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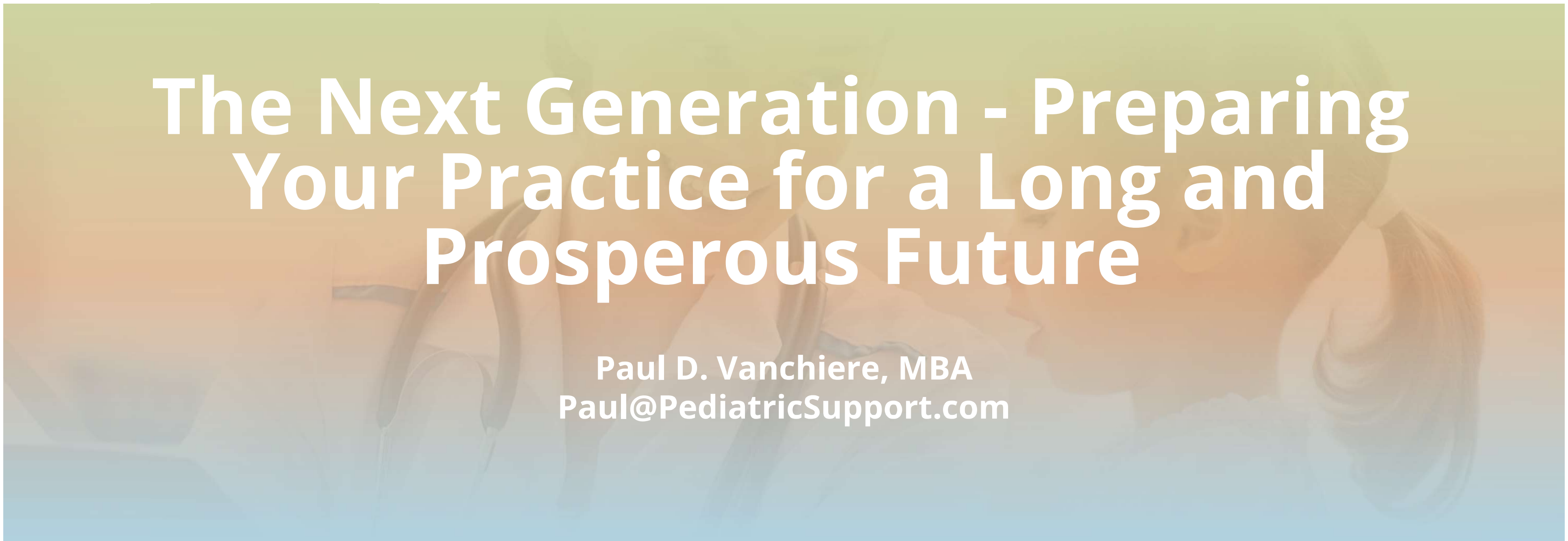

The Next Generation - Preparing Your Practice for a Long and Prosperous Future

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Disclosures:

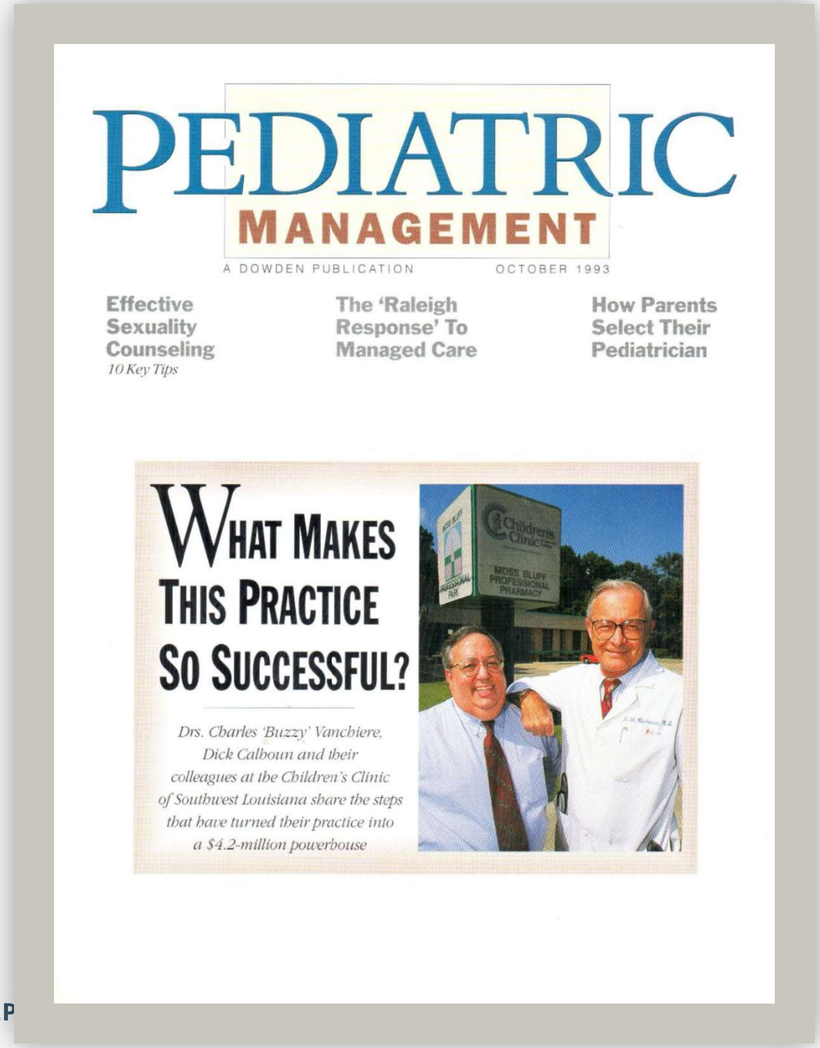
- **Pediatric Management Institute**
  - *Founder/Principal Consultant*
- **Greenwood Pediatrics & All Pediatrics**
  - *Chief Financial Officer*

