

Texas ASC Society Annual Meeting

November 10-11, 2011

Tips to Maximize the Value of Your Practice

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This information is not, nor is it intended to be, legal advice.
You should consult an attorney for individual advice
regarding your own situation.

Tips to Maximize Value of Your Practice

1. Understand the Value of Your Practice
 - a. Value of Your Practice - Don't fall for the common misconceptions that your practice has no real value. You are not necessarily limited to book value.
 - b. Principles of Valuation - Understand appraiser valuation methodologies:
 - Cost Approach - Valuation based on the value of the assets, net of liabilities;
 - Income Approach - Valuation based on discounted cash flows; and
 - Market Approach - Valuation based on sales of other similar practices (*Definitions provided by American Society of Appraisers*).
 - c. Types of Assets - – Tangible (furniture, equipment, and improvements) and Intangible (goodwill)
2. Create Value in Your Practice
 - a. Primary Planning Focus – Seller's primary planning focus should be to take every competitive advantage to maximize the take-home cash. Seller should develop sound operational strategies including incorporating additional revenue streams, determining personal objectives and creating a business opportunity for potential buyers
 - b. Secondary Planning Focus - Secondary Planning Focus – Build your practice such that your sales price will hold up to the recognized appraisal methodologies.

Tips to Maximize Value of Your Practice

3. Identify Your Buyer

- a. Five General Categories - The five general categories for Buyers are new physicians, lateral physicians, existing employee physicians, competitors and hospitals.

4. Identify Your Legal Strategy

- a. Legal Model – There are numerous elements to developing a legal model, including but not limited to determining the following: Number of doctors, asset protection/non-competes, Federal and State regulations, ancillary entities, business succession plan, timing for exit and compensation model.
- b. Compensation Model – There are numerous models that a practice can use to design its ownership. The following are some of the most common: Eat What You Kill, Enterprise Model and Communist Model. Each one has pros and cons and should be weighed as to best fit the owners' personalities.
- c. Control – This becomes a big issue if Buyer and Seller partner after the sale. Both parties must weigh the risk associated with the practice after the closing. Parties can minimize the risk by developing sound operational structures.
- d. Timing – The Seller should consider this question as it relates to when they want to retire and what type of value they can receive. The Buyer must weigh the timing of how long the Seller will stay after the sale is closed.

5. Overcome Obstacles to Sell

- a. Battle of Appraisers – Don't get stuck in thinking that a valuation expert's numbers are the only numbers. Understand you have many variables.
- b. Advisors – Use health care advisors (Financial/Legal/ Accounting) to streamline the process and confirm you are in compliance with the applicable laws.
- c. Goodwill – Don't be side tracked by locker-room talk on goodwill and appraiser methodologies.
- d. Control – When the Seller is unwilling to cede some control it impacts the willingness of a Buyer to participate.
- e. Patient – Be patient with the process. A good sale does not happen overnight.

Overview

- Tips to Maximize Value of Your Practice
 1. Understand the Value of Your Practice
 2. Create Value in Your Practice
 3. Identify Your Buyer
 4. Identify Your Legal Strategy
 5. Overcome Obstacles to Sell

Value of Your Practice

- Common Misconceptions:
 - No Real Value
 - No Goodwill
 - Limited Book Value of Assets
- Reality:
 - The Misconceptions Can Impact Value
 - Valuation can be Complex
 - Can Be Multiple Variables
 - Practices Sold Greater Than Book Value

Principles of Valuation

Appraiser Valuation Methodologies:

(Definitions by American Society of Appraisers)

1. Cost Approach – Value of Assets,
Less Liabilities
2. Income Approach - Discounted
Cash Flow (“DCF”)
3. Market Approach - Sales of Other
Similar Practices

Types of Assets

- Tangible - furniture, equipment, and improvements
- Tangible - Valued at Book Value or Appraised Separately
- Intangible –Goodwill
 - Two types:
 - Professional Goodwill
 - Practice Goodwill

Goodwill

- Saleable Nature of Goodwill
 - Cannot Account for Volume or Values of Referrals Between Parties
 - Existing or Future
- Appropriate
 - Set at Fair Market Value
 - Valuation Uses Recognized Valuation Methodology
 - Supported by Written Documentation

Fair Market Value

- FMV=
 - Buyer and Seller
 - Arms Length
 - Open Unrestricted Market
 - Neither Compulsion to Buy or Sell
 - Reasonable Knowledge

