

Four Surprising Reasons Why a Dental Practice's Overhead May Be Out of Control

By David J. Goodman, CPA, Partner, Dental Practice Leader

If a dental practice's overhead, before paying owners and associates, is greater than 65%, the practice's overhead may be out of control. The median dental practice overhead is 75% of collections. This means that a practice collecting \$1 million will provide only \$250,000 for owners and associates. Lowering overhead by 10% could result in an extra \$100,000 of profit per year available for owners and associates. Over a 10-year period, that would be an additional \$1 million of profit. Most dentists who work with a CPA firm with membership in the Academy of Dental CPAs (ADCPA) find overhead averaging between 60 to 65% of collections.

There are a few surprising reasons why dental practice overhead may be out of control.

1. Not Looking at the Numbers

We find that most dentists usually focus on some – but not all – of their important practice numbers. Overlooking the impact of overhead on the net income happens when dentists focus solely on cash in the bank, production and collections. While a practice can experience consistent growth through increasing revenue, all that extra income can be easily absorbed by an increase in overhead costs.

There are industry benchmarks dentists can use to compare overhead percentages to an average practice. For example, the profession's standard for the cost of dental supplies as a percentage of collections is about 5% to 8%. If a practice has a higher percentage, dentists can review the purchasing, inventory control and supply usage systems for inefficiencies. Even a 1% decrease in a practice's overhead category can mean thousands of dollars being added to net income.

2. Too Many Appointment Cancellations and No Shows

When a practice reserves time for a patient and the patient misses their appointment, the production time is lost forever unless free time is used to make up for the missed appointment. More importantly, income is lost. Besides lost income, when patients do not show up for appointments much of the overhead associated with the time is still incurred. Employee wages, rent, utilities and other fixed costs create higher overhead percentages when there is a reduction in production.

We believe that patient education is critical to minimizing missed appointments. Patients who understand the importance of treatment and the consequences of not being treated are more likely to show up for their appointments. Keeping a list of short notice patients who can be flexible with their schedules can also help fill in for cancellations.

3. Employee Theft

It is not surprising that dental industry statistics reveal that as many as 35% of dental practices will experience some form of embezzlement according to the ADA Center for Professional Success: Protecting Your Dental Office from Fraud. Many dentists do not have the training or knowledge on how to protect their assets.

The most common form of embezzlement is the theft of collections. The theft of cash and checks can be relatively easy, especially for an experienced embezzler. An "experienced embezzler" is someone who stole from a practice and was not reported to the authorities because the dentist was embarrassed or had pity for the employee.

Embezzlement of cash and checks reduces the income of the practice and increases the overhead as a percentage of collections. Embezzlement through the unauthorized use of credit cards or the over reporting of hours worked by employees can also increase overhead.

There are other signs of an embezzler. The person is usually the most trusted employee. They come to work early, stay late and demand to be in control of everything even if their work environment is a mess. This person rarely takes vacation and, if they do, no one is allowed to do their job while they are away. This person may also seem to be enjoying a lifestyle that appears to go beyond their means. Another sign of embezzlement is the rising of accounts receivable. A dentist should be comparing accounts receivable aging reports at least monthly.

A practice owner sets the example for the employees to follow. Ethical behavior helps to reduce the threat of employee theft.

The implementation of controls to prevent embezzlement can raise trust issues with employees. We recommend that all employees be informed of the implementation of new controls as a way to protect them from unwarranted accusations.

4. Work More or Make Less

In many practices, there is an expectation by the employees that each year they will receive an automatic pay increase. If an employee receives a raise, how does the dentist pay for it? Unless there is some sort of patient fee increase, the dentist will most likely have to work more to pay for the raise or take home less money. From our perspective, neither is a healthy option.

Not only is employee compensation increasing overhead annually, but there are also other overhead expenses that increase each year as well. An increase in employee wages will increase payroll tax expenses. Utility costs increase periodically. Many office leases increase annually, and the cost of living rises due to inflation.

We believe that annual fee increases are warranted to cover the rising cost of overhead. Increases do not have to be substantial. For 2022, we are recommending fee increases for fee for service patients of about 4% to 5%. Even if the practice is an insurance-based practice, the increase in the UCR (usual, customary and reasonable) charges will put an insurance provider on notice that fees are increasing in that area. If fee for service rates are submitted when billing the insurance company, renegotiation of reimbursement rates are then more compelling. We understand this may require more recordkeeping when adjusting for insurance reimbursement, but we believe it is better than having to work more or make less.

Contact Us

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