Today is not a substitute for Legal or Accounting Advice

PMI does not offer legal or accounting services. As such, all information shared should be reviewed with your attorney to ensure compliance with applicable state and federal laws.

Today's presentation focuses on the operational aspects of practice valuations, mergers and/or acquisitions as a guide to educate you on issues involved.

Children's Clinic of Southwest Louisiana, Inc.



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A DOWDEN PUBLICATION OCTOBER 1993

Effective Sexuality Counseling
10 Key Tips

The 'Raleigh Response' To Managed Care

How Parents Select Their Pediatrician

WHAT MAKES THIS PRACTICE SO SUCCESSFUL?

Drs. Charles 'Buzzy' Vanchiere, Dick Calhoun and their colleagues at the Children's Clinic of Southwest Louisiana share the steps that have turned their practice into a $4.2-million powerhouse

Agenda

- Why practice valuations may be needed
- Review some valuations
- Walk through an example
- Things to consider

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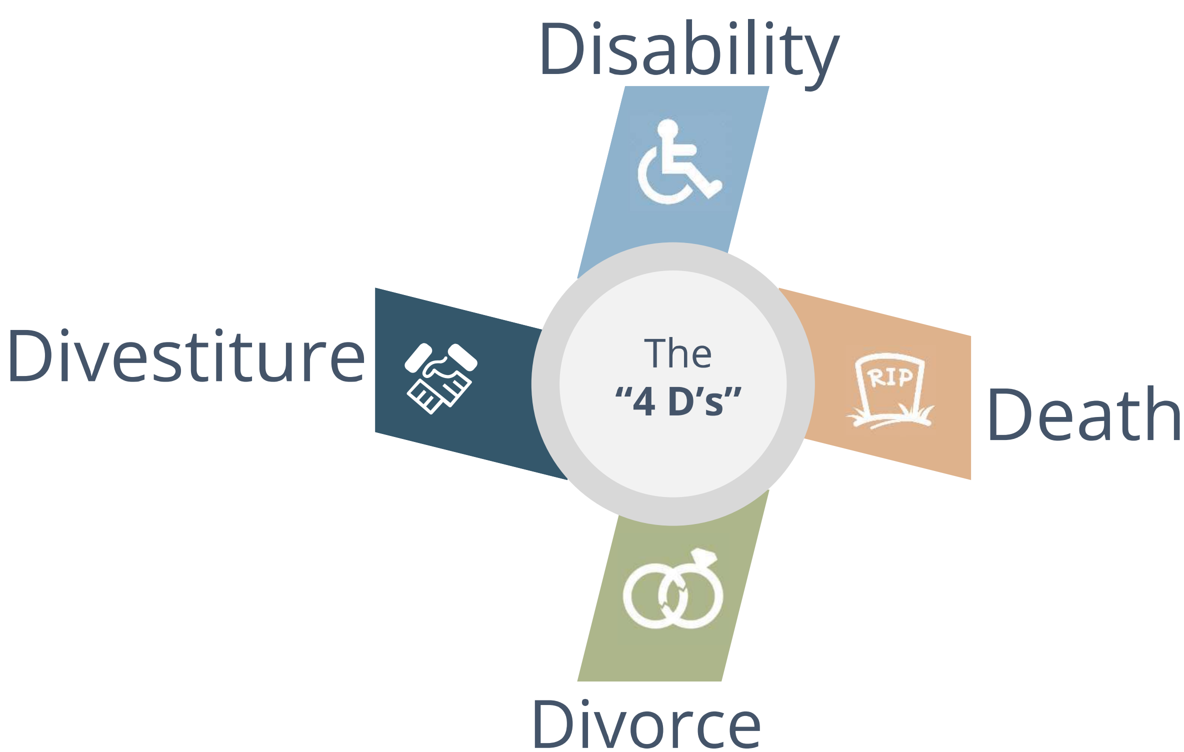
Tough Marketplace…