(Definitions by American Society of Appraisers)

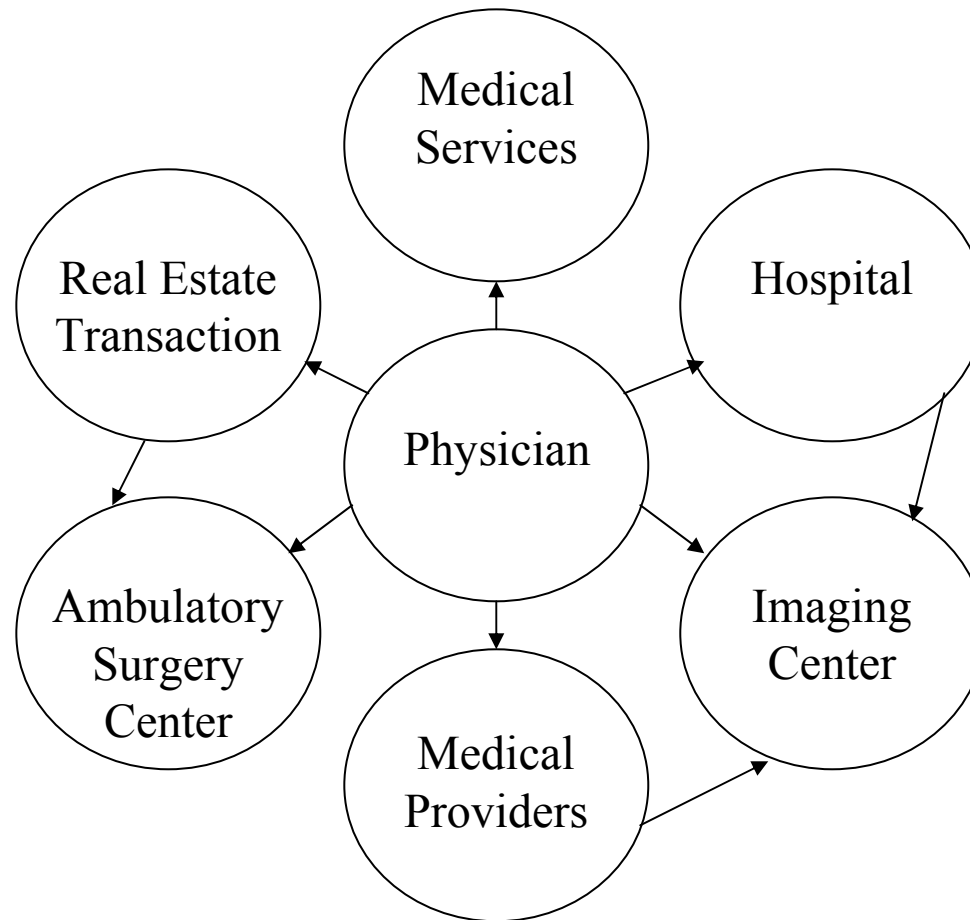
Create Value

- Primary Planning Focus
 - Competitive Advantage
 - Maximize Cash Take-Home
 - Use Operational Strategies
 - Compliance Plans
 - Incorporate Additional Revenue
 - Personal Objectives
 - Business Opportunity Greater Potential for Buyer

Incorporate Additional Revenue

- Exploring Opportunities
 - Imaging Centers
 - Lithotripsy
 - ASCs
 - Lab
 - Pain Management Centers
 - Medical Office Buildings

Relationships



Create Value

- Secondary Planning Focus
 - Sales Price Recognized Appraisal Methodology

Identify Your Buyer

- Five General Categories:
 - New Physician
 - Lateral Hire
 - Existing Employee Physician
 - Competitor
 - Hospital

New Physician

- Develop Valuation Prior to Hiring/ Investing
 - Comprehensive Employment/Governing Documents Agreement
 - *Include* Potential Buy-in/Buy-Out Terms

Lateral Hire

- Seasoned Physician
 - Less Training
 - Less Hand Holding
 - Book of Business
- More Complicated

Existing Employee Physician

- Longer Wait, More Challenging
- Low Success Rate
- Valuation Heated

Competitor

- Appraisal Issues
- Valuation Heated
- Non-competes

Hospital

- Hospital Practice Acquisitions ASC/Clinic
- Appraisal Issues
- Downside – Loss of Control
- Physician Owners to Employees

