



What is the Value of my Medical Practice?

By Eric Yetter

This article focuses on how medical practices are valued by private equity-backed groups, and to an extent, health systems and other strategic acquirers. Only some specialties are candidates for this type of transaction, while others may rely on more traditional physician-to-physician deals (often buying and selling for asset value plus “goodwill”).

Specialties that are currently candidates for private equity acquisition include ophthalmology, dermatology, ENT, pain management, urology, women’s health, orthopedics, oncology, cardiology, neurology, nephrology, rheumatology, gastroenterology, and both general and specialty dentists. Emergency medicine, radiology, and anesthesiology groups may also be candidates for acquisition by longer-established acquirers.

Physician practices are almost always valued on a multiple of EBITDA basis in transactions with private equity groups or similar buyers. That is,

$$\text{EBITDA} \times \text{EBITDA Multiple} = \text{Valuation}$$

The key inputs are 1) the practice’s EBITDA, and 2) the EBITDA multiple. We explore each in turn below.

Determining EBITDA

The term “EBITDA” stands for Earnings Before Interest, Taxes, Depreciation, and Amortization. However, most transactions are technically valued with a multiple of “Adjusted EBITDA”, which means the simple EBITDA calculation above plus adjustments for key items – most often non-recurring expenses, excess owner compensation and benefits, and sometimes proforma adjustments for new providers and other near-term growth opportunities.

In using the term EBITDA here, we are referring to Transaction EBITDA, which means whatever calculation of EBITDA is used in the relevant transaction.

EBITDA is typically calculated using the steps below:

1. Determine the practice's net profit in the most recent twelve-month period.
2. Add the following expenses back (add them to your net profit)
 - a. The core "EBITDA" elements – interest, taxes (generally income taxes only), depreciation, and amortization.
 - b. All owners' compensation and benefits (including anything like auto leases, retirement contributions etc. and payroll taxes related to the owners)
 - c. Any non-recurring expenses – meaning expenses that were one-time in nature, have been eliminated going forward, or should have been characterized as capital investment vs. an expense. Keep in mind that buyers will make sure you are not adding back expenses that are necessary to continue operating the practice.
3. Occasionally, revenue should be adjusted due to non-recurring items (e.g., COVID-19 related payments) or absences (e.g., a physician was out on medical leave) and similar matters.
4. Subtract any compensation and benefits that owners will receive for professional services provided after the transaction closes.
 - a. Usually, selling physicians are paid for the professional services they provide after closing under a new employment agreement with the buyer. The compensation formula is most often a percentage of professional collections, but it can also be a share of profits available for distribution, an RVU based calculation, or a combination of factors.
 - b. Add expected benefits and payroll taxes to that amount.
5. Optional – make further adjustments for "pro forma" future items. For example, if a new physician has been hired and has not yet reached full productivity, it might make sense to adjust as if that physician was at their full expected performance level. Pro forma adjustments can be appropriate where expectations are sufficiently concrete, which is determined on a case-by-case basis.

Now, we have a calculation for EBITDA:

$$\begin{array}{r} \text{Net Income} \\ \textit{plus} \\ \text{Interest, Taxes, Depreciation, and Amortization} \\ \textit{plus} \\ \text{Owners' Historic Compensation and Benefits} \\ \textit{plus} \\ \text{Non-Recurring and Other Appropriate Expense Adjustments} \\ \textit{plus/minus} \\ \text{Any Adjustments to Revenue} \\ \textit{minus} \\ \text{Owners' Post-Transaction Compensation} \\ \textit{plus} \\ \text{Any Pro-Forma Adjustments} \\ \textit{equals} \\ \text{EBITDA} \end{array}$$

Determining the EBITDA Multiple

Once EBITDA is calculated, a multiple is applied to arrive at transaction value. For example, a practice with \$4,000,000 in EBITDA selling at a 10x multiple yields \$40,000,000 in transaction value. The math is simple here, but determining the multiple is multifaceted.

