Practice Transitions Made Perfect™

Newsletter Article Reprint

How Much Does it Cost Per Month?

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Have you ever gone to purchase a car and asked the question: How much will the car cost? The salesman doesn't give you the price of the car anymore. You will be told that there are financing terms that will allow your monthly payments to fit into your budget. No matter how many times you ask, the total cost of the car is not relevant! The salesman knows that confronting you with the total cost of the car is usually beyond the ability of most purchasers today, but if he can reduce that cost to a manageable monthly figure, you will drive out in that new car.

All practice finance companies look to the cashflow of the existing practice to repay the acquisition loan. The industry standard is that the practice for moderately priced practices is a five to seven year financing term. Some may finance for up to tenyears to accommodate the buyer, but still want the analysis to be able to pay back the loan over no more than seven years. If the cashflow does not support those requisites, the practice either was priced too high, or was the wrong one for the doctor.

We have recently seen that some dental practice acquisition lenders must have learned something from the car salesmen. If the cashflow of the practice will not support the needs of the doctor, they simply extend the payments for up to 15 years! Well that sounds like it should work, doesn't it? If you can reduce your monthly payments enough, you can certainly afford to buy the practice. In looking at the numbers, consider the following table:

Principal Amount	$500,000	$500,000	$500,000
Interest Rate	8.5%	8.5%	8.5%
Term	7 years (84 months)	7 years (84 months)	7 years (84 months)
Monthly Payment	$7,918	$6,199	$4,923
Total Interest Paid	$165,132	$243,913	$386,266
Total Cost	$665,132	$743,913	$886,266
Cost Differential		$(78,781)	$(221,133)

By extending your loan from 7 years to 15 years, your monthly payment is reduced by $3,000 and you will pay an additional $221,133 or a total of $386,266 in interest for a $500,000 loan! So, while you can afford the monthly payments, you have spent additional money for the original purchase that could have gone into your retirement account.

We suggest that when the buyer is forced to finance a purchase over 10 to 15 years just to make the cashflow work, the purchase price is unrealistic for that buyer. You should insist that a realistic cashflow analysis of the existing practice produce enough income for your lifestyle needs. A practice that does not have a realistic cashflow is either overpriced or too small for your needs.

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