Financing To Grow Your Practice

Consider the pros and cons of various funding sources.

By Cheryl Whitman

If your practice isn't constantly welcoming new patients and keeping up to date with regard to equipment, treatments, and procedures, then it may be heading for trouble. New patients are the life-blood of a medical practice or medispa and providing excellent service and the best standard of care by offering state-of-the-art technology is key to keeping them coming through the door. However, doing so requires the commitment of resources, both financial and human. A previous article addressed human resources; this article will address ways to secure financial resources to grow your practice.

Internal Finance

One method is to internally finance your own growth by using the profits from your practice and the ongoing cash flow to purchase new equipment or expand. The advantages to this are that you are "borrowing" from yourself, no applications to fill out, no approvals to wait for and no interest to pay. However, there are downsides to this approach. First, new technology is expensive, so it may require extended time to save up enough cash for the purchase. It can also mean you have to delay other investments in your practice, which can hurt your growth potential. A third concern is it depletes your profit/cash flow cushion so any unexpected or unplanned expenses can have a negative impact on your practice. Given these concerns, it is important to consider other financing options.

Line of Credit

A word of caution is in order. Getting loans is more difficult than it was in the past and many small businesses, and small medical practices and medispas will find it challenging to secure financing. According to a 2017 National Small Business Association studyDisplay footnote number:1, one-fourth of small business owners say they can't obtain the necessary funds to operate their businesses.

Interestingly enough, the study also reveals that of those that do successfully secure financing, 85% of that financing is coming from a source other than a large bank; and the situation has only gotten worse due to COVID. With this in mind, it makes sense for your practice to develop a variety of financial allies.

First, consider a line of credit. Bankrate defines a line of credit or credit line as, "an open-ended, revolving loan that a borrower may access on demand. The lender determines the total amount of credit to extend based on the borrower's creditworthiness. The borrower can access funds from the line of credit at any time, up to the maximum amount set by the lender."Display footnote number:2 Having a line of credit offers your practice flexibility because it's available when you need it and you only pay interest on the amount you use. It's better to have one and not use it than need one and not have it.

Ann Welsh, Commercial Lender for First National Bank Coastal Community in Wellington, FL explains how it works, "We offer a medical guidance loan. A client would be approved for a certain amount of funds that the client can draw on for a year for medical equipment, expansion and working capital. After the year is up, whatever has been used will be put into a 4 year term loan. At the time of signing, the client will know what the rate of the term loan will be in a year's time.

The benefits of this type of loan include the following.

The medical practice is locking into today's rates for next year.

Flexible payments while growing the practice.

Don't have to provide financials for each equipment purchase – 1x

Local contact – we can only work with clients in Florida"

Asset and Term Loans

In addition to credit lines, there are other types of loans to consider. These include asset-based loans and term loans. Asset-based loans are collateral secured loans ranging from one to five years and are secured by the asset being financed. This type of loan may offer a lower interest rate than an unsecured loan. Some of the other advantages of an asset-based loan are that they allow you to better manage your cash flow by making a set payment over time; they help you finance critical technology at a lower cost; and help free up your cash flow for other opportunities as opposed to using cash for the purchase. Finally, since the loan funds are spent for capital equipment, it can have tax advantages for your practice.

Term loans provide a lump sum of capital, which your practice will need to repay over time in regular installments. Term loans vary in length from a few months to as long as 25 years. The amount of the loan and the interest rate will vary based on your practice's financial criteria. They may be applied to operating expenses, real estate or equipment purchases, renovations, or a variety of other things. They may also require a personal guarantee.

Medical Practice Loans

Medical practice loans are available from various lenders and can be used to cover new business start-up costs, purchase equipment, purchase an existing practice or promote your current medical practice.

Medical practice loans are similar to other types of business loans, but generally require you to provide additional documentation to the lender. Some sources of medical practice loans are detailed below.

Private investors and venture capital companies often invest in medical practices with good cash flow. Their objective is to help grow the practice, making it more profitable, then divest themselves of the investment, often to another venture capital or private equity investor. They prefer to invest in practices with significant levels of unencumbered cash flow and strong growth. The benefit of using these funding sources is their ability to inject capital to facilitate faster practice growth. However, venture capital and private equity firms require you to give up a portion of the equity or control in your practice in exchange for funding. You may have to give up seats on your board of directors and therefore some of your decision-making power.

Beth Herdegan of SEDCO explained, "The Small Business Administration (SBA) offers several types of loans through their network of participating lenders. The SBA 504 loan program can be used to finance tangible assets such as owner-occupied commercial real estate, large machinery and equipment purchases. This type of loan can typically cover up to 90% of the cost. SBA 504 loans offer fixed rates for periods ranging from 10 to 25 years."

SBA loans usually offer higher funding amounts, lower interest rates, long terms, and can be used for a variety of business expenses. They can be difficult to obtain as they require good credit and a minimum of two years of business history. Additionally, you must be able to meet the SBA's size standard criteria. Size standards define the largest size a business can be to participate in government contracting programs and compete for contracts reserved or set aside for small businesses. Size standards vary by industry and are generally based on the number of employees or the amount of annual receipts the business has.

Banks and credit unions are a traditional source of loans and offer a variety of financial products. They tend to have strict requirements and long application processes. Online lenders are more relaxed when it comes to requirements and have higher funding approval rates than banks and credit unions. They offer a broad spectrum of financing solutions and are also more inclined to fund start-up practices. Additionally, they have rapid approval and processing times so you can receive your funds quickly. The downside is that online lenders generally charge higher interest rates than credit unions, banks or the SBA.

Prepare Documentation

Regardless of which option you choose or where you seek funds, you will need to provide basic documentation such as business plans, balance sheets, profit and loss statements, historical and projected cash flows, debt schedules and other business financials. You will also need to supply credit scores, lists of available collateral, personal financial history and legal documents showing your medical licensing, etc. You may be asked to personally guarantee the loans.

Borrower Beware

A word of caution is in order. According to Medical Economics, the most common mistake practices make is taking on too much debt.Display footnote number:3 Frequently, a practice is growing quickly and therefore adds more office space, new equipment and staff. However, they take on substantial debt to fund this and their cash flow hasn't grown quickly enough to sufficiently support the practice and cover the debt service. Another scenario: rapid expansion financed by extensive debt puts the practice at risk should there be an unexpected event such as an economic downturn or a key staff member becoming incapacitated. It's important to plan for unpleasant surprises when you consider taking on extensive debt. It could help prevent business failure.

Shop Around

Whatever financing method you pursue, it's important to shop around for the best funding options available to your practice and be certain you clearly understand the terms before you choose. Once you finalize a loan or equity/venture capital investment, you are committing your practice to an extended period of financial obligation, which will affect your bottom line.

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