- Limited qualified buyers
- Limited interest
- No two practices are similar enough to estimate a “fair” price
  - Medicaid/Private pay percentage
  - Lack of standards
- Very different from the housing market to find comparable

Plan for the Future



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Traditional Valuation Methods

Income Approach

Determining the value of the practice by converting future economic benefits into a single present amount

Asset Approach

Determining the practice's value based on the assets net of liabilities.

Market Approach

Comparable Sales- comparing the practice to similar businesses, business ownership interests, securities or intangible assets.

Valuation Objective

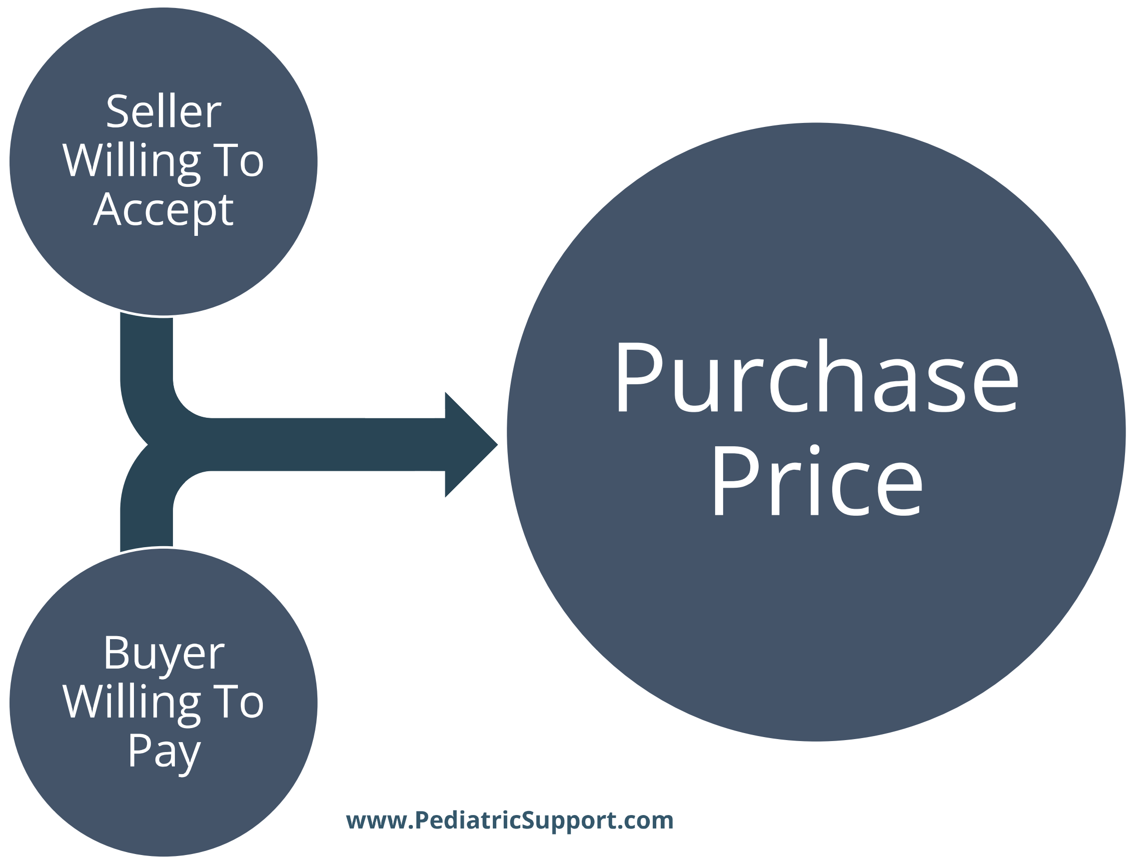
Establish a fair and mutually agreed upon price to facilitate the transfer of ownership in the practice.

