Is a Dental Practice Management Model Right For You?

Many dentists are opting into a dental practice management ("DPM") model, as evidenced by the increasingly large number of DPM deals occurring across the country, including in the Chicagoland area.

The DPM model provides an opportunity for a management company to form a joint venture or other business arrangement with one or more dental practices. The management company performs the administrative and management services for the dental practice, thereby allowing the dentists to focus on patient care. In exchange, the dental practice pays the management company a fee for its administrative services and/or the opportunity to share in the revenue or profits of the practice.

While the DPM structure provides certain economies of scale not otherwise attainable to a practice, leading to increased profitability and revenue, structuring such a transaction to comply with Federal and state regulations requires experience and expertise. The ADA neither encourages nor discourages dentists from the DPM model; however, the ADA believes dentists should understand the pros and cons.

The most common DPM structure begins with the management company purchasing all of the practice’s tangible assets and entering into a long-term management contract (anywhere from 15 to 40 years). Under the management contract, the management company agrees to provide and/or oversee all of the non-treatment, administrative aspects of the practice. For example, the management company will hire and train all support staff, purchase equipment and supplies on behalf of the practice, and handle the practice’s billing and coding. Frequently, the management company also attempts to increase the practice’s patient flow through advertising and obtaining managed-care contracts for the practice. In theory, the management company’s expertise in these areas will increase the practice’s efficiency,
free dentists from administrative burden, and increase the time they have available to practice and bill patients, both of which should increase revenues.

The actual practice of dentistry is done by a separate professional corporation, which owns all intangible assets of the practice, such as the patient records and goodwill of the practice. The dentists are employed by the professional corporation, with compensation usually consisting of a base salary plus bonus. From time to time, equity in the management company may be offered.

When contemplating whether or not to enter into a DPM model, you must consider:

1. Financial Terms: In addition to the purchase price for the practice, the dentist must be content with the salary and bonus terms, as well as the fees to be paid to the management company. For example, although the management company may want its fee based on a percentage of revenues or profits, it may not be permissible if the state has a fee-splitting law like Illinois. Additionally, equity may be relevant.

2. Structure of the DPM Arrangement: The structure of the transaction must fit within the parameters of the regulatory framework and applicable state corporate practice of dentistry doctrine. For example, Illinois will not allow a non-dentist to own or control a professional corporation. Thus, the management company cannot be a shareholder of this entity. Since the management company cannot have a direct ownership interest, it may seek other mechanisms to exercise control over the practice. Yet most states, including Illinois, restrict to some extent the involvement of the management company in the practice’s operations.

To circumvent these restrictions, some DPM transactions are structured so that a “friendly” dentist is the sole owner of the practice entity. This dentist will enter into a nominee agreement with the management company entity, restricting the dentist’s ability to vote his or her shares or membership interests and ability to freely transfer his or her ownership interest in the professional corporation. The nominee agreement typically requires the dentist to consult with the management company (or be subject to mandatory redemption) on significant issues impacting the practice. These provisions can raise concerns with the corporate practice of dentistry prohibitions under Illinois law. Thus, the guidance of legal counsel experienced in the sale and purchase of dental practices is critical.

3. Tax Advice: Since most sales of dental practices are taxable transactions, you will also need advice from a tax specialist and a financial consultant. With an asset-sale transaction, a seller corporation could be subject to ordinary income tax. Goodwill is relevant here as well. With a stock-for-stock exchange transaction, the shareholders will be subject to capital-gains tax on the sale of their interests. Depending on the type of transaction, the differences in tax rates can be significant. Thus, consultation with a tax specialist is critical.

Deciding on a DPM model of practice will take careful consideration. As you conduct your deliberations, be sure to consult with the appropriate advisors so that your decision is an informed one.

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