Protect Your Investment

- Confidentiality Agreement
- Non-Disclosure Agreement
- Letter of Intent
- Memorandum of Understanding

Legal Model

- Number of Doctors
- Asset Protection/Non-Competes
- Federal and State Regulations
- Ancillary Entities
- Business Succession Plan
- Timing for Exit
- Compensation Model
- Estate Planning
- Tax Planning

Non-Compete

- Rule of Enforcement –
 - 1st Enforceable Agreement
 - 2nd Covenant Ancillary to Agreement
- Reasonable Restraint of Trade
 - Time
 - Geographic Scope
 - Activity
- Physicians Special Rules
 - List of Patients
 - Access to Medical Records
 - Buy-out
 - Continuing Treatment

Anti-Kickback

- Prohibits any person from knowingly and willfully offering or paying any remuneration to induce a person to make referrals for services or items (purchase, lease and order)
- Prohibits any person from soliciting or receiving any remuneration in return for making referrals
- Safe Harbors
 - Not Meeting Every Element is Not *per se* Violation
- Texas Anti-Kickback Law

ASC Safe Harbor

- Four Categories of ASCs
 - Surgeon-owned
 - Single Specialty
 - Multi-Specialty
 - Hospital/Physician
- Common Elements
 - 1/3 Income Test - Physician-Investor's Medical Practice Income Derived from ASC Procedures
 - Multi-Specialty 1/3 Income Test Exception
- Must Meet All of the Elements of the 1/3 Income Test