Establish a concrete formula that can be referenced or updated as the need arises.

Eliminate Uncertainty

- Set the expectation in advance of the need.
- If you wait until stressful time to establish a value, emotions get in the way of a fair deal for both sides.

What Is A “Fair” Price?



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Succession Planning 101: When You May Need A Partner

Share the workload	Too much for just Paulie or Brandon to do
Share / Mitigate Individual Risk	One (or both) is hesitant to go “all in” on the investment
Need capital for expansion	Neither have the capital to add new locations or expand the practice
Equity redemption	One of them want to move on to fulfill their passion as a rodeo clown

Succession Plans…
…the bad options

Other Options…

Find A Buyer (Internal)
- Existing Provider

Find A Partner
- MSO Companies
- SuperGroup
- CIN/IPA’s

Find A Buyer (External)
- Another group
- New provider in town
- SuperGroup
- PE-Backed Firm

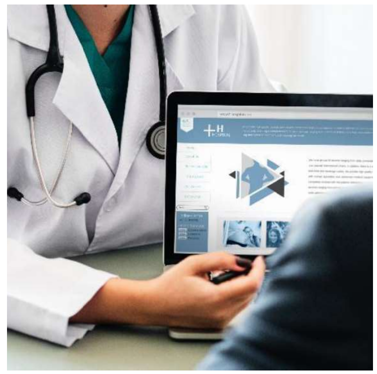
Shut Down

Sell To Hospital

Sell to Hospital

Private Inurement

- Applies to tax exempt hospitals - section 501 (c) (3)
- Defined: No part of a hospital's net earnings may inure to the benefit of any private individual
- Just because a transaction may be "fair market value" does not necessarily make it "commercially



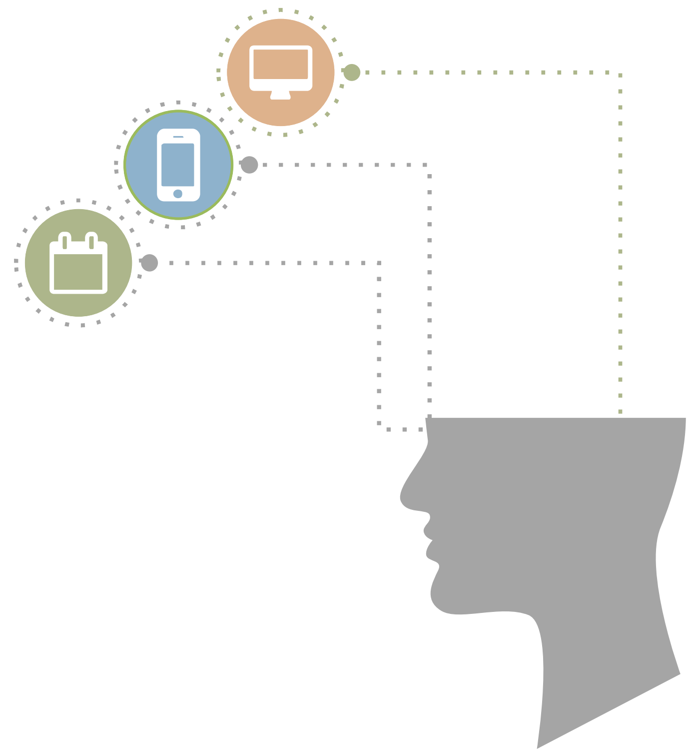
Medicaid Fraud and Abuse

- Known as the "anti-kickback law"
- Prohibits payments, offers, or inducements of any remuneration for referrals
- Issue: If acquisition price exceeds fair market value, transaction may be considered a inducement for referrals "Commercially Reasonable"

Sell to Hospital

Usually Combination Offer

- **Purchase of Current Practice**
  - Asset Driven
- **Future Compensation Package**
  - Base Salary
  - Benefits
  - Production (wRVU Incentives)
  - Limited by “Fair Market Value”
- **Office Building Lease**



Sell to Network of Large Competitor

Offers Access to Better Paying Contracts

Net effect is higher compensation for Pediatricians

- Buyer has payment rates far greater than smaller practice can obtain
- After allocating operating expenses, could see net increase in "take home pay" & benefits
- Usually burdened with higher employee benefit costs
- Loss of autonomy (not as bad if sell to hospital)
- Less headache for seller in the future (HR issues, payroll, etc)

