Efficiently Planning for Practice Succession

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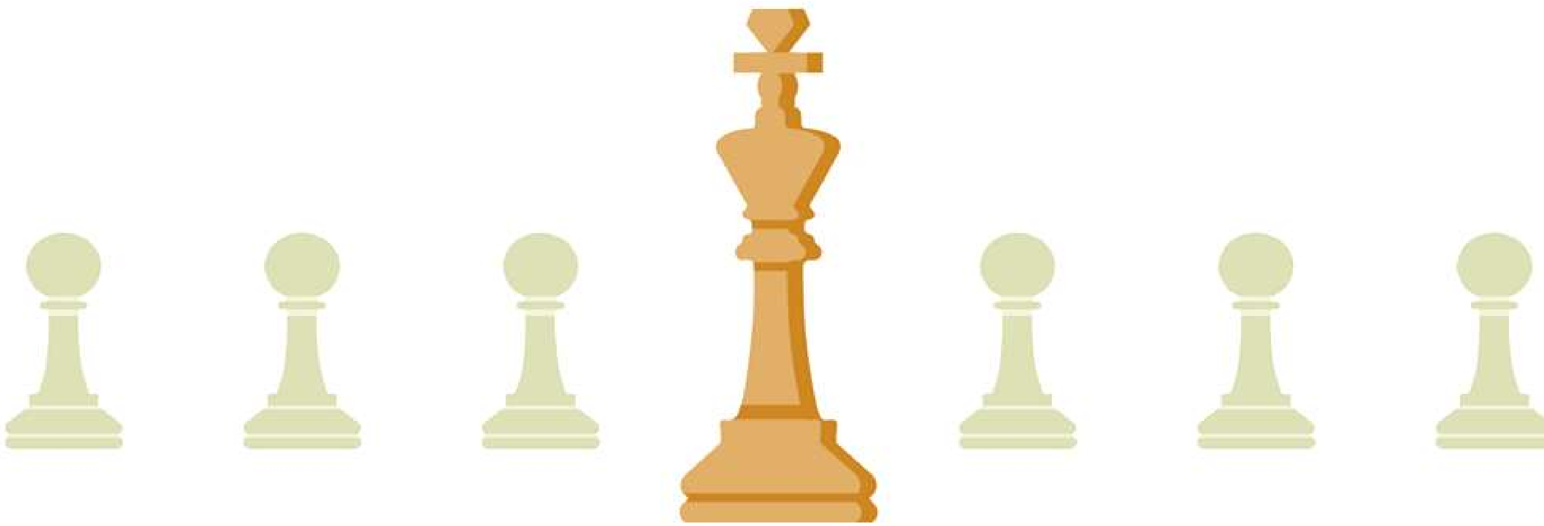
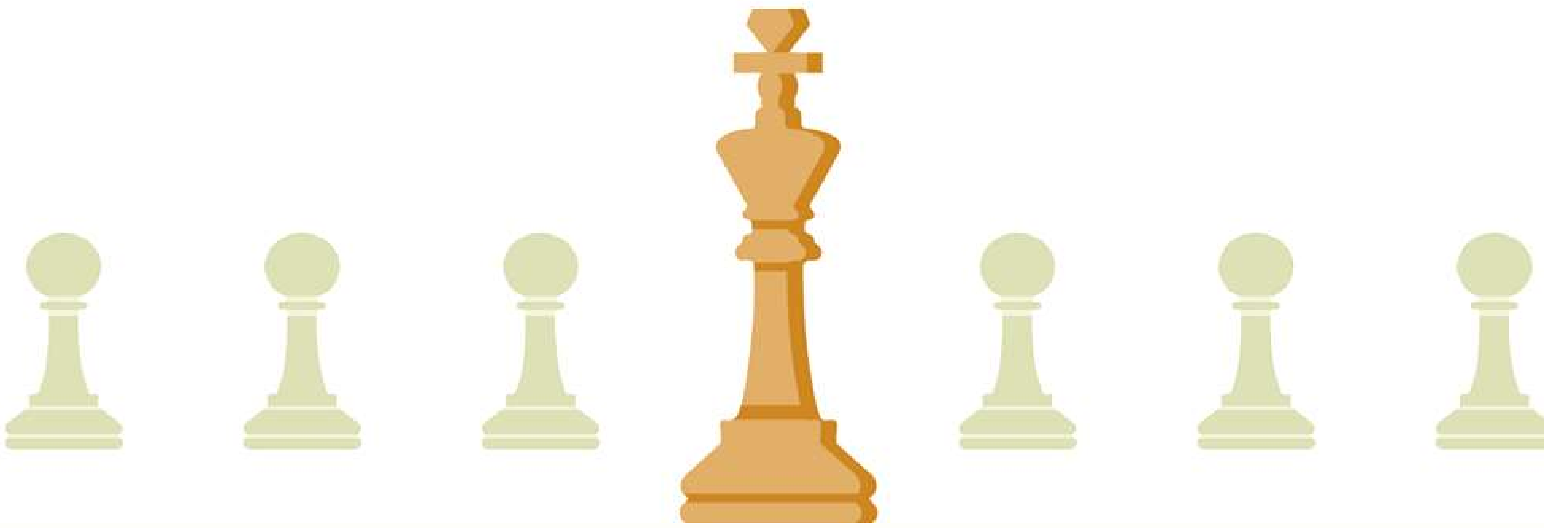
Most Common Ways to Sell a Practice



