The most common questions dentists ask about credit

By Joseph Flumian, MPA

The most common phrase I hear as I help dentists with their financing situations at McKenzie Management and the one I wish I had a dollar for every time it is spoken is: "They never taught us business in dental school."

This is apparently a true statement because I never cease to be amazed at how some of the most intelligent, thoughtful people I have had the pleasure to help in my 50-year career are lost when it comes to the financial side of their personal lives and business operations. Following are some of the most common questions dentists ask.

What affects my credit score?

This is the No. 1 question dentists ask. Your credit score is composed of how much of your available credit you have used, the number of late payments, length of credit history, new credit applications and the types of credit accounts you have used.

Certain decisions have an impact on your credit score as you go through life and some can last for years. Divorce, in particular, is the No. 1 credit score killer, followed by over-spending and bankruptcy. Many dentists have not reduced personal spending even though practice incomes have gone down. Do you really need the $75,000 automobile?

What I see happening now is that banks are lowering credit limits on many dentists. One of the key components of your credit score is how much of your available credit you have used.

Even though you might be spending the same, the ratio has actually gone up as a percentage because the banks lowered the limits. In some cases, banks will report a $0 credit limit on your credit report even though you may have $25,000 line with a bank. Consequently, your credit score is lower and you won't even know it.

Tax liens from both the IRS and state government and any open judgments will also affect your score. Too many dentists get into trouble because they forget to pay state taxes on their employees. They do figure it out eventually when they are served a notice to pay up with penalties attached.

One way to keep your score high is to pay credit cards in full each month and to keep the same cards for as long as you can. A long-term line of credit scores you higher than a new card just issued.

Thus, “hopping and shopping” credit cards frequently is not a good idea. As a side note: felony arrests make getting a U.S. Small Business Association (SBA) loan extremely difficult and they will make you go to your local police station to submit fingerprints.

Things are so bad, should I file bankruptcy?

Bankruptcy is probably the last thing you should consider doing. I would only consider this with the advice of an attorney who specializes in bankruptcy. Dentists make sense when your credit score is so severely dinged for at least seven years and understand that some lenders will never again lend to you, period.

Should I incorporate?

There are still many dentists who are not proprietors for tax or financial advice. Again, this is the time to talk to your attorney about what you should be. Every state has different liability and estate building, and the main purpose of incorporating is to try to protect personal assets in case of litigation. That’s the “limited liability” in LLC.

Creditors make sense when you have more than $2 million in production, and then it’s all about defined benefit plans for you and allocation if you include your staff. It really is worth going to a professional and getting the best tax and liability advice.

Should I buy the building or should I continue to lease?

Here’s another cash flow question. If you buy a building, purchase real estate and build, or buy an office condominium, each of these decisions affects your long-term retirement strategy. The key is to have a strategy.

Selling your practice at the end of your career is a strategy, but very risky. If you purchase property, you can typically get a 20-25 year term loan and wrap your other practice debt in as well.

You own the property separately from your practice, generally in separate corporate entities. The idea here is that when you sell the practice, you retain the income from the property as part of your cash flow in retirement.

Leasing makes sense if you have a short horizon and will be selling or moving to another location. It’s a fixed cost of doing business per your lease. You can depreciate the equipment, software, etc., but not the building, which you can only if you owned.

Should I refinance?

Refinancing for an established practice with rates as low as they are now can be an excellent idea. A practice start-up loan can be taken out for 10 years and practice real estate loans can last 20-25 years. The purpose of a refinancing, especially with the current economy, is to increase cash flow to the practice and to save interest expense by moving from a higher interest rate to a lower rate.

Generally, the payment stream for a new loan will be dependent on what is being refinanced. Look for funding sources that have no prepay- ment penalties and no fees. Despite the economy and stock market, dentists should invest in their pensions and/or retirement plans to increase cash flow if possible.

Can I include other items in my refinance?

Absolutely. It’s a great opportunity to add additional equipment, computer, etc., to the practice while lowering your monthly payments.

For example, our clients refinance and add in payment to receive practice management consulting help for their practices. This allows them to increase revenues while decreasing payments.

What is debt service to coverage ratio?

This is the measurement of your cash flow after the refinancing that shows there are sufficient funds to cover the new lender expense and your ratio. We have a free calculator if you want to see what your current ratio is, please e-mail me at joe@mckenziegmt.com and I will send it to you.

It only takes a few minutes and it allows you to determine if refinancing makes sense. If you can’t meet the ratio, the likelihood of an approval is no longer a mystery. It won’t happen.

How can I improve my credit score?

Pay credit cards in full every month. Keep your oldest credit card for as long as it makes sense, pay your student loans, make your mortgage payments on time and check your credit report annually.

You can get a real free credit report at www.annualcreditreport.com. They won’t give you a score, but you can see all of your activity and it gives you the ability to promptly contest anything that’s incorrect. Here’s a true story: I am currently working with a dentist who lives in the south, and an individual with the identical name but is deceased had horrible credit.

The credit bureaus cross-pollinate the data between the dentist and the deceased. The dentist can’t get a loan until this is cleared up, and he didn’t discover the problem until he accessed his credit report.

I’m a new dentist and I want to start up a new practice, what do I do first?

That’s easy. Enroll in the McKenzie Management’s two-day, one-on-one training program. It’s everything they didn’t teach you in dental school about business. The frightening reality is you don’t know what you don’t know, so get help.

The materials and workbooks alone make this a worthwhile investment. From there, develop a business plan with the information you receive and put together a team of trusted and experienced advisors, including an attorney, a certified public accountant, a reputable dental supplier, etc.

Should I use a credit counseling service?

Cautions here. Some charge thousands of dollars. I have had dentists proudly tell me that they were able to reduce their debt obligations on their credit cards by thousands of dollars. Do you think the banks are going to be happy with this negotiated settlement? Are you going to be happy to be forced to take 50 percent of a crown fee? Of course not, and nor are they.

The banks get even by killing your credit. Don’t be surprised if you can’t get a loan for up to 10 years for your business. You are better off trying just about anything else. Consider doing a merchant advance or a cash for collateral loan. These are two options to consider first. Again, I can’t stress enough the importance of seeking professional advice from a financial advisor first. It’s a worthwhile investment.