Sell to Private Equity-Backed Firm

- Often stems from the lack of a succession plan
- Concerns about future reduced margins
- Often provides higher redemption value for owners
- Concerns about the loss of autonomy
  - Time for outside interests
  - Expectations related to volume of business
  - Potential issue with decision-making done “outside” the practice
- Can be financially lucrative for practice owners

Goodwill

- **Goodwill** is an intangible asset that arises as a result of the acquisition of one **company** by another for a premium value. The value of a **company's** brand name, solid customer base, good customer relations, good employee relations and any patents or proprietary technology represent **goodwill**.
- Hogwash…benefits of reputation is what drives practice revenue…
- Allocation of “Goodwill” is double-dipping

Year End Cash Bonus vs. Equity

Not unheard of to offer equity in lieu of cash bonus

- Production incentive converted to equity
- Usually a premium above cash value
  - $15k cash bonus or 20% equity

Be careful of tax implication for both parties

Traditional Valuation Methods

Schedule 1

[redacted]

Fair Market Value - Calculation of Value

[redacted]

Summary of Methods Used	Indicated Value	Weight	Weighted Value
Net Tangible Asset Value (Schedule 10)	$ 42,000	-	$ -
Capitalization of Earnings Method (Schedule 13)	-	-	-
Guideline Merged and Acquired Company Method (Schedule 14)	295,000	25.0%	73,750
Goodwill Registry Method (Schedule 23)	170,000	50.0%	85,000
Industry Formula (Schedule 24)	261,000	25.0%	65,250
Totals		100.0%	224,000
Calculation of the Fair Market Value of a 100% equity interest in [redacted] (Rounded)			**$ 224,000**

Net Tangible Asset Value	$ 42,000
Capitalization of Earnings Method	$ -
Guideline Merged and Acquired Company Method	$ 295,000
Goodwill Registry Method	$ 170,000
Industry Formula	$ 161,000

Summary of Results

Average:	$ 133,600
Median:	$ 161,000
Standard Deviation:	$ 104,274

Summary of Results (Toss Out $0.00)

Average:	$ 167,000
Median:	$ 165,500
Standard Deviation:	$ 89,518

The gross collected income for the [redacted] practice for the latest calendar year is $[redacted] The computed price using an amortization of excess earnings approach is $[redacted], which gives a price/gross ratio of 52%.

A review of the practice sale database yields two comparable sales. The comparables compare, contrast, and were sold as follows:

Practice comparable #1		Subject Practice
Gross collected income:	$670,913	$646,677
Actual practice sale price:	$359,000	$335,000
Price / Gross ratio	54%	52%
This practice is located in	Carrollton, Texas	

Practice comparable #2		Subject Practice
Gross collected income:	$757,073	$646,677
Actual practice sale price:	$375,000	$335,000
Price / Gross ratio	50%	52%
This practice is located in	Houston, Texas	

The comparable values stated for each of the above practices were the actual sales prices for those practices. The average price/gross ratio for the two comparable practices is determined to be 52%.

