

How Much is a Medical Practice Worth?

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Medical practices that want to purchase another medical practice need to understand the different ways of valuing a medical practice depending on whether the whole practice is being purchased or whether it will be merged with an existing practice. There are many factors that determine the value of any medical practice, including the value of the assets, the income the practice can yield, the liabilities of the medical practice, the type of care being provided, the reputation and experience of the medical practice being acquired, and many other factors.

When two medical practices merge, many of the same factors that are used to value a medical practice should be reviewed by both practices to help determine if the merger is wise.

Experienced healthcare lawyers help medical practices understand the factors that are used to determine the financial value of a medical practice, the ability to obtain financing, other factors that may affect the ability of the new medical practice to produce income, the ability to expand the medical services to more patients, and many other financial value issues. We also work with financial appraisers who are skilled at placing a value on a medical practice.

LEGAL KEYS EVERY MEDICAL DOCTOR MUST KNOW BEFORE MERGING WITH OR ACQUIRING A MEDICAL PRACTICE

If you plan to acquire a medical practice or any healthcare venture, consult a healthcare and FDA attorney who understands the specific legal and regulatory landscape

Medical practice valuation methods include the following:

Using a multiplier

This method examines the general revenue of the business – the amount of yearly receipts for medical services – and then multiplies that amount by a “multiplier” which varies depending on the type of practice, the location, and many other factors.

The fair market value (FMV) approach

This financial appraisal method examines similar medical practices in the region where you practice. Whether a practice is similar must take into account the type of practice, the number of physicians, the services that are offered, how long the medical practice has been in office, and other factors.

The FMV is commonly used in the buying and selling of a home or a building. The difference is that the sales of homes are

generally of public record because the sale is recorded with the local county offices. Medical sales are generally not publicly recorded. Even if the sales of comparable medical practices are recorded, there often are not enough comparable sales to make a reliable analysis.

The income approach

This approach examines the cash flow of the practice – usually for the past few years – and the potential future income that the practice can expect to generate. The income approach analyzes the following:

- **Analyzing the stream of income.** This analysis normally examines prior tax returns and financial statements along with other documents to determine the “net” income of the business. The net figure considers the liabilities of the practice starting with the federal, state, and local tax returns. The analysis may differ depending on the type of medical practice, how the bills are submitted and paid, and other standards.
- **Forecasting the future income flow.** This analysis reviews market trends, the overall industry outlook for your type of practice, and any other information that can indicate how much income the medical practice will generate over the next 3-5 years.
- **Growth and risk factors.** This part of the income analysis examines the competition, how much the practice is regulated, the possibilities for providing additional services, and the growth potential of the medical practice.
- **Applying a discount rate.** An analysis of future income needs to be discounted to reflect the rate of return the practice would obtain if the practice just invested the funds in safe investments such as certificates of deposit. “The discount rate is typically based on industry benchmarks, market rates of return, and the specific risk profile of the practice.” The discount rate is then used to determine the current value of the medical practice.
- **The termination value.** This analysis estimates the value of the practice at the end of a specific term such as 3-5 years.

Whether the income approach is the best way to value a medical practice is debatable. We’ll explain whether this approach is reliable – especially in light of other factors such as an aging population or any likely expenditures over and above normal overhead.

The asset approach

This method is more common for valuing a medical practice. The approach examines the tangible assets of the practice, the intangible assets, and the goodwill of the medical practice. This approach helps determine the value of each type of asset. The approach is useful for accounting and tax purposes.