Options

- Sell to outside OD
- Internal succession plan
- External sale to 3rd party buyer (i.e. private equity firm)

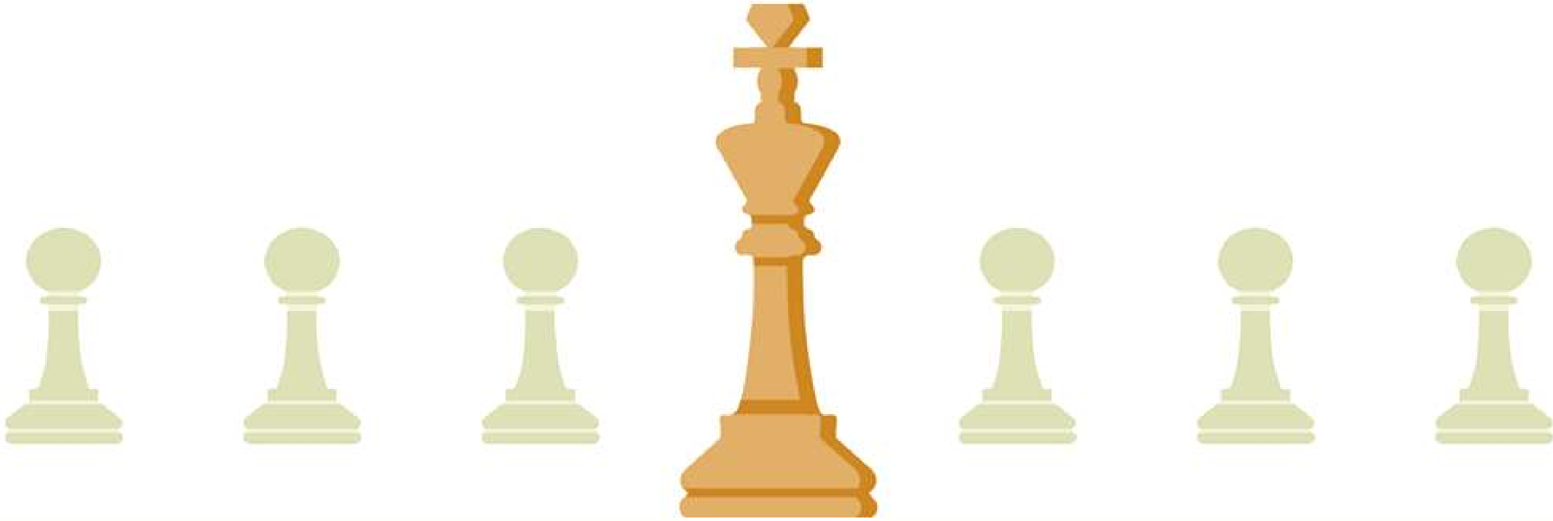
Details: Selling to Outside OD



Finding a Buyer

Executing a Buy/Sell or PCA (Practice Continuation Agreement)

Details: Selling to Internal OD



Owner Does Due Diligence on Current Value

Owner and Successor Negotiate Price and Date of Execution

Goodwill can be negotiated

Most valuable part of sale for current owner

For buyer: don’t buy your own equity back at a future point!

