

Lines of credit for medical practices

- Stephanie Bouchard

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It is a common business strategy for medical practices to use lines of credit from a bank or other financial institution. With this business tool, medical practices reap many benefits, including the ability to bridge unexpected shortfalls in cash flow.

Which is exactly how Jeffrey Kagan, MD, an internist practicing in Newington, Conn., and a member of the Medical Economics editorial advisory board, has used his practice's line of credit. "Every once in a while, things get a little behind, so we draw on a line of credit and then we pay it off," he says.

A good example of this is when an insurance company that paid in 30 to 45 days suddenly—and without notice—began paying in 60 to 90 days, Kagan says.

Slow or delayed reimbursement is the most common likely scenario practices need a line of credit for, but there are many other uses, he notes. Some of those are having to hire a temporary replacement for an employee out on medical leave; needing to replace a broken piece of equipment; or a natural disaster that closes the practice temporarily.

"It's nice to have a line of credit to fall back on once in a while," he says. "It takes a lot of stress off if you have a pile of bills to pay."

A business line of credit allows borrowers to draw money from a predetermined credit limit as the money is needed, says Matt Jones, director of business lending at the National Institutes of Health Federal Credit Union (NIHFCU) in Rockville, Md.

Borrowers pay interest only on the amount of money they actually need at a given time and are only required to pay the monthly interest payment, says Jones.

With a line of credit, the financial institution doesn't apply the monthly payments to both the principal and the interest; borrowers must put in the money to pay both. So unless

borrowers make an effort to pay off the principal, it is still owed, even if they pay the interest for years, Jones says.

Many owners of medical practices have and use a business credit card to meet some of the practice's short-term financial needs. A business credit card typically has an interest rate of between 10 percent and 27 percent, whereas a business line of credit usually is in the 5 percent range. Additionally, lines of credit can be in the six digits or higher—far more than is available with a business credit card, he says.

Getting a safety net

Obtaining a line of credit generally is a pretty straightforward procedure, says James Edwards, a managing director in the medical specialty group of SunTrust Private Wealth Management in Atlanta, Ga.

The application process usually takes about two weeks. Potential borrowers meet with a representative of a financial institution and discuss the practice's needs. Applicants need to provide their financials—typically about three years' worth. The bank will review those and analyze the practice's accounts receivables to determine possible cashflow gaps.

For establishing a new practice, the bank will want to review the physician's business plan as well as revenue and expense projections for the next two to three years, Edwards says. The personal financial statement of the physician (or physicians, if a group practice) is also required.

The amount of the credit line is based on a ratio that factors in the needs and size of the practice and the accounts receivables if the practice is already established. The typical term of a line of credit is about a year, but that can vary and can be renewed annually, he says. The interest rate is tied to the U.S. prime interest rate or London Interbank Offered Rate.

Medical practices shouldn't hesitate to apply for a line of credit because having one should be standard operating procedure, Edwards says. "It's quick access to funds and eliminates business disruptions that could be caused by not having access."

It's all about being prepared

Typically, a line of credit costs medical practices nothing until they're used, although some financial institutions require a small annual fee, says NIHFCU's Jones. Therefore, because there are no or minimal costs to having a line of credit, he says it makes good business sense for medical practices to have one.

"It's healthy for a business to have an approved line of credit of some sort that they can access quickly to navigate short-term liquidity issues," he says. "I would relate it again to personal life where most people have that credit card that they have stashed off to the side just in case they need it."