



The Letter of Intent in Dental Practice Sales

An overview of the importance of the Letter of Intent in dental practice sales and acquisitions

The Letter of Intent in Dental Practice Sales



LOI sets deal momentum

The letter of intent establishes the initial terms and conditions for the transaction, setting the tone and direction for the rest of the deal process.



Most leverage exists here

Sellers have the greatest negotiating power at the LOI stage, before committing to exclusivity and diligence.



Later documents rarely fix LOI mistakes

Issues that arise in the LOI are difficult to address in subsequent transaction documents, making it critical to get the LOI right.

The letter of intent is a crucial juncture in dental practice sales, where the terms of the deal are established and the relative leverage of the parties is at its highest point.

Why the LOI Matters More Than Sellers Think



LOI sets deal momentum

The Letter of Intent is the first step in the negotiation process and sets the tone for the entire deal.



Most leverage exists here

Sellers have the most negotiating power at the LOI stage before the buyer gains significant information through diligence.



Later documents rarely fix LOI mistakes

Issues that arise in the LOI are often difficult to remedy in subsequent purchase agreement negotiations.

The Letter of Intent is a critical stage in the dental practice sales process, as it sets the foundation for the entire deal and determines the seller's leverage moving forward.

Common Misconception About LOIs



"It's non-binding"

Many sellers mistakenly believe the LOI is not legally enforceable, when in fact key provisions are typically binding.



"We'll fix it later"

Sellers often think they can renegotiate the LOI terms later, but the LOI usually sets the framework for the final deal.



"This is just a formality"

The LOI is a critical document that establishes the foundation of the transaction - it's not just a formality to get through.

The LOI is a legally binding document that sets the tone for the entire transaction, contrary to common misconceptions.

What an LOI Actually Does



Locks economic terms

The LOI establishes the key financial and commercial terms of the transaction, such as the purchase price, payment structure, and allocation of assets and liabilities.



Shapes diligence scope

The LOI outlines the areas of due diligence that the buyer will focus on, which can significantly impact the final deal terms.



Sets expectations for final deal

The LOI sets the foundation for the definitive purchase agreement, outlining the parties' expectations and the framework for the final transaction.

The LOI is a critical document that establishes the key terms, scope, and expectations for the final transaction, making it a crucial step in the dental practice sale process.

Binding vs Non-Binding Provisions



Exclusivity

Exclusivity provisions restrict the seller from negotiating with other buyers during the LOI period.



No-shop clauses

No-shop provisions prevent the seller from soliciting or entertaining offers from other potential buyers.



Confidentiality

Confidentiality clauses protect sensitive information about the practice and the transaction.



Cost allocation

The LOI may specify how transaction costs like legal fees and due diligence expenses will be allocated between buyer and seller.

The LOI establishes key binding and non-binding terms that set the stage for the final transaction documents.

Economic Terms Set at the LOI Stage



Purchase price structure

The structure of the purchase price, including upfront cash, deferred payments, and equity rollovers.



Cash vs rollover equity

The balance between cash consideration and the seller's equity stake in the buyer entity.



Earn-outs and holdbacks

Performance-based deferred payments and escrow arrangements to manage post-closing risks.

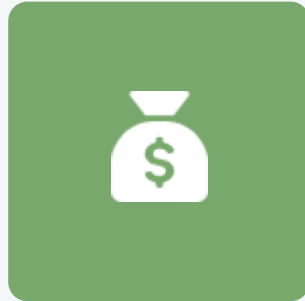
The LOI sets the foundation for the economic terms of the transaction, which will significantly impact the seller's net proceeds and risk exposure.

Why Price Alone Is Misleading



Structure determines risk

The way the purchase price is structured (e.g. cash vs. rollover equity, earnouts, holdbacks) affects the overall risk profile of the transaction for the seller.



Deferred consideration changes value

Payments that are deferred or contingent on future performance can significantly impact the actual value the seller receives, even if the headline purchase price seems high.



Net proceeds matter more than headline price

After accounting for transaction costs, taxes, and other adjustments, the net amount the seller walks away with is more important than the top-line purchase price figure.

When evaluating an offer, sellers need to look beyond just the headline purchase price and carefully consider the overall transaction structure, deferred payments, and net proceeds to determine the true value and risk profile of the deal.

Exclusivity: The Silent Leverage Killer



No-shop provisions

Exclusivity clauses that prevent the seller from negotiating with other buyers



Loss of negotiating power

Once the seller is locked into exclusivity, they lose leverage to negotiate better terms



Timing traps for sellers

Exclusivity periods can create time pressure for the seller, forcing them to accept unfavorable terms

Exclusivity clauses in the LOI can significantly reduce the seller's leverage and negotiating power, leading to less favorable deal terms.

Diligence Scope Is Decided Early



Financial diligence

Comprehensive review of financial records, including income statements, balance sheets, and cash flow statements.



Legal and compliance review

Examination of legal contracts, regulatory filings, and any potential legal risks or liabilities.



Operational exposure

Analysis of the practice's operations, including staffing, equipment, workflow, and patient records.

