

Myth buster: “I can’t become a practice owner with my debt”

Melvin D. Wenger, DVM; Gabriel E. Middleton, DVM
Orrville Veterinary Clinic, Inc., Orrville, OH 44667

Abstract

Practice sustainability is a necessity for the viability of the mixed animal veterinary practice industry. To keep mixed animal practices thriving, a plan is needed to transition practices from 1 generation to another. Buying into a mixed animal practice is often promised to a new associate doctor but not fulfilled. The process often lacks communication and a good plan. Drs. Wenger and Middleton will share their experiences on how their practice has transitioned from 1 generation to another. They continue to focus on transition as new-generation partners are joining the practice. They will touch on how to value a mixed animal practice. Purchasing a practice is a return on investment for the owner that is selling and a huge investment for the new owner that is buying shares of the practice. Much has been written about valuing, buying, and selling small animal practices, but there is little information on how this relates to mixed animal practices. Large student loan debts complicate the process and often stop the discussion because no solution is presented. Current student loan income-based repayment plans may create challenges to young veterinary practice owners due to an increase in income, thereby increasing student loan payments and creating cash flow dilemmas. Drs. Wenger and Middleton conclude that it is possible to become an owner with student loan debt and complicated loan repayment schedules, and will share their experience as to how to make it happen.

Key words: veterinary practice, mixed practice, practice management

Résumé

La pérennité de la pratique est une nécessité pour assurer la viabilité dans le domaine des pratiques mixtes de médecine vétérinaire. Pour que la pratique vétérinaire mixte prospère, il faut un plan pour passer la pratique d'une génération à l'autre. Les nouveaux docteurs associés se voient souvent offrir l'achat de parts dans une pratique vétérinaire mixte mais cette promesse n'est pas toujours tenue. La communication n'est pas toujours au rendez-vous et le processus n'est pas nécessairement basé sur un bon plan. Les docteurs Wenger et Middleton vont partager leur expérience sur la transition de leur pratique d'une génération à l'autre. Ils continuent d'orienter leurs efforts sur la transition car la pratique accueille des nouveaux partenaires d'une autre génération. Ils vont aborder la valorisation d'une pratique vétérinaire mixte.

L'achat d'une pratique est un retour sur l'investissement pour le propriétaire qui vend et un très gros investissement pour le nouveau propriétaire qui achète des parts dans la pratique. On a beaucoup écrit sur la valorisation, l'achat et la vente de petites pratiques animales. Il est moins clair si tout cela est pertinent pour les pratiques vétérinaires mixtes. Des dettes élevées de prêt d'étude compliquent le processus et mettent souvent un terme aux discussions car aucune solution n'est proposée. Les plans actuels de remboursement des dettes de prêt d'étude basés sur le salaire peuvent causer des difficultés car la hausse de salaire chez les jeunes propriétaires d'une pratique vétérinaire accroît les paiements de la dette et engendre des problèmes de liquidités. Les docteurs Wenger et Middleton concluent qu'il est possible de devenir propriétaire même avec des dettes de prêt d'étude et des calendriers compliqués de remboursement de la dette et vont partager leur expérience sur comment s'y prendre.

Introduction

As the older generation ages, the question of what to do with the practice ownership is often asked. The new generation of associate veterinarians is often saddled with a huge amount of student loan debt that it appears impossible to consider owning a practice. Older practice owners often have no plan in place to transition the practice and thus nothing happens. Transitioning is something that takes time, often a 10-year process to develop a plan and implement it. In this paper, we will share our experiences on this topic and share how it has worked in our practice as we have transitioned from the older generation to the younger generation.

Most veterinary practices focus on high quality veterinary medicine to provide their clients with the best skilled care possible. It is well known that the business side of practice is largely ignored in veterinary schools. As veterinarians, we continue our education to keep up with the constant changes in our profession. We develop strong relationships with our clientele, so strong that it is difficult to fathom that we may need to retire and pass our practice on to someone else. Through the pressure of keeping up the demands of our profession and our clientele, we often overlook the business side of veterinary medicine. The business side of the practice is the most neglected area of veterinary practice. It is either delegated to a staff member or a spouse or maybe given some attention at the end of a busy day or weekend if necessary. This behavior becomes a concern for new associate doctors joining the practice because they are instantly recognizing

the business concerns as they join the practice with a large student loan debt and concurrently starting a family and looking to buy a house. This is when ownership possibilities are often promised but the time given to sitting down and preparing a plan is often lacking due to time constraints and a lack of understanding as to what it takes to draw up a transition plan for the business. Practice sustainability must include a plan to allow a young associate doctor to work through paying off the student loan, providing finances to adequately raise a family, and provide for a future as a practice owner. Younger veterinarians often struggle with the idea of practice ownership without the creation and communication of any plan moving forward. Without a formal plan in place, the process can frustrate both sides, especially the younger generation. The financial feasibility of purchasing a practice can be challenging unless both sides can sit down and crunch the numbers to determine if it can work.