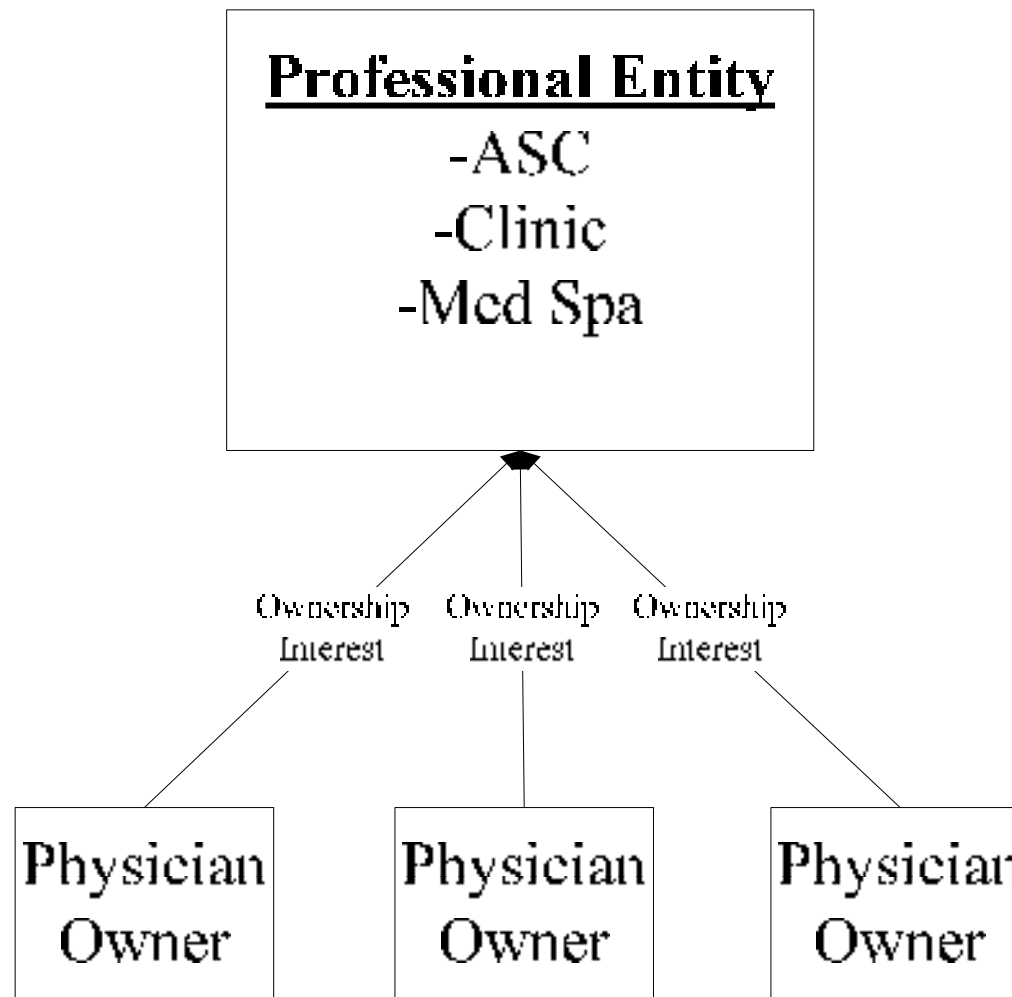
Business Succession Plan

- Buy-Sell Agreements
- Voluntary Withdrawal
 - Without Cause
 - Retirement
- Involuntary Withdrawal
 - Disability
 - Death
 - Mentally Incompetent
 - Bankruptcy
 - For Cause
- Divorce

Examples of Practice Models

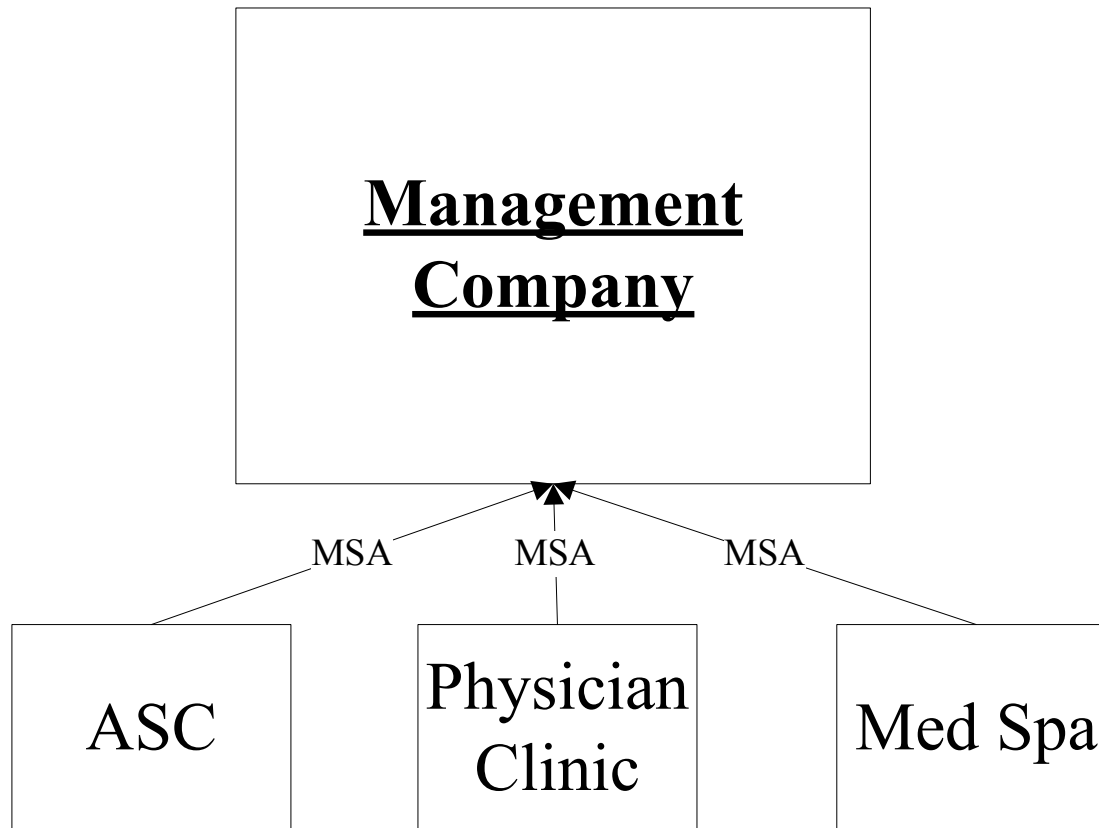
1. Single Entity Model
2. Management Company Hub – One Practice
3. Management Company Hub – Multiple Practices
4. Doctor Ownership Hub – Multiple Unrelated Entities