Funding of the Transaction Must Be Secured
Options Include:

Traditional financing (bank) – 100% financing an option

Seller financed

- Seller agrees to fixed payments for a period of time for given interest rate and duration
- Seller financed gives most flexibility but also most risk to seller
- Not ideal in most situations as the seller

Importance of Communicating the Big Picture with Your Buyer!

Buyers: Get focused on how much the loan will cost

Sellers: Ensure they understand their participation in the profits

- There should be a return above and beyond what they make producing in the practice
- They now get rewarded for working ON the practice

Asset Sale:
Sale is Tied to the Assets of the Practice

Total sale is split between allocation to goodwill and assets of practice

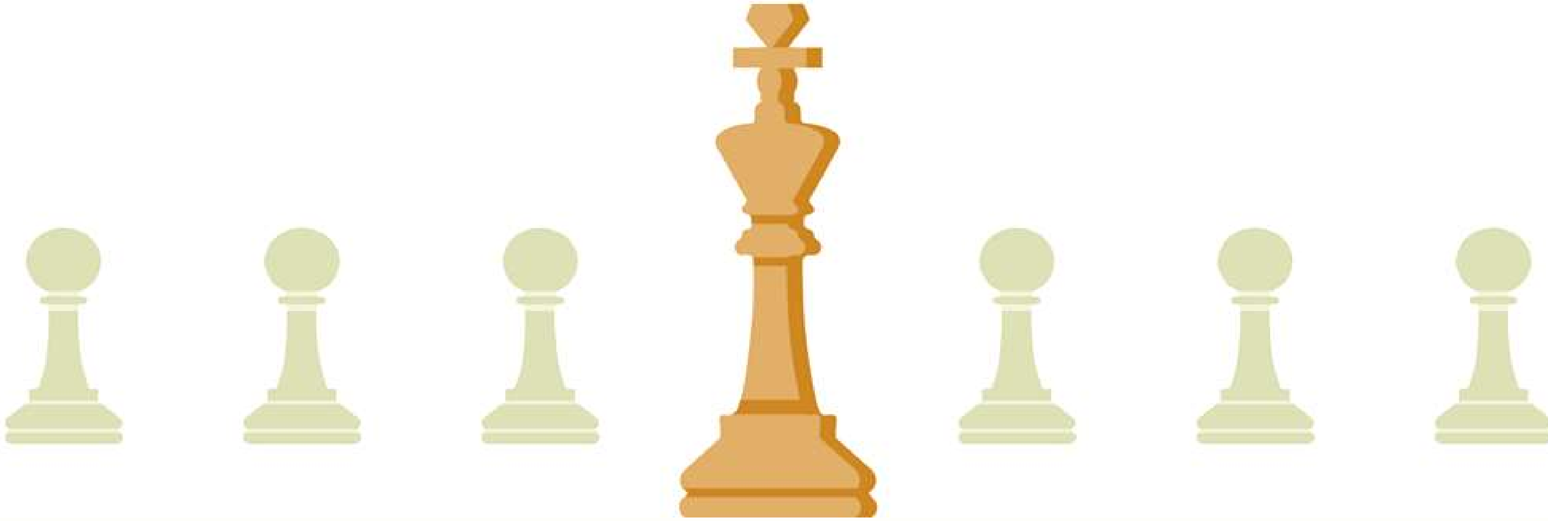
- Goodwill is personal/intangible assets—majority of the value
- Assets remain in business
  - Buyer: wants valuation weighted towards asset
  - Seller: wants valuation weighted towards goodwill