Over the past 15 years at Orrville Veterinary Clinic, Inc., we have taken this topic seriously as we have transitioned our practice from 4 owners from the older generation to a new generation of owners. The older generation had been partners for 25 years and there was little thought given to transition until retirement became part of the conversation. This was mostly due to the fact that the practice was stable in regards to ownership and it the partners didn't find it necessary to address the topic. After an associate was hired with ownership aspirations, we had to come up with a plan. We will share the plan we came up with and how we proceeded with the transition.

As the managing partner of Orrville Veterinary Clinic, Inc and the youngest partner Dr. Wenger was tasked with how to make the transition happen. We recognized change was coming. We had no plan but knew we needed to hire new associates and give them an idea of how this would all work. He started the process by attending numerous continuing education seminars but found most dealt with small animal practices, so there were still many questions left unanswered. The first task that needed dealt with was to determine a practice value. There are numerous methods to value practices but again mostly published formulas are for small animal practices. Most practice owners have a guess for what they would like the value of their practice to be but few have a good reliable value. You can pay practice evaluators to come up with a number but often it is a number both sides can't agree with or understand how it was derived. Large and small animal practices differ greatly on product sale value, overhead for services, and sources of revenue. Profit is a reliable number so that plays into the value of a practice. Using the profit of the practice, we developed a formula that annual numbers can be plugged into and a practice value is easily established year after year. We used this for several years and it seemed to work for us. We now have a reliable, consistent practice value each year to use for any buying or selling of shares for that year. It is critical to keep the valuing formula consistent year after year so an associate will

buy shares using the same formula that they will eventually sell those same shares for. This allows for sustainability of the practice.

Younger veterinarians are more likely to question the status quo and must understand the justification for a decision before accepting it. Creating a system that values a practice in a transparent manner is critical for a young veterinarian to understand before accepting the burden of the practice purchase. Including the previous and projected practice values also helps the next generation understand the financial potential of their investment. The younger generation must understand that the practice must grow in order to make their investment worthwhile.

Once the value of the practice is established, the number is divided by the number of total shares in the practice. The number of shares is an arbitrary number to allow purchasing portions of a practice in affordable amounts. Our practice has 200 shares and we sell shares to an associate doctor that we invite to become an owner. We sell the number of shares the previous owners are willing to sell and the amount the new owner can afford to purchase. The share price increases in value year after year as the practice prospers.

Associate veterinarians have many financial obligations as they struggle with student loans, family commitments, and basic living expenses. To afford the purchase price of a practice the dollars needed to pay for the purchase must come from additional income from becoming a partial owner. Associate pay, prior to ownership, cannot become too high or out of line with production pay as a veterinarian. This is critical to maintaining cash flow for the young veterinarian after the process of purchasing the practice begins. The new additional wages from becoming an owner must go towards paying for the shares of the practice. This additional pay is paid directly to the seller before the buyer has a chance to use it for some other purchases. This financing by the previous owner will go for 7-12 years depending on shares purchased and amount financed. The young veterinary practice owner may not realize much of a year-end bonus for a few years until practice growth allows for revenue to grow above the expenses of the new loan payments to purchase the practice. In this system, however, young veterinarians are not asked to take any form of a pay cut to purchase the practice so the cash strapped next generation is not asked to have a further financial burden. With the possibility of home ownership, a young family, and high student loan payments, a reduction in cash flow is almost impossible for most young veterinarians to incur. When the shares are paid in full the new owner then realizes the full salary as an owner. This allows for a succession plan and practice sustainability.

There are possibly generational differences on the idea of work/life balance. The younger generation places a higher value on personal time. There should be open communication to the young veterinarian in regards to additional responsibilities with practice ownership and the time spent in management, meetings, bookkeeping, etc. It is challenging

when the expectations are not clear and there are unexpected time and emotional burdens in addition to the financial burden of practice ownership.

Real estate ownership may not necessarily be tied to the ownership of the practice. Our practice has a plan to transition real estate to the new practice owner. This usually occurs after the shares of the practice are paid off in 7-12 years. This is done in an effort to not create too significant of a debt load on the young veterinarian all at once. Young veterinarians who are already deep in debt may risk opportunities for personal purchases if they are leveraged too much with both real estate debt and practice ownership debt. Just as with purchase of the practice, we attempt to make the real estate purchase pay for itself by utilizing real estate rent payment to pay for that. The younger generation must understand that financial gain from purchasing a veterinary practice is not always immediately realized, but the process does pay off in the end as long as the practice has sufficient growth and vision for the future.

Conclusion

To ensure practice sustainability a succession plan must be in place. This encourages associate veterinarians to stay with a practice knowing there is a plan in place to allow for future ownership. Practice value is the first thing needed to start the process. A method to easily determine practice value each year allows for a consistent and reliable process for the transition. A financing plan must be in place to allow the purchase price to be paid with new income from becoming an owner. In our seminar at AABP conference, Drs. Wenger and Middleton will share their experiences and details of how the transition process has worked in their practice as we pass the practice from one generation to another. A well-planned transition is a rewarding experience for both the buyer and the seller