By clearly defining the diligence scope in the LOI, sellers can better understand the buyer's expectations and prepare accordingly, maintaining leverage throughout the process.

How Buyers Use Diligence After the LOI



Retrades

Buyers may attempt to renegotiate the deal terms, such as the purchase price, after the initial LOI is signed



Price adjustments

Buyers may use diligence findings to justify lowering the agreed-upon purchase price



Risk shifting to sellers

Buyers may try to shift more risk and liability onto the sellers based on diligence discoveries

Buyers often leverage the diligence process after the LOI is signed to gain more favorable terms, underscoring the importance of a well-negotiated LOI that protects the seller's interests.

Employment Terms Often Start in the LOI



Length of post-closing employment

The LOI often specifies the expected length of the seller's continued employment after the closing of the transaction.



Compensation assumptions

The LOI outlines the assumptions around the seller's post-closing compensation, such as salary, bonuses, and benefits.



Termination expectations

The LOI may also address the terms and conditions under which the seller's employment can be terminated after the transaction.

The LOI is an important document that sets the stage for the seller's post-closing employment terms, including the length of employment, compensation, and termination provisions.

Restrictive Covenants Previewed in the LOI



Non-competes

Restrictions on the seller's ability to compete with the buyer's business after the sale



Non-solicits

Restrictions on the seller's ability to solicit the buyer's customers or employees after the sale



Geographic and time scope

The specific geographic area and time period during which the restrictive covenants will apply

The LOI sets the stage for the restrictive covenants that will be included in the final deal documents, allowing the parties to negotiate the scope and limitations upfront.

DSO vs Private Buyer LOIs



Different leverage dynamics

DSOs typically have more negotiating power and resources, while private buyers may have a smaller margin for error.



Different risk tolerance

DSOs may be willing to take on more risk compared to private buyers, who may be more conservative in their approach.



Different negotiation posture

DSOs often have a more aggressive negotiation style, while private buyers may be more willing to compromise to secure the deal.

The differences in leverage, risk tolerance, and negotiation styles between DSOs and private buyers can significantly impact the LOI process and outcome for dental practice sellers.

Red Flags Sellers Miss in LOIs



Vague language

Ambiguous or open-ended terms that give buyers discretion to interpret or change deal parameters.



Buyer discretion clauses

Provisions that allow buyers to unilaterally make decisions or changes without seller approval.



Open-ended diligence

Diligence requirements that are not clearly defined, allowing buyers to extend or expand the review process.

These common LOI pitfalls can erode a seller's leverage and lead to unfavorable outcomes if not addressed proactively.

Why Sellers Lose Leverage After Signing



Market exposure disappears

Once the LOI is signed, the seller's ability to solicit and negotiate with other potential buyers is severely limited, reducing their leverage.



Switching buyers becomes costly

If the seller tries to back out or switch to another buyer, they may face significant legal and financial penalties, further reducing their bargaining power.



Momentum favors buyer

After the LOI is signed, the buyer gains significant momentum and leverage, as the seller is now invested in the deal and may be reluctant to risk losing it.

Once the LOI is signed, the seller's leverage diminishes significantly, as their market exposure is limited, switching buyers becomes costly, and the buyer gains the upper hand in negotiations.

When to Push Back—and When Not To



Economic certainty vs deal flow

Balancing the need for clear economic terms with the desire to keep the deal moving forward and maintain negotiating momentum



Strategic concessions

Identifying areas where tactical concessions can be made to the buyer to preserve more important leverage points



Protecting downside

Ensuring key protections are in place to mitigate risks and limit the seller's exposure, even if it means some negotiation

The LOI stage is a delicate balance between securing favorable terms and maintaining deal momentum. Sellers must carefully evaluate which points to push back on and which concessions can be made strategically to protect their interests.

Role of Legal Counsel at the LOI Stage



Translating economics into risk

Helping clients understand the legal implications of the economic terms in the LOI and how they impact overall risk.



Preserving leverage

Advising clients on negotiation strategies to maintain their bargaining power throughout the LOI process.



Preventing retrades

Ensuring that the LOI sets clear expectations and prevents the buyer from renegotiating key terms during the due diligence phase.

By providing expert counsel at the LOI stage, lawyers can help clients navigate the complex dynamics of the dental practice sale process and secure the best possible outcome.

What a Seller-Protective LOI Looks Like



Clear economics

The LOI should clearly define the purchase price structure, any deferred consideration, and other key financial terms.



Defined diligence

The LOI should specify the scope and timeline of the buyer's due diligence, limiting open-ended review.



Balanced exclusivity

The LOI should provide a reasonable exclusivity period for the buyer, while preserving the seller's ability to consider other offers.

A seller-protective LOI establishes clear deal terms, a defined diligence process, and balanced exclusivity - protecting the seller's leverage throughout the transaction.



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In conclusion, the letter of intent (LOI) is a critical stage in dental practice mergers and acquisitions. Sellers must approach the LOI carefully, get legal counsel involved early, and protect their leverage before the due diligence process begins. By understanding the importance of the LOI and taking proactive steps, dental practice owners can position themselves for a successful transaction.



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