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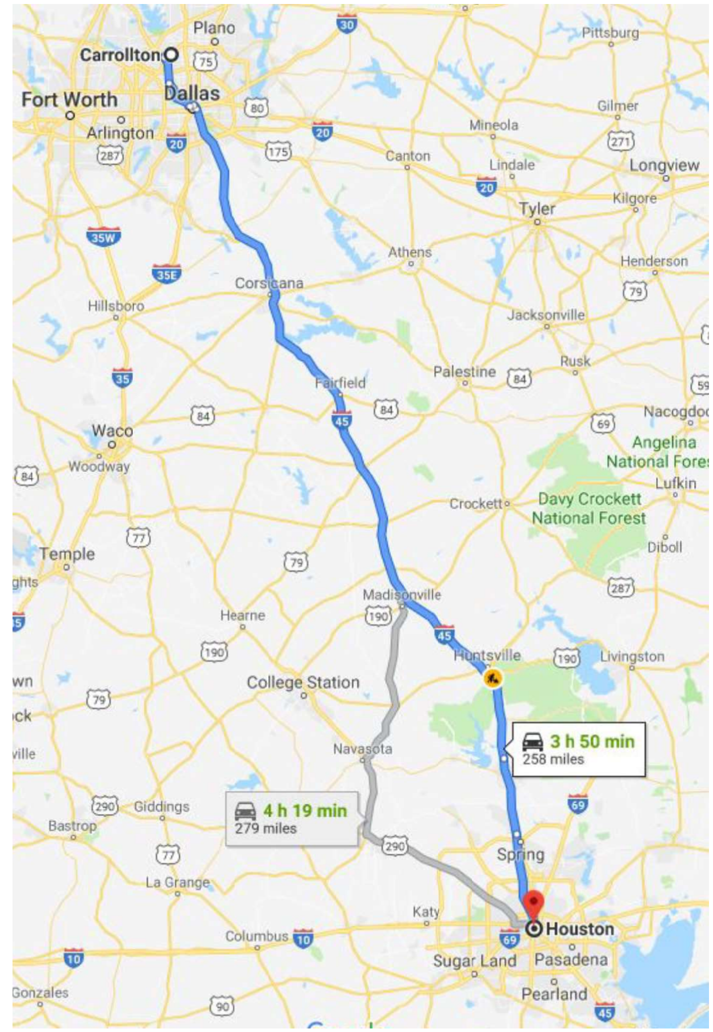
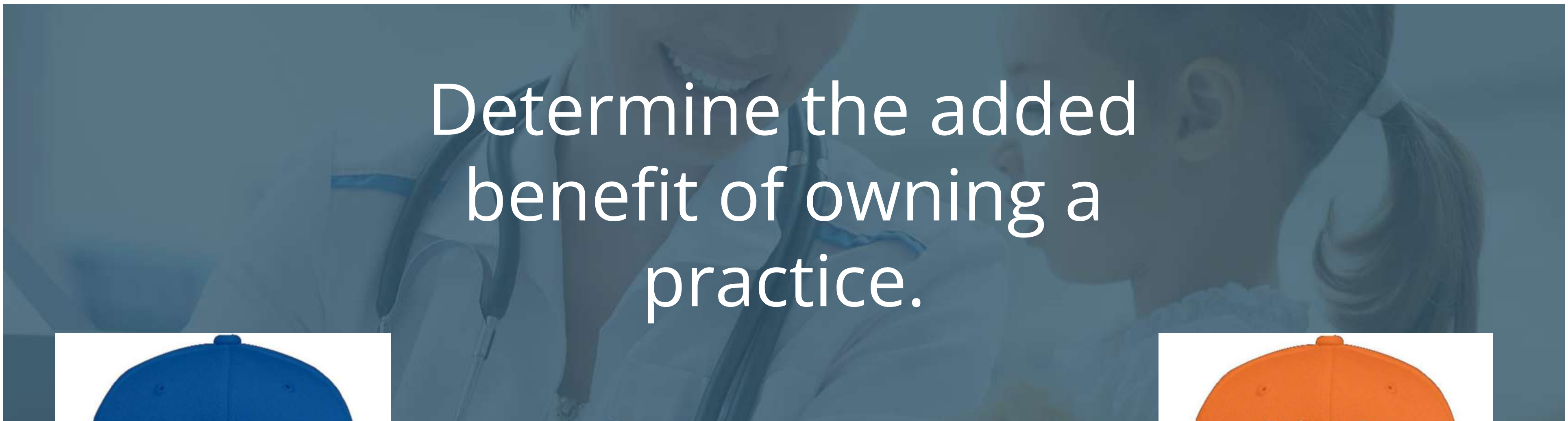


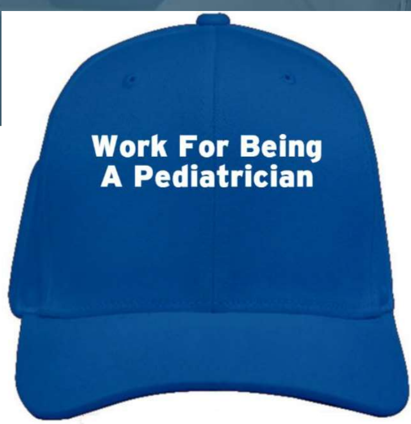
The **essence of mathematics** is not to make *simple things complicated,* but to make complicated things simple.

– Stan Gudder
Mathematician

Goal of Valuation Formula?



Determine the added benefit of owning a practice.



