



FLCB HANDBOOK: BUYING & SELLING A MEDICAL PRACTICE

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Physicians are valued professionals in their communities. Medical practices can provide care for our general health, and ensure that people are keeping their bodies in prime condition. As a physician, you have the opportunity to build a legacy that contributes to the good of your community. Owning your own medical practice is a great way to build this legacy in addition to providing for your own future retirement.

If you are a physician who has been building a practice for years, you are most likely familiar with the high esteem that you hold in the eyes of your clients. As you consider your retirement, you'll want to protect your legacy and make sure that your clients continue to receive excellent care. Even if you have been running your practice successfully for years, it is likely that selling a medical practice is not something you have immediate experience with. You may need help to make sure that you protect the value of your practice both to fund your own retirement and to continue to serve the community.

If you are a young physician looking to take that next step in your career, buying an established practice may seem daunting. Instituting a practice of your own is an excellent move that will allow you to be your own boss, and contribute to the larger community with your expertise. If you do not have a lot of personal business experience, you will want to make sure that you are setting yourself up for success.

This guide can help you by providing some valuable insight on issues you should consider when you are selling or buying a medical practice. We will discuss establishing the value of an existing practice, using a business broker, relationships between buyers and sellers in a business deal and how to finance the sale of a practice. This guide is meant to remove some of the fear associated with buying or selling a medical practice and help you to make some important decisions moving forward.

One of the most important issues in the sale of a medical practice is establishing value. If you are the seller, you will want to preserve as much of the value as possible in the sale. As the buyer, you may want to establish a lower value because the seller might believe that much of the future value is based on the hard work that they have done. The two parties will have to meet somewhere in the middle if the sale is going to happen.

There are many different ways to establish the value of the practice. Ultimately, the responsibility to set an initial price offering belongs to the seller. The seller needs to have a reasonable idea of what the value of their practice is so that offers can be evaluated from buyers. If you are working with a business broker, they can help you to determine the value of the practice.

Here are just a few different ways to determine the value of the practice:

VALUE OF PRACTICE ASSETS

You simply add up the value of all the assets and subtract the liabilities. Assets include property, equipment and outstanding invoices. Liabilities include debts and bills. With this method of determining value, the buyer is basically purchasing the existing practice's equipment. Sometimes the real estate is included in the purchase, but sometimes the buyer rents the building from the seller.

This method of valuation does not favor the seller because it does not include the value of the existing customers who are going to produce sales and cash flow for the new owner. The buyer may believe that the future sales and cash flow are not predictable and are dependent on the work that the buyer will put in after the sale, so they might insist on a value closer to the that of the assets of the practice.

FAIR MARKET VALUE OF THE PRACTICE

Another way of establishing the value of the practice is to see what other similar practices exist in the market place. You can find a practice with a similar number of physicians, clients and revenues that has recently sold. This represents a good starting point for the value of the practice. Keep in mind that no two practices are exactly alike, so it may be necessary to adjust this number based on the value of these differences.

VALUE OF OWNERSHIP

One way to look at the sale of the practice is that the buyer is purchasing certain benefits of ownership. These benefits include the owner's salary, the profits of the business and any other valuable benefits that the owner receives. Any depreciation or interest that was taken out in the calculation of profits is added back and anticipated capital expenses are subtracted. The total then represents the value of owning the practice. It can be a good place to start negotiations for the sale. In order to value your practice, you should have a business valuation done by a professional business appraiser who is familiar with the medical industry.

CASH FLOW METHOD

One method that takes into account the ongoing revenues of the business is the cash flow method. Projections of cash flow are made for three to five years in the future. These projections are discounted to yield the value of this cash flow in the present. This method is more advantageous to the seller who expects that their present clients will continue with the practice into the future.

There are many other methods of establishing the value of a medical practice. These methods can give you an idea of the minimum and maximum estimates of value. From there you can start negotiating.

