

Figure 10-1

SUMMATION OF PRACTICE ASSETS

I. Estimated FMV of Tangible Assets of the Practice

A. FMV of Dental Equipment, Office Equipment, Furniture and Cabinetry/Balance Sheet Approach

1.	Furniture and Fixtures.....	\$ 162,808
2.	Accumulated Depreciation — Furniture and Fixtures.....	<\$ 125,041>
3.	Book Value	\$ 37,767
4.	Accumulated Depreciation — Furniture and Fixtures.....	\$ 125,041
5.	1/3 Multiple.....	<u>x 1/3</u>
6.	1/3 of Accumulated Depreciation — Furniture and Fixtures.....	\$ 41,264
7.	Book Value, plus 1/3 Accumulated Depreciation — Furniture and Fixtures	\$ 79,031
8.	Estimated FMV of Dental Equipment, Office Equipment, Furniture and Cabinetry	\$ 79,031

B. Leasehold Improvements

1.	Leasehold Improvements	\$ 22,389
2.	Accumulated Depreciation — Leasehold Improvements	<\$ 14,725>
3.	Estimated FMV of Improvements	\$ 7,664

C. Dental and Office Supplies

1.	Dental and Office Supplies.....	\$ 46,800
2.	Divided by 12 Months	<u>? 12</u>
3.	Cost of Dental and Office Supplies Monthly.....	\$ 3,900
4.	Three Month Multiple.....	<u>x 3</u>
5.	Estimated FMV of Dental and Office Supplies	\$ 11,700

D. Dental Instruments @ 20% of \$10,000..... \$ 2,400

1.	Estimated FMV of Dental Instruments	\$ 2,400
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Figure 10-1

E.	Recap of Tangible Asset Categories	
1.	Dental Equipment, Office Equipment, Furniture and Cabinetry	\$ 79,031
2.	Leasehold Improvements and Furniture.....	\$ 7,664
3.	Dental and Office Supplies.....	\$ 11,700
4.	Dental Instruments.....	<u>\$ 2,400</u>
5.	Estimated FMV of Tangible Assets of the Practice	\$100,795
II.	Agreed Intangible Asset Value of the Practice or Selling Owner at 37% of Practice Gross Revenues of \$432,000	\$158,405

Figure 10-2

PRACTICE PROFILE FACTORS FOR

SELECTION OF CAPITALIZATION AND GOODWILL RATES

1. Annual owner compensation in all forms
2. Annual gross revenues of the practice
3. Operating expenses as a percentage of gross revenues
4. Ability of the seller(s) to transfer the patients and/or referral sources of the practice
5. Number of active patients/referral sources in the practice
6. Number of new patients per month and degree of patient turnover/The number of referral sources in the practice
7. Stability of the practice and surrounding community
8. Competition
9. Fee structure
10. Practice location
11. Demographic characteristics of patients, location, age and income
12. Likelihood that staff, including any associate doctor(s), will remain with the practice after it is sold
13. Availability of seller assisted financing
14. Facility design and square footage
15. Number of treatment rooms, age and condition of dental equipment (right or left handed)
16. Overall appearance, aesthetics and condition of practice facility
17. Reputation of the practice
18. The number of hours and days worked per year
19. The percentage of patients covered by insurance/managed care/medicaid/other
20. Assignability and term of lease/availability of practice facility, land and building, for purchase

Figure 10-2

21. Ability to expand the practice facility
22. Patient and/or referral source demographics
23. Percentage of collections to gross revenues and age
24. Willingness of seller to assist the purchaser in practice transition
25. Parking and of public transportation availability
26. Effectiveness of recall system
27. Quality of patient records and clinical work performed
28. Quality and experience of staff and degree of turnover
29. Effectiveness of management systems
30. Entity form/completeness of accounting and legal records, as well as any owner agreements, e.g., buy-sell agreement

Figure 10-3

PURCHASE ANALYSIS

1.	Practice Gross Revenues.....	\$ 432,000
2.	Proposed Selling Price of Practice at 60% of Gross Revenues: (Tangible Assets, \$100,795; Goodwill, \$158,405 or 37% of One Year's Gross Revenues).....	\$ 259,200
3.	Less: Payment of Debt Service for Practice (Yearly Payment of Selling Price Over 5 Years @ 9%).....	\$ 64,580
4.	Less: Working Capital (Yearly Payment of \$30,000, Payable Over 5 Years @ 9%)	<\$ 7,473>
5.	Less: Remodeling and Equipment Replacement Costs (Yearly Payment of \$40,000, Payable Over 5 Years @ 9%).....	<\$ 9,964>
6.	Practice Operating Expenses @ 60% of Gross Revenues	\$259,200
7.	Adjusted Yearly Owner Compensation.....	\$172,800
	(Owner's net profit from Federal income tax return, plus: (i) automobile expense; (ii) existing equipment lease paid off by the selling doctor; (iii) retirement plan contribution for the doctor(s); (iv) continuing education; (v) travel expense; (vi) entertainment expense, less: (i) rental increase after acquisition; (ii) wages, part-time employee)	
8.	Less: Total of Items 3, 4 & 5	< <u>\$ 82,017</u> >
9.	Compensation Available for Purchaser	\$ 90,783