EBITDA multiples are generally determined by various factors, which blend in a non-formulaic way. It is perhaps more an art than a science and dictated by the human element; multiples are influenced by outlook, capital markets, comparable transactions, and general sentiment in the community. Key items include:

1. Profitability – Practices with higher EBITDA tend to receive higher multiples. E.g., a practice with \$1M EBITDA might receive a 7x multiple, whereas one with \$5M EBITDA might receive a 12x multiple.
2. Durability – Practices with durable operations tend to be valued at higher multiples. Again, this is multifaceted and can include factors like:
 - a. Payor mix
 - b. Case mix
 - c. Depth of provider bench
 - d. Ages of providers
 - e. Referral sources
 - f. Supply and demand forces in the local market and generally in the specialty
 - g. Ease of provider recruitment in the area
3. Growth Prospects – Practices with robust growth opportunities to add new ancillaries, new providers, locations, etc. tend to receive higher multiples.
4. Economic Market – Multiples are heavily influenced by investor sentiment in the market including:
 - a. General private equity sentiment, including interest rates on debt sometimes used to fund acquisitions, what comparable companies have been sold at (other PE groups selling their investments), and the fundraising environment (where PE groups raise the money they invest).
 - b. Specifics to the specialty, including its unique reimbursement outlook and other supply and demand factors.
5. Specific value to a buyer – certain buyers may see special strategic value in a practice based on their own current operations or plans.

All above factors blend to set the multiple in each transaction, and different buyers will often value a practice using different multiples (based on unique view of each factor above).

Pursuing a Deal

Physician sellers can maximize their transaction value by working with a team of experienced advisors. At FOCUS, we offer a preparation, marketing, and closing process that is tailored to physician groups and designed to attack the factors listed above. It allows us to maximize EBITDA, maximize the multiple, and maximize value.

KEY FACTS

- Team: 5 investment bankers and 1 senior advisor
- One of the most experienced sell-side advisors in private equity/physician deals – over 20 entities sold
- A proven process to create competition and maximize client value
- Deep experience with medical practice/ancillary operations; informs identification of future growth opportunities

<p>This announcement appears as a matter of record only.</p> <p>THE CENTER FOR DERMATOLOGY CARE has been acquired by FOREFRONT DERMATOLOGY a portfolio company of Partners Group</p> <p>A FOCUS Managing Director represented The Center for Dermatology Care and introduced this transaction while working at a prior firm.</p>	<p>This announcement appears as a matter of record only.</p> <p>Lee SURGERY CENTER has been acquired by MIDWEST VISION PARTNERS</p> <p>The undersigned initiated this transaction, assisted in the negotiations, and acted as financial advisor to Lee Surgery Center.</p> <p>FOCUS</p>	<p>This announcement appears as a matter of record only.</p> <p>Interventional Pain Management Practice has been acquired by a PE-Backed Practice Management Organization</p> <p>The undersigned initiated this transaction, assisted in the negotiations, and acted as financial advisor to Interventional Pain Management.</p> <p>FOCUS</p>	<p>This announcement appears as a matter of record only.</p> <p>Vista SURGICAL CENTER has been acquired by SURGERY PARTNERS</p> <p>A FOCUS Managing Director represented Vista Surgical Center and introduced this transaction while working at a prior firm.</p>	<p>This announcement appears as a matter of record only.</p> <p>VISTA EYE SPECIALISTS has been acquired by ATLANTIC VISION PARTNERS a portfolio company of SHERIDAN LITHIA, NETS</p> <p>The undersigned initiated this transaction, assisted in the negotiations, and acted as financial advisor to Vista Eye Specialists.</p> <p>FOCUS</p>	<p>This announcement appears as a matter of record only.</p> <p>The Retina Eye Center has been acquired by RETINA SPECIALTY GROUP OF AMERICA</p> <p>The undersigned initiated this transaction, assisted in the negotiations, and acted as financial advisor to The Retina Eye Center.</p> <p>FOCUS</p>
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About FOCUS Investment Banking LLC

With more than four decades of experience, [FOCUS Investment Banking](http://www.focusbankers.com/) is a trusted name in M&A advisory services worldwide. FOCUS works to understand each client's strategic and financial objectives, craft the best plan to achieve these goals, and deliver success. Whether helping to sell, buy, or raise capital, FOCUS strives to maximize the value of every transaction to the benefit of its clients. FOCUS bankers are seasoned operating and financial executives with extensive transaction experience. Securities transactions conducted by FOCUS Securities LLC, an affiliated company, registered Broker Dealer member FINRA/SIPC. For more information on FOCUS, please visit <http://www.focusbankers.com/>.