The asset approach generally uses the following analysis:

- **The tangible assets.** This portion of the value includes the physical items in the office including the medical equipment, fixtures, furniture, and filing cabinets. The value is what a willing buyer would pay for these items – not what the practice originally paid for the items or how much the seller thinks the assets are worth. A big expense for any medical practice is the cost of medical equipment such as diagnostic equipment, software and hardware, surgical tools, and other types of healthcare equipment. A key question is whether the new practice will buy these assets or rent them.
- **The revenue of the medical practice.** This figure represents the total receipts of the practice before considering the expenses. This sum is the gross income. For a medical practice, gross income generally means the accounts receivable and any income from lectures or other health services.
- **The net income of the medical practice.** This sum is the profit – the amount the medical practice receives (takes in) minus – the amount of the expenses and operating costs – such as the computer costs, salaries, and rental costs.
- **Any add-backs.** These items include such things as the benefits to the doctors such as healthcare, travel reimbursements, salary, and other items.
- **Goodwill.** This asset is essentially the medical practice’s reputation. Generally, the practice that is buying the business also

wants to acquire the patients of the other practice (or keep those patients) if there is a merger. As we explained in our general discussion on acquiring or merging a medical practice, there are certain legal and ethical considerations to ensure that patients can make free decisions about which doctors the patients will use and their electronic health records. Goodwill is essentially a calculation as to whether the old patients will continue to see the doctors in the new medical practice. Goodwill also includes the location of the practice, how well the staff connects with patients, and other factors.

Other factors include the expenses of the business and any intellectual property such as patents. Another issue is that the new practice may not assume some of the expenses of the old office. For example, the buyer may keep some of the staff but not all of the staff or some of the equipment but not all of the equipment.

Additional valuation factors for a medical practice

A few other notable factors that will affect the value of a medical practice include:

- The general state of the economy.
- The payment arrangement including whether there is a full payment or the sale of the practice is financed by having the seller accept payments over time as the new practice evolves. The payment terms may also have tax consequences.
- Tax considerations. The tax considerations do affect how much a buyer will be willing to pay for a medical practice and how much the seller will accept.
- The need for cash. A doctor who is retiring may be more in need of cash now than a younger doctor who is quitting to pursue other interests and has the time to accept a payout.
- Whether other medical practices are interested in the same practice that is being sold

Generally, the more a medical business has been in existence and the better reputation that practice has, the higher the value of the medical practice will be.

Many other factors may also affect the value of a medical practice.

HEALTHCARE M&A: DO'S AND DON'TS OF BUYING OR SELLING A MEDICAL PRACTICE

Buying and selling a medical practice is much different than selling a commercial business. Due diligence must address special healthcare legal compliance issues, licensing requirements, patient [...]

Other factors to consider regarding the cash flow of a business include:

Income cash flow issues

- The cost of replacing office space or equipment that cannot be transferred to the new practice.
- The cost to hire new physicians and other medical care providers.
- Whether Stark Law or AKS affects these purchases and compensation needs.
- How likely the doctors in the practice that is being bought are to help the new practice during the transition period

Legal costs

The cost of any litigation if the business being acquired has any judgments, current lawsuits, or lawsuits that may be filed. Any outstanding contracts and other obligations that should be obtained through a due diligence review.

According to Medical Economics, the appraisal of a medical practice should also examine where existing and new patients are coming from, and examine all the contracts with doctors and nonphysician providers. It's very important to actually visit the medical office you're acquiring.

Some offers may be subject to negotiation. Other offers may be one-time offers. Aesthetics can add value to a medical practice. If the medical practice you're acquiring has an MSO, that can add value by simplifying the need to separate the business side of the practice from the medical/clinical side of the practice.

Medical practices can be valued in different ways – by using a multiplier, fair market value comparables, estimating net income, and the value of tangible and intangible assets including goodwill. Our seasoned healthcare lawyers work with medical appraisers who are skilled at placing value on a medical business. Our team is skilled at all the related issues such as legal and healthcare compliance, financing issues, agreements of sale, and other issues.

Any medical practice that is considering buying from, selling to, or merging with another medical practice should contact Cohen Healthcare Law Group to discuss their legal and healthcare compliance requirements. Our experienced healthcare attorneys advise doctors and practices about valuing a medical practice and healthcare compliance laws and regulations.

[Book Your Legal Strategy Session Today](#)

Contact our healthcare law and FDA attorneys for legal advice relevant to your healthcare venture.