For such a substantial and important transaction, you will most likely want to engage the services of a business broker to facilitate the sale of your practice.



While there are many advantages of using a business broker, there are also some drawbacks. You will want to make sure that you thoroughly vet a number of business brokers before selecting one to manage this transaction for you.

BENEFITS OF A BUSINESS BROKER

- Business brokers can market the medical practice for the seller. They find prospective buyers and sift the serious buyers from the people who are just kicking the tires.
- The broker can vet potential buyers. They want to make sure that they bring the right buyer on board. They will try to sell your practice to someone who can successfully run it.
- A broker can provide an independent estimation of the value of the practice. Brokers know the market so they can determine a fair price. You should also have your own rough estimation as well, just to make sure that the broker is in the right ballpark.
- Business brokers streamline the selling process. There is a lot of paperwork and documentation involved in the sale of a medical practice. Brokers make sure that all the necessary details are taken care of in a timely way.
- Brokers provide a buffer between the buyer and the seller. They can be the bearer of bad news, conveying the situation as an objective third-party. This prevents



emotions from flaring between the buyer and the seller.

DRAWBACKS OF USING A BUSINESS BROKER

- In the end, a business broker will want to get paid. There are fees associated with using a business broker, as well as a commission on the sale. Make sure you know what these are so you are not surprised.
- Brokers can have conflicts of interest. A broker could simply be interested in getting a deal done to collect the commission and move on. In most cases, brokers work for the seller, so they have a fiduciary responsibility to protect the interests of the seller. If you are buying a business, you may want to engage your own broker to protect your interests.
- The broker may demand exclusive rights to sell your business. You may negotiate a carve-out clause if you have an associate that is interested in buying the business. If you sell to this associate, the broker will not receive their commission.

FACTORS TO CONSIDER WHEN SELECTING A BROKER

- Many business brokers specialize in medical practices. These people have the experience required to facilitate a sale. You should seriously consider these specialized brokers.
- Make sure that the business broker you use is certified. The Certified Business Intermediary (CBI) is the gold standard in certification for a business broker.
- Ask how many transactions the broker has conducted. You can also ask how long they have been in business.
- Be sure to ask for and check references for any business brokers you are considering. Make sure you ask about the results from the broker's most recent transactions.

The right broker can facilitate a fair deal that benefits both the seller and the buyer. If you are looking to sell your practice, this could very well be the most important decision that you make. You want to investigate a number of

different brokers and make sure you choose one that you can work with.

Selling and buying a medical practice can be a sensitive process. The seller must reveal confidential business information about the practice to potential buyers. The buyer must have accurate information about the practice and the terms of the sale. Sellers need assurances that the buyer will use this information only to evaluate the feasibility of the sale. This is just some of the documentation and assurances that must be exchanged to make the transaction work.

FINANCIAL DOCUMENTATION

Sellers are going to need to turn over the practice's financial records to potential buyers. This provides evidence that a practice is in good condition to buttress to seller's estimation of the value of the business. A buyer should have an accountant go over the books before deciding to make an offer. Buyers should also be able to read and interpret the financial statements on their own to verify what the accountant says.

ASSET LIST

The seller needs a clear list of assets that will be transferred in the sale. The value of each asset should be noted. This should include a list of inventory that is to be included in the sale. Running a medical practices requires a lot of resources. Buyers want to know that they will have the right equipment to get started out

of the gate.

COMPLIANCE DOCUMENTATION

From medical waste to storing hazardous chemicals, there are lots of dimensions of a medical practice that are governed by federal regulations. Compliance issues can result in large fines that can cost a practice a lot of money. A buyer needs to be sure that everything is in order in this area to avoid these costs in the future. If the seller cannot demonstrate that the practice is in compliance with all regulations, this will negatively affect the value of the practice. Sellers should prepare for a sale by conducting a thorough compliance audit, remedy any problems and offer this documentation to the buyer. Buyers should have a lawyer inspect this documentation to make sure everything is up to snuff.

