates, but they were afraid that if they switched back to a more conventional dental accounting firm Megabank would interpret it as a sign of weakness and push them even harder. The partner who had recruited them to Big Firm had long since become too busy and far too expensive to see them. Bob, who dealt with them, was really a little out of his depth but was able to work a deal with the financier of practice equipment whereby some leases were selectively shortened and some lengthened, but overall cash flow remained the same. The result was that the equipment in practice two reached payout and they put it on the market because it had the best prospect of producing a profit. By adding back the foregone financing charges, they were able to present a profitable picture and as the practice was well equipped it attracted interest in the marketplace. They managed to sell at an overall loss of about $400,000 but retained a small amount of the capital to meet some urgent personal expenses whilst marginally reducing Megabank's debt.

The exercise of selling practice two bought them a little time and they were able to repeat it within a further nine months at practice three.

As they shed two of the practices, the attention to detail at both the original practice and at practice four began to improve. There was a slight upturn in profitability. It took a further year and they were able to shed practice four.

With the external weight lifted and less pressure, profitability began to flow back into Crash's practice. Whilst it subsequently produced enough profit to enable them to survive in the medium term and as financing charges were reduced, Megabank was no longer concerned. They shifted their accounting back to a more economical arrangement.

Crash re-enters associateship

By this stage, Fred had begun to thrive in the environment and they were able to sell him an associateship. Crash's dental empire now consisted of a dental associateship with Fred. They jointly employed two dentists and a hygienist and ran a profitable practice but it never again broke records.

Sale of beach property at huge loss

It took several more years but they were able to eventually sell the beach property out at a slight capital loss, but the net loss on financing their ownership over about eight and a half years, together with purchase and sale costs, had left him about $750,000 out of pocket. Given the time value of money, the real impact of the decision to buy it had been much greater.

They were able to borrow to buy a home but their previous experience had made them risk averse and they purchased into a much more modest area. Out of necessity, Jane had taken up employment in her old profession of podiatry.

There was now a lot less pressure on Crash and although he still produced excellent dentistry, he was limited to about $800,000 of fees per annum in his own surgery; and paced himself for health reasons. He shared the net production of two employed dentists and a hygienist with his associate, Fred, but they only contributed modestly to profit.

Comparison of Crash and Steddie at age 42

Crash's Assets

- Home, current market value $900,000
- 50% of dental practice = 50% of goodwill and equipment value = $700,000
- 50% of premises = 50% of $2.4 million = $1.2 million
- Crash and Jane's superannuation fund $700,000
- Total assets = $2.3 million

Crash's Debt

- Residual debt on premises $700,000
- Debt on home $550,000
- Total = $1,250,000

Net assets = $1,050,000

This was far less than Crash and Jane's net asset value had been nine years earlier. They realised that it would take years to work themselves back to a sound financial position.

Steddie's Assets

- Home, current market value $1.8 million
- Practice, current market value $1.2 million
- Practice premises, current market value $1.3 million
- Superannuation fund $1.3 million
- Total assets $5.6 million

Steddie's Debt

Total debt = $600,000 all of it being interest tax deductible.

Net assets = $5 million

Steddie was producing $1.2 million of fees in his own surgery and two em-ployed dentists were producing a further $1.175 million.

Mamie worked 20 hours per week as a literature teacher at a private school, not out of necessity but out of love for what she did. Steddie and Mamie were able to make regular non tax deductible contributions to their superannuation fund in addition to their deductible contributions. Their net asset value was growing at a healthy rate.

Discretionary income

Steddie now had far more discretionary income than Crash. In the long term, Steddie and Mamie decided that they would like to sell his practice while he was still in his 50s in order that they could pursue other personal interests. By contrast, Crash and Jane realised that if they were able to afford to again live in a suburb of choice and have sufficient assets to retire, they were going to have to work for many years and restrict their spending. Crash figured that he could not afford to retire before age 60 at earliest, but some projections suggested that he would have to work longer than that. Jane realised that she would have to spend many years working as a podiatrist to bring in the additional income they needed.

About Crash and Steddie

Crash and Steddie are not based on particular dentists, but rather a montage of dentists that we have observed. Only a small percentage of dentists generate fees of the levels referred to.

The lessons

- No two dentists are exactly alike.
- Sometimes high-flying dentists make bad strategic decisions. There is no substitute for regular, knowledgeable advice concerning business plans and advice must be taken before decisions which have a major financial impact.
- Some of the most successful dentists we know are able to achieve a great deal without their success being obvious to professional peers.
- Some of the most outwardly successful dentists pursue practice business plans which are deeply flawed and place them at serious risk.
- Usually major financial decisions taken in haste are difficult to undo.
- Most dentists have fewer years of high productivity than they realise. If they embark on a wrong business strategy, there is usually insufficient time to rectify matters and create substantial wealth from dentistry.

About the author

Graham Middleton personally has been advising dentists on strategic, practice management, valuation and conflict resolution processes for 24 years, the last 17 as a partner and director of Synstrat Management Pty Ltd and Synstrat Accounting Pty Ltd. He was once a regular army officer, and later Director Human Resources Manager, Attorney General's Department of Victoria. He is considered an expert on dental practice valuation and practice performance benchmarking. He has spent many years advising dentists in respect of their business and financial strategy and measuring their practice and financial performance. The Synstrat Group is an independent data-based organisation providing management, benchmarking, valuation, financial and accounting services to the dental profession. Synstrat Management Pty Ltd is a Licensed Dealer owned by its directors who work within the Synstrat Group. Tel: (03) 9843-7777 Fax: (03) 9843-7799 Internet: www.synstrat.com.au Email: dental@synstrat.com.au