Mindset

Total Compensation:	$ 210,000
"Pediatrician Work":	$ (165,000)
Benefit Of Owning The Practice:	$ 45,000

Scenario

1. Dr. Smith is a 65 year old Pediatrician wants to retire in 2 years
2. Dr. Johnson is a 45 year old Pediatrician has been there for five years, is good fit, and wants to buy the practice
3. 1 NP (Full Time)
4. 1 NP (Part Time)

Practice Valuation Summary

Acme Pediatrics

As Of December 31, 202X

			12/31/2022	Formula	Notes
	Part A- Earnings				
A	Total Revenue	$	2,675,000		*As reported on P&L*
B	Total Expenses	$	(2,600,000)		*As reported on P&L*
C	Other Income	$	80,000		*As reported on P&L*
D	Net Ordinary Income	$	155,000	*Sum A:C*	
E	Owner Draw	$	160,200		*As reported on Provider Comp Summary*
F	Owner Retirement Match	$	7,500		*As reported on Provider Comp Summary*
G	Total Owner Comp/Benefit	$	167,700	*E + F*	
H	12-Month Estimated Total Owner Earnings	$	322,700	*D + G*	
I	Employed Provider Salary	$	160,000		*Actual compare or national statistics*
J	Employed Provider Bonus & Retirement	$	4,800	*I * 3%*	
K	Employed Provider Total Comp	$	164,800	*K + L*	*Salary + Bonus*
L	Number of Partners		1.00		*Listed number of Partners/Owners of Practice*
M	Per Partner Earnings	$	322,700	*J / N*	*Average Partner/Owner Earnings*
N	Variance	$	157,900	*O - M*	*Benefit of owning practice as described in article.*
O	Multiple		1.10		*Multiple Of Earnings Estimated*
P	Part A Total	$	173,690	*P X Q*	*Per Partner/Owner Part A Value*
Q	Part A Total For Practice	**$**	**173,690**	*N X R*	*Total Part A Value For Practice*
	Part B- Assets & Liabilities				
T1	Cash on Hand	$	225,000	*Increase*	*As reported on 012/31/202X Balance Sheet*
T2	Equipment & Furnishings	$	60,000	*Increase*	*30% of Assets Listed On Balance Sheet (Before Dep)*
T3	Other Assets			*Increase*	
T4	Vaccine/Med Supply Inventory	$	45,000	*Increase*	*Total 2022 expense divided by 12 in lieu of inventory count*
T5	Credit Cards & Accounts Payable	$	(52,500)	*Decrease*	*As reported on 12/31/2023 Balance Sheet*
T6	Estimated Accounts Receivable	$	116,847	*Increase*	*Calculated per based on report provided*
T7	**Part B Total**	**$**	**394,347**		*Sum T1:T10*
U	**Total Value (Part A + Part B)**	**$**	**568,037**	*Q + T7*	*Total Earnings Value + Total Asset Value*

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Part B- Assets & Liabilities

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Estimating The A/R Value

Step 1:Determiniation of Gross Collection Rate

Month	Charges	Payments	Adjustments
Aug-18	$ 202,000	$ 113,000	$ 112,000
Sep-18	$ 185,000	$ 96,000	$ 69,500
Oct-18	$ 230,000	$ 125,000	$ 103,500
Nov-18	$ 205,000	$ 127,000	$ 88,000
Dec-18	$ 145,000	$ 83,750	$ 63,000
Jan-19	$ 195,000	$ 95,000	$ 88,000
Feb-19	$ 197,000	$ 107,000	$ 85,000
Mar-19	$ 192,000	$ 97,000	$ 81,000
Apr-19	$ 155,000	$ 98,000	$ 95,000
May-19	$ 228,000	$ 115,000	$ 86,000
Jun-19	$ 180,000	$ 87,000	$ 72,000
Jul-19	$ 152,000	$ 104,000	$ 75,000
	$ 2,266,000	$ 1,247,750	$ 1,018,000
Gross Collection Rate:		**55.06%**	

Estimating The A/R Value

Step 2: Weighted Collectability Based On Balance Age

Insurance

<30 days	$83,000	55.06%	$45,703
31-60 days	$22,000	50.06%	$11,014
61-90 days	$13,000	45.06%	$5,858
> 90 days	$33,000	40.06%	$13,221
Total	$151,000		$75,797

Patient Responsibilty

<30 days	$2,750	40.06%	$1,102
31-60 days	$3,100	30.06%	$932
61-90 days	$5,600	20.06%	$1,124
>91 days	$8,500	10.06%	$855
Total	$19,950		$4,013

Totals

<30 days	$85,750		$46,805
31-60 days	$25,100		$11,946
61-90 days	$18,600		$6,982
>90 days	$41,500		$14,077
Total	$170,950		**$79,809**

