Spending Less

Before adding expenses, consider the financial consequences.

BY JON A. HULTMAN, DPM, MBA

Doctors typically obtain practice management insights from journal articles, lectures, newspapers, and conversations with peers. Occasionally, these insights "jump out" at us when least expected, such as in verses of songs or lines from films. Early on, a line from the 2001 film "Bandits" caught my attention. It offered insight into an issue applicable to practice management. This film featured actors Billy Bob Thornton and Bruce Willis as professional bank robbers. Following a lucrative bank heist, Thornton's character went on a spending spree, purchasing a host of unnecessary luxury items. In order to "educate" him regarding the foolishness of his wasteful ways, Willis' character remarked: "Every dollar you spend is another dollar that we have to steal!"

While, in the context of the movie, this line is funny, it offered an important lesson regarding unnecessary spending in a medical practice as well as in one's personal life. Willis was intending to give Thornton a fresh perspective with this line, offering him an impetus to change his behavior and focus. What he wanted was for Thornton to focus on his unnecessary splurges and recognize the effort fraught with danger that was required to produce the cash making it possible. Willis recognized the impact of each on the other. Likewise, doctors could benefit if they were to focus on maximizing the profit garnered from their labor through controlling costs in their practices. They should also be aware of just how much work must be done to create the profit necessary for purchase of personal luxury items.

Doctors could benefit if they were to focus on maximizing the profit garnered from their labor through controlling costs in their practices.

Unfortunately, the relationship between revenue and profit in a medical practice is not the same dollar for dollar one as the one presented in a bank heist. This fact creates an even greater challenge for medical practitioners. If a movie were to be made that included a scene depicting two physician partners discussing the expenses of their medical practice, the Willis line would need to be changed to, "Every dollar you spend is another four dollars that we need to bill." Assume the following statistics for the average practice: 1) collection ratio = 77%, 2) overhead = 50%, and 3) tax rate = 35%. *Table 1* shows how this translates to the fact that only one dollar of profit is available for personal spending for every four dollars billed.

TABLE 1

50% Overhead

Amount Billed	$4.00
Collect 77%	$3.08
After 50% Overhead	$1.54
After 35% Tax	$1.00

We can see from *Table 1* that any unnecessary spending (overhead)

Continued on page 146

Spending Less *(from page 145)*

must be controlled at the office. If a practice's overhead meets the 50% average, four dollars must be billed to generate each dollar of a doctor's take-home (profit). Additionally, each personal income dollar has been provided by billing four times that amount at the practice. Each $1.54 of overhead cost conserved at the practice produces

If a practice's overhead meets the 50% average, four dollars must be billed to generate each dollar of a doctor's take-home (profit).

the same result as billing an additional $4.00. This does not mean that a medical practice should discontinue marketing or stop increasing patient volume; however, the upside leverage made possible through controlling practice costs and reducing unnecessary expenses (spending), is a strategy that should at least be considered.

This four-to-one billing/profit ratio for the average practice can become a nine-to-one relationship as inefficiencies build up—especially in larger groups. It is not unusual to see a large group practice with 65% overhead and a 48% collection ratio, resulting in $1.00 after-tax, for every $9.20 billed *(Table 2)*. Overhead is a necessary cost for providing medical services and producing revenue, but excessively high overheads are typical and as can be seen in *Table 2,* can present a significant burden for doctors. Know that controlling expenses does not require "being cheap" or putting off investing in a practice; it means selectively spending in areas that increase quality and/or provide a return that is greater than their cost. Expenses that do not accomplish these ends are wasteful, add no value, and should, therefore, be eliminated. Identifying such expenses and controlling them during periods of growth is healthy for a practice. This will provide more leverage for increased profit than that created by a much larger increase in revenue.

TABLE 2

65% Overhead

Amount Billed	$9.20
Collect 48%	$4.42
After 65% Overhead	$1.55
After 35% Tax	$1.00

Before adding any new expense—either personally or in your practice, you should do a cost-benefit analysis that includes a consideration of the amount of work that will be required to cover the full cost of that new expenditure.

The same holds true for personal spending. Imagine the amount of money that a doctor needs to bill in order to have enough left over (profit), after paying overhead and taxes, to purchase extravagant, depreciating assets such as cars. Say that the purchasing of a car requires $73,000. It should give you pause to recognize that you may need to bill $671,600 (9.2 times the price) to take home the amount necessary to purchase that car. The point being, before adding any new expense—either personally or in your practice, you should do a cost-benefit analysis that includes a consideration of the amount of work that will be required to cover the full cost of that new expenditure. **PM**

Dr. Hultman is Executive Director, California Podiatric Medical Association, President, Medical Business Advisors, specializing in practice evaluations, valuations, and mergers. He is the author of *Reengineering the Medical Practice* and *Medical Practitioner's Survival Handbook.*