MANAGEMENT & MARKETING

(Editor's Note: This quarterly JCO column is compiled by Contributing Editor Howard Iba. Every three months, Dr. Iba presents a successful approach or strategy for a particular aspect of practice management. Your suggestions for future topics or authors are welcome.)

When I first started practice nearly 25 years ago, the focus of many consultants and practice-management lecturers was on gross production. That was the way to evaluate the success of a practice. Many us can remember the books and presentations on the "Million-Dollar Practice", which was the benchmark in those days. It always surprised me how long it took some "experts" to make the simple change of focusing on net profitability rather than on gross production.

In this month's article, Dr. Jerry Clark, a practicing orthodontist in Greensboro, North Carolina, presents a somewhat different way to evaluate our practices, by what he calls "profit realization". He adds another factor to the productivity-profitability equation—that of time. For those of us who are sprouting gray hairs, the efficient and effective utilization of time has become more important with each passing year.

Time-and-motion efficiency studies have always considered time, but they have centered on gross production per doctor hour. Plugging time into the equation at the net profitability level gives us a better evaluation of the overall effectiveness of our practices.

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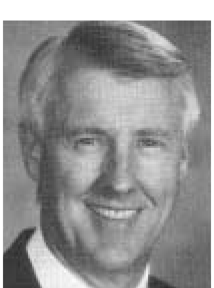
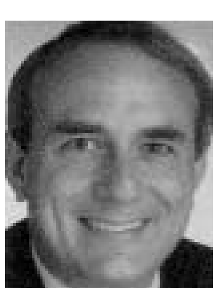


Dr. Iba



Dr. Clark

Profit Realization: A New Standard of Practice Success

Besides the most important issue—quality of orthodontic treatment—there is one other factor that clearly demonstrates how successful we are as orthodontists. This key statistic, which graphically represents the efficiency and productivity of a practice, is *profit per doctor hour worked.* We call this statistic *profit realization.*

The formula for computing profit realization is *actual profit* divided by the number of doctor hours worked. Actual profit is the gross income of the practice minus the *actual business-related expenses.* The actual business-related expenses are determined by subtracting all orthodontist income and discretionary expenses from the total practice expenses. A sample computation is as follows:

Total expenses		$856,000
Doctor salary and taxes	$280,000	
Discretionary expenses:		
Insurance	8,000	
Continuing education	12,000	
Retirement	28,000	
Entertainment	8,000	
Miscellaneous (car, etc.)	10,000	
Less total		—$346,000
Actual business-related expenses		$510,000

Gross income	$1,000,000
Actual business-related expenses	-$510,000
Actual profit	$490,000

If the orthodontist in this example averaged working eight hours per day, 15 days per month for that year, the total hours worked would be 1,440. The profit realization can then be calculated as follows:

$$\frac{\$490{,}000}{1{,}440} = \$340$$

Comparison to Other Practices

The profit realization formula provides the opportunity to compare solo practices with group practices. The computation is the same. Simply add up the total hours worked by all the doctors in the practice and plug them into the formula.

A practice's profit realization can be compared to that of other practices in an effort to improve profitability. We have devised the arbitrary ranges shown here to allow our clients to quickly gauge how they stack up.

Profit Realization	Evaluation
Less than $200	Needs improvement
$200-300	Good
$300-400	Excellent
$400-500	Outstanding
More than $500	A goal to shoot for!

Which of these practices looks most like yours?

	Practice No. 1	2	3
Days worked per year	185	218	168
No. staff members	18	10	6
Patients seen per day	65	85	58
Overhead	78%	68%	56%
Profit realization	$186	$237	$322

I hope you answered "Practice 3". This doctor is working less and making more, has fewer staff members to manage and pay, and has less stress because of seeing fewer patients per day. If your practice looks more like Practice 1 or Practice 2, you should consider making some meaningful changes.

Improving Profit Realization

Anything that increases your practice's gross income can have a positive effect on profit—if expenses are kept constant or even decreased. A combination of increasing gross receipts and decreasing expenses will have a dramatic effect on the profit of the practice.

Increasing the top line usually requires making meaningful changes in many different areas. Targeted areas might include:

• *Clinical efficiency.* Reduced chairtime means increased profit.

• *Marketing.* A comprehensive marketing plan and practice promotion video can dramatically increase the number of new patients seeking treatment.

• *Case acceptance.* A smooth, effective new-patient process can successfully integrate more patients into the practice.

• *Fee structuring.* Are you charging enough for your treatment? If it has been awhile, raise your fees.

• *Flexible financing arrangements.* Don't let rigid payment policies stand in the way of good patients' starting treatment.

• *Collection policies.* Accounts more than 60 days past due should be less than 1% of the practice's annual gross income.

Ways to decrease expenses include:

• *Budgeting.* Develop a budget—and stick to it. If you don't know what you are going to spend your hard-earned money on, you are probably wasting it.

• *Appropriate staffing.* More than 70% of the practices we visit are overstaffed.

• *Purchasing strategies.* Negotiate with vendors; buy in volume, and buy smart.

• *Inventory control.* Develop a system.

• *Tracking your numbers.* Always know your overhead percentage and where it should be.

• *Stop whim spending.* Orthodontists are notorious for trying to save 1 cent on a bracket, yet spending $40,000 on some newfangled high-tech item. Before you buy, ask yourself, "Will this purchase increase my profitability?" If not, don't buy it.

Conclusion

Will tracking practice profitability help your practice? I can only tell you what it's done for mine. I am now 55 years old, but over the past five years—at a time when many practices are leveling off or declining—my practice has doubled its profit realization, from $163 to $322. What it boils down to is this: for every hour I work, I now make twice as much as I did five years ago.

Start tracking this telling statistic and see what it does for your practice.

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