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Internal Finance Options

2 Year Buyout					
Sale Price	$ 235,000	$235,000	$235,000	$235,000	$235,000
Downpayment %age	10.00%	15.00%	20.00%	25.00%	30.00%
Downpayment $	$ 23,500	$ 35,250	$ 47,000	$ 58,750	$ 70,500
Balance to Finance	$ 211,500	$199,750	$188,000	$176,250	$164,500
Years to Pay	2	2	2	2	2
WSJ Prime Rate	3.50%	3.50%	3.50%	3.50%	3.50%
Interest Premium	2.25%	2.00%	1.75%	1.50%	1.25%
Total Interest	5.75%	5.50%	5.25%	5.00%	4.75%
Monthly Payment	**$9,350**	**$8,808**	**$8,269**	**$7,732**	**$7,198**
Annual Amount	$112,200	$105,697	$99,227	$92,788	$86,381

3 Year Buyout					
Sale Price	$ 235,000	$235,000	$235,000	$235,000	$235,000
Downpayment %age	10.00%	15.00%	20.00%	25.00%	30.00%
Downpayment $	$ 23,500	$ 35,250	$ 47,000	$ 58,750	$ 70,500
Balance to Finance	$ 211,500	$199,750	$188,000	$176,250	$164,500
Years to Pay	3	3	3	3	3
WSJ Prime Rate	3.50%	3.50%	3.50%	3.50%	3.50%
Interest Premium	3.75%	3.50%	3.25%	3.00%	2.75%
Total Interest	7.25%	7.00%	6.75%	6.50%	6.25%
Monthly Payment	**$6,555**	**$6,168**	**$5,783**	**$5,402**	**$5,023**
Annual Amount	$78,657	$74,012	$69,401	$64,823	$60,277

NT

How Much Is Too Much To Buy Into A Practice?

Token Payment?

Key Factors Impacting the Valuation of a Pediatric Practice

- Continuation of Patient Volume
  2 visits per day at $150 per encounter
  =
  $60,000 swing in payments per provider per year (200 days)
- Continuation of Current Payment Rates
- Shift in Payor Mix
- Local Economy
- Building/Rent Expenses along with future liabilities
  - Need to relocate to better location
  - Interior Updating

Earnings Surveys For Comparison Compensation

- MGMA Cost and Productivity Report
- MGMA Physician Compensation Survey
- American Medical Group Association (AMGA)
- Currently Employed Pediatricians
- Modern Healthcare's Physician Compensation Report

Adjustments

01 Taking average shareholder salary for previous 2 or 3 years.

02 Adjusting Average Shareholder Compensation based on PPE, ERC, or Government COVID funds

03 Adjusting Average Shareholder Compensation based on whether or not the shareholders may have previously taken lower salaries to fund practice projects that are expected to generate additional earnings in the future.

04 Adjusting for a variety of nuances in the shareholder compensation formula and other Shareholder Concerns

Considerations

1. Continued Employment for Dr. Smith
2. Management Responsibilities
3. Future Compensation
4. Do Not Intermingle Buyout and Future Salary
   Need two separate agreements (Buy/Sell and Employment)
5. Internally Financed or Require Cash?
6. Right of First Refusal to Repurchase Practice In Future
7. Include Practice Real Estate
   Not a good idea to do so
8. Is it a fair deal for both sides?

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Considerations

Ownership position immediate or as paid in?

01 If financed, should be immediate since liability created between buyer and seller

02 If cash sale, immediate

03 If in lieu of bonus(es)- maybe deferred

Common Question/Request

Should the ownership position be proportional to the amount actually paid towards the purchase price?

Purchase Price: $200,000

Year One Payment	$ 50,000	25.00%
Year Two Payment	$ 50,000	50.00%
Year Three Payment	$ 50,000	75.00%
Year Four Payment	$ 50,000	100.00%

- If price set in advance and financing terms in place, no.
- If agree to reestablish the value each year, acceptable.

Financing Issues & Ownership Interest

- Agree to purchase price & terms
  - Purchase Agreement
  - Financing Agreement
    - Cash Payment
    - Finance With Ford Credit
    - Bank Loan

- You receive 100% ownership of car
  - Subject to lien (if any)

Shareholder/Partnership Considerations

- Personal Responsibility for Coding
- Insurability for Life Insurance
- Spouse Signatures
- Personal Guarantees for Current Debt
- Consecutive Days Out of Office
- Disability- Continue to pay until insurance kicks in
- Failure to Plan Provision- Discounted if no notice
- Pledging of Assets- Prevent Collateralization
- Personal Bankruptcy- Allow practice to purchase before third party becomes owner
- Future Plans/Expansion- Finance expansions with “cheap” loan options

- **Valuation Updated Annually**