NON-DISCLOSURE AGREEMENTS

Buyers will be privy to the seller's confidential practice information. Business brokers and potential buyers will need to sign non-disclosure agreements to prevent confidential information from leaking out in a way that is detrimental to the practice. Even the fact that the practice is up for sale can be damaging. If clients learn that their physician is planning on retiring, they may start shopping for other practices. The resulting loss of clientele can be devastating to the value of the business.

NON-COMPETE AGREEMENTS

If the practice employs any physicians, the buyer should make sure that they sign non-compete agreements. Physicians employed by the practice receive appropriate pay for their services. They are not entitled to plunder the practice of its value beyond their legitimate pay. A non-compete agreement prevents currently employed physicians from taking a new job or opening a practice within a certain area. This protects the value of the practice because physicians cannot just leave and take customers with them. Employed physicians probably already have non-compete agreements with the current owner. A buyer will want to make sure these are appropriate and that they transfer with the sale.

Buyers need accurate information about the practice in order to negotiate a sale that is in their best interest. Sellers are going to reveal sensitive business information to potential buyers. They need protection to make sure that this information is not used to damage the business. These kind of agreements and information exchanges are required to make sure a fair deal can be reached.

After the value of the practice, the most important issue remaining is how to finance the purchase of the practice. Buyers have a number of financing options for the purchase of a medical practice. Here are some of them.

FINANCING FROM THE SMALL BUSINESS ASSOCIATION (SBA)

The first place you should check to finance the purchase of a medical practice is the SBA, a government agency that works with lenders to provide funds for small businesses. Since these loans are guaranteed by the government for up to 85% of the loan, they are easier to obtain and have lower interest rates. In addition, both business and personal assets can be used as collateral.

TRADITIONAL BANK LOAN

Bank loans are a very reliable and safe way to secure financing for your practice. In most cases you will need to have collateral or other assets available. An experienced lender can help you understand the various types of business loans and make a recommendation applicable to your situation. Government Guaranteed loans, such as an SBA loan, can also be an option as well.

VENTURE CAPITAL

Finding private investors to help you purchase a medical practice is another avenue. You will have to share the profits of the practices with these investors. More often, venture capital is useful for expanding practices to other locations. If you have an established practice and would like to purchase more practices to expand into other regions, you might approach venture capital investors to finance your expansion.

FINANCING FROM THE SELLER

Sometimes, the seller is willing to accept an initial down payment and receive the rest of the price in installments over time. Most sellers do not want to do this because there is no guarantee that they will receive these future payments if the practice should fail. However, sellers might be willing to do this for a physician who is already an employee of the practice. This gives some continuity to the practice and some confidence of future success.

REAL ESTATE THAT BELONGS TO THE PRACTICE

Many practices own the real estate and buildings that they operate out of. If this is the case, the buyer and seller may elect to include these in the assets of the practice. This adds a real estate aspect to the sale of the business. The alternative is to have the buyer rent the facilities for the practice and buy the real estate at a later date. The seller would become a landlord but would cash out of running the practice. The buyer would pay less for the business because it would exclude the real estate, but would have higher operating costs due to rent. Buyers and sellers need to carefully consider whether or not real estate should be included in the sale of the practice.

There are many good avenues for the buyer to pursue in order to finance the purchase of a practice. Sellers may be willing to help some buyers out with an installment plan; however, many sellers may want to completely cash out of the business.

CONCLUSION

The buying or selling of a medical practices marks a significant milestone in the life and career of a physician. For a young physician, buying a practice is the beginning of an amazing adventure. For a physician who is ready to retire, it represents the culmination of years of service to the community and the beginning of a new phase of life. The sale of a medical practice can be complex and tense, but with proper education and lots of good advice, you can navigate these issues to structure a deal that benefits both the buyer and the seller.

*This document is for informational purposes only and does not constitute an ability to lend. Please contact a qualified lending professional to review your specific needs.



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