Figure 10-3

10. Ratio of Compensation for Purchaser to Average
Gross Revenues where Initial Remodeling, Equipment
Costs and Working Capital are Considered
 $(\$90,783 \div \$432,000 = 21\%) \dots\dots\dots 21\%$
11. Ratio of Compensation for Purchaser to Average
Gross Revenues where Initial Remodeling,
Equipment, and Working Capital Are Not Considered
(\$172,800, Less Yearly Payment Of Acquisition Price
of \$64,580 = \$108,220)
 $(\$108,220 \div \$432,000 = 25\%) \dots\dots\dots 25\%$

Considerations

1. Decrease Purchase Price
2. Increase Payment Term
3. Accept 21% or 25% as Compensation While Practice is Paid For
4. Acquire Another Practice
5. Start Your Own Practice
6. Increase Revenues — Are You Selling or Acquiring Potential?
7. What if Revenues and/or Referral Sources Decrease?

Figure 10-4

**CAPITALIZATION OF PRACTICE EARNINGS/
VERIFICATION ANALYSIS**

1.	Gross Revenues	\$ 432,000	
2.	Operating Expenses	\$ 259,200	
3.	Less: Remodeling and Equipment Replacement Costs (Yearly Payment of \$40,000, Payable over 5 Years at 9%):	<\$ 9,964>	
4.	Less Working Capital Needs (Yearly Payment of \$30,000, Payable over 5 Years @ 9%):.....	<\$ 7,473>	
5.	Subtotal: Operating Expenses, Remodeling and Equipment Replacement Costs and Working Capital Needs:	\$ 276,637	
6.	Yearly Available Owner Compensation in All Forms.....	\$ 155,363	
7.	Less, Compensation Requirements for Purchaser @ 25% of Practice Gross Revenues:	\$ 108,000	
8.	Yearly Available Owner Compensation In All Forms.....	\$ 155,363	
9.	Less, Purchaser Compensation Requirements.....	<u>\$ 108,000</u>	
10.	Yearly Available Sum to Pay Purchase Price, Inclusive of Interest.....	\$ 47,363	
11.	Above Sum Capitalized @ 20%, Payable over 5 Years, Inclusive of Interest:	\$ 236,815	
12.	Above Sum, Adjusted for 9% Interest/Purchaser Price of Practice	\$ 190,130	
13.	Purchase Price as a Percentage of Practice Gross Revenues:	<u>\$ 190,130</u>	
		\$ 432,000	= 44%

Assuming that the Purchaser requires 25% of gross collections as compensation, and that the purchase price will be paid over 5 years, given 9% interest, as well as working capital and equipment replacement needs, the purchase price would approximate \$190,130.00 or 44% of practice gross revenues. This assumes owner compensation in all forms of 40%.

Figure 10-5

EXCESS EARNINGS METHOD

1.	Tangible Assets.....	\$ 100,795
2.	10% Return of Tangible Asset Investment	\$ 10,080
3.	Adjusted Owner Compensation.....	\$ 172,800
4.	Amount in Excess of 10% Return (Adjusted Owner Compensation, \$172,800, less 10% Return of \$10,080).....	\$ 162,720
5.	Agreeable Compensation for Purchaser.....	\$ 108,000
6.	Equipment Replacement and Working Capital-Yearly Payment, Based Upon Figure 10-3.....	\$ <18,263>
7.	Excess Earnings.....	\$ 36,007
8.	Intangible Assets (Earnings \$36,007.00 x 3*).....	\$ 108,021
9.	Practice Value (Tangible Assets: \$82,600, plus 10% Return of \$10,080 plus Intangible Assets).....	\$ 200,701

*A multiple of 3 was used, as a multiple of 5 or a 20% capitalization rate may have included tangible asset value. Therefore, a lower multiple or higher capitalization rate was used as tangible value is in addition to the intangible value.

Figure 10-6

MULTIPLE OF PRACTICE GROSS REVENUES

Gross Revenues.....	\$ 432,000
Gross Revenue Multiplier.....	<u> x 55%</u>
Practice Value.....	\$ 237,600

Figure 10-7

RECAP OF PRACTICE VALUES

Summation of Assets.....	\$ 259,200
Capitalization of Earnings/Verification Analysis.....	\$ 190,130
Excess Earnings Method	\$ 200,701
Gross Revenue Multiplier.....	<u>\$ 237,600</u>
Subtotal	\$ 887,631
	<u> ? 4</u>
Total Practice Value.....	\$ 221,908

Irrespective of the appraised practice value, the capitalization of earnings/verification analysis only supports a purchase price of \$190,130. Therefore, if the purchaser has equipment replacement costs, working capital needs, 40% profitability, no reduction in gross revenues, is willing to receive 25% of gross revenues as compensation, and desires to pay for the acquired practice over 5 years, the purchase price should be \$190,130, not \$221,908.