Single Entity Model

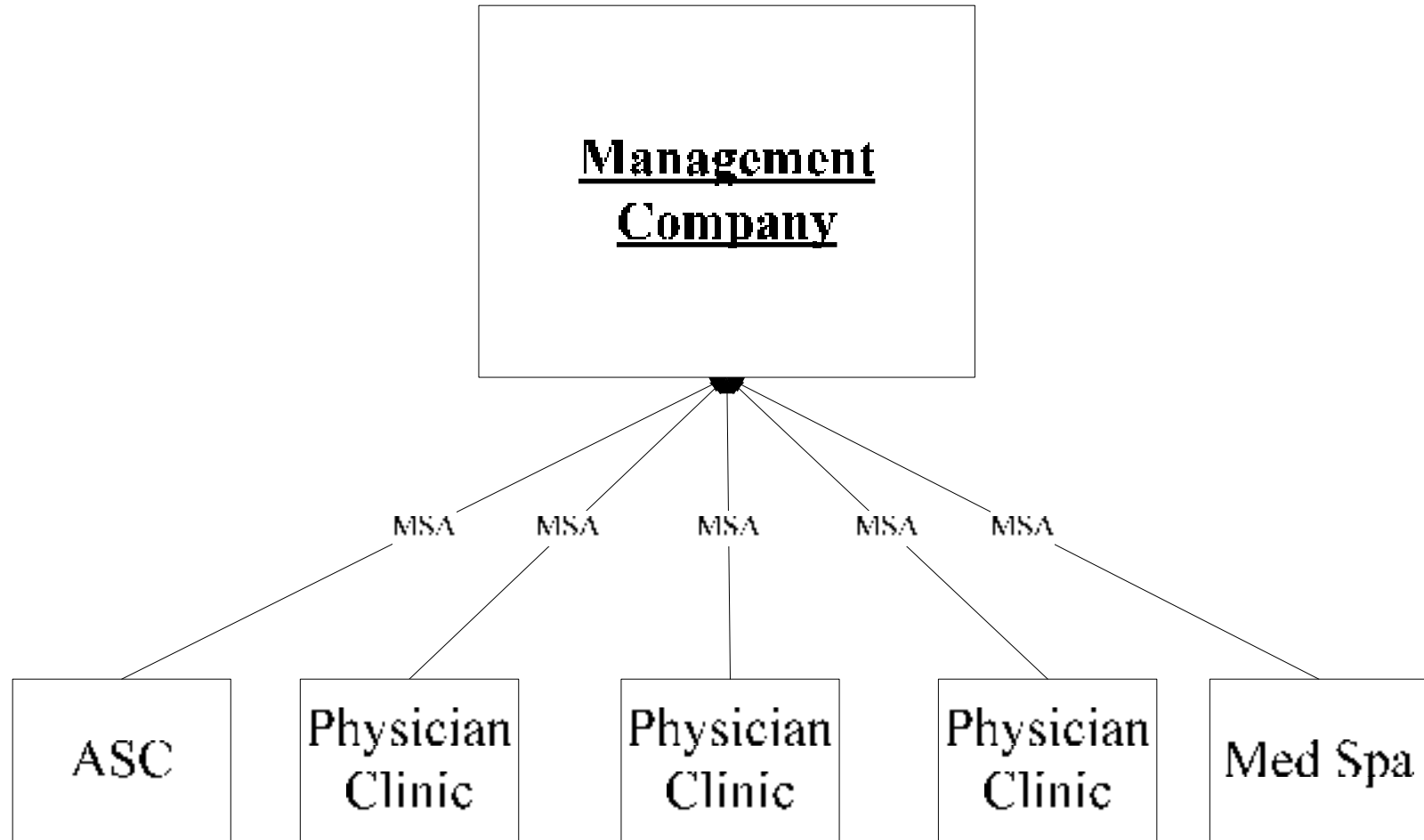


Management Company Hub-One Practice

- Corporate Practice Of Medicine

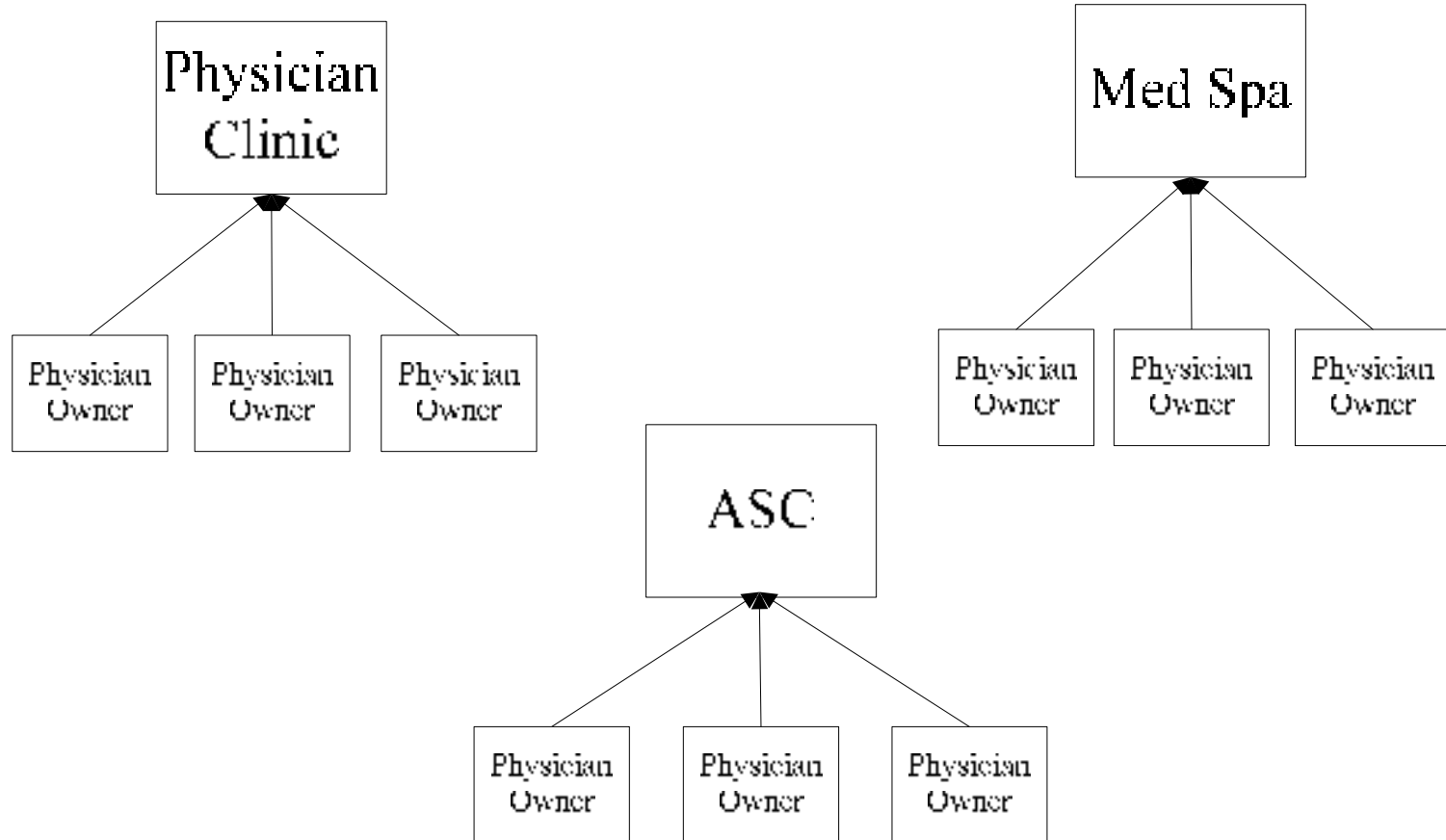


Management Company Hub-Multiple Practices



Doctor Ownership Hub

Multiple Unrelated Entities



Compensation Model

Three Basic Compensation Models:

1. Eat What You Kill
2. Enterprise Model
3. Communist Model

Compensation Model

Eat What You Kill

- Net Collections Less Shared Overhead + Less Direct Overhead
- Common Model for Single Specialist
- Negatively Impacts Certain Valuations

Compensation Model

Enterprise Model

- Guaranteed Salary and Share Profits Based on Productivity Formula
- Appraisers Love Model
- Compensation Still Productivity Based, Model Good for Single Specialist

Compensation Model

Communist Model

- Pool Collections and Share Profits Equally
- Traditional Business
- Similar to Enterprise Model
- Pitfall
 - Partner Disputes
 - Mix Personalities

Control

- Big Issue if Buyer and Seller Partner
- Risk to Buyer
- Risk to Seller
- Minimize Risk
- Operational Structures
 - Day to Day Decisions
 - Approval Process Major Decisions

Obstacles to Sell

1. Battle of Appraisers
2. Advisors (Financial/Legal/Accounting)
3. Goodwill
4. Control
5. Be Patient

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