Stock Sale:
Buyer Purchases Selling Shareholder's Stock

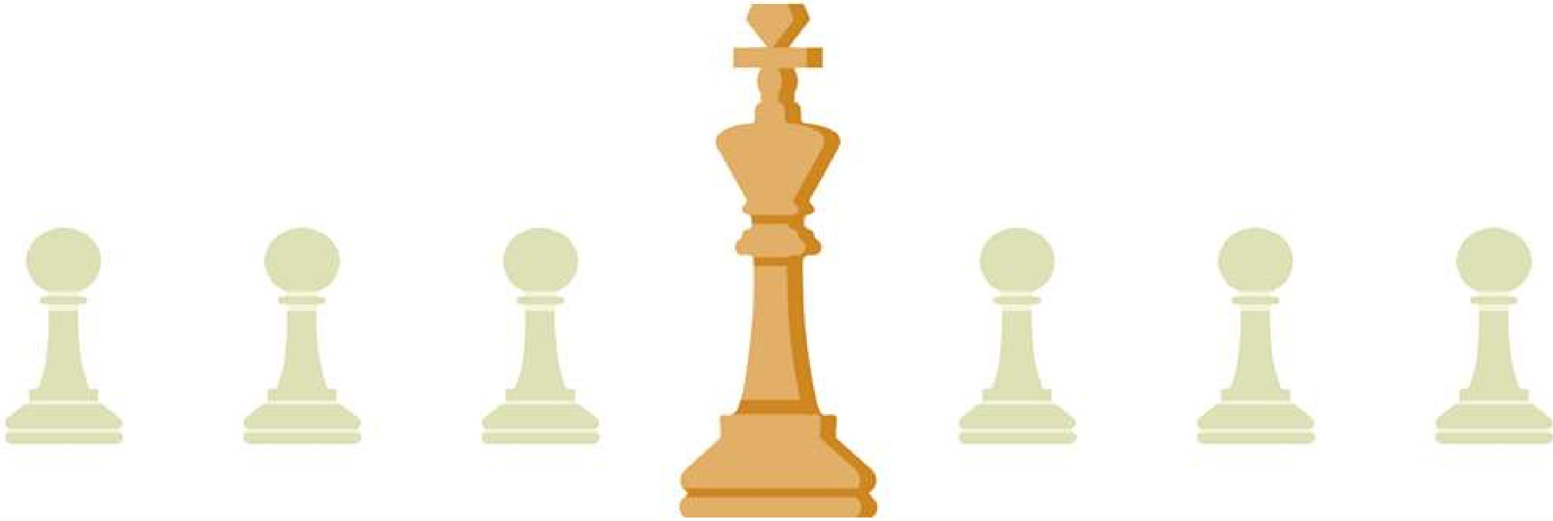
Buyer loses ability to depreciate

- Usually not favorable for OD practices

The Basics of the Sale: Assets vs Stock

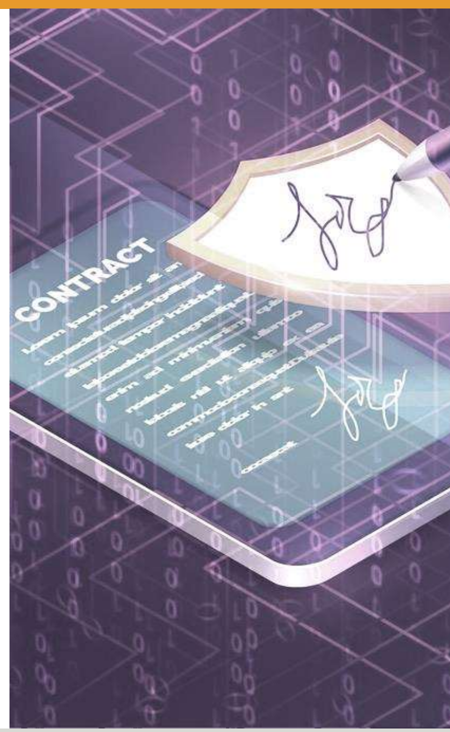


Details: Selling to 3rd Party Buyer (i.e. Private Equity)

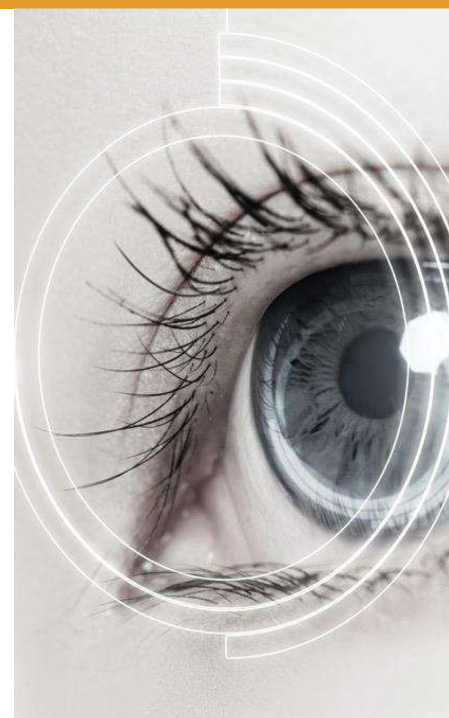


Typically has quicker turnaround
(can be 90 days or less)

Heavily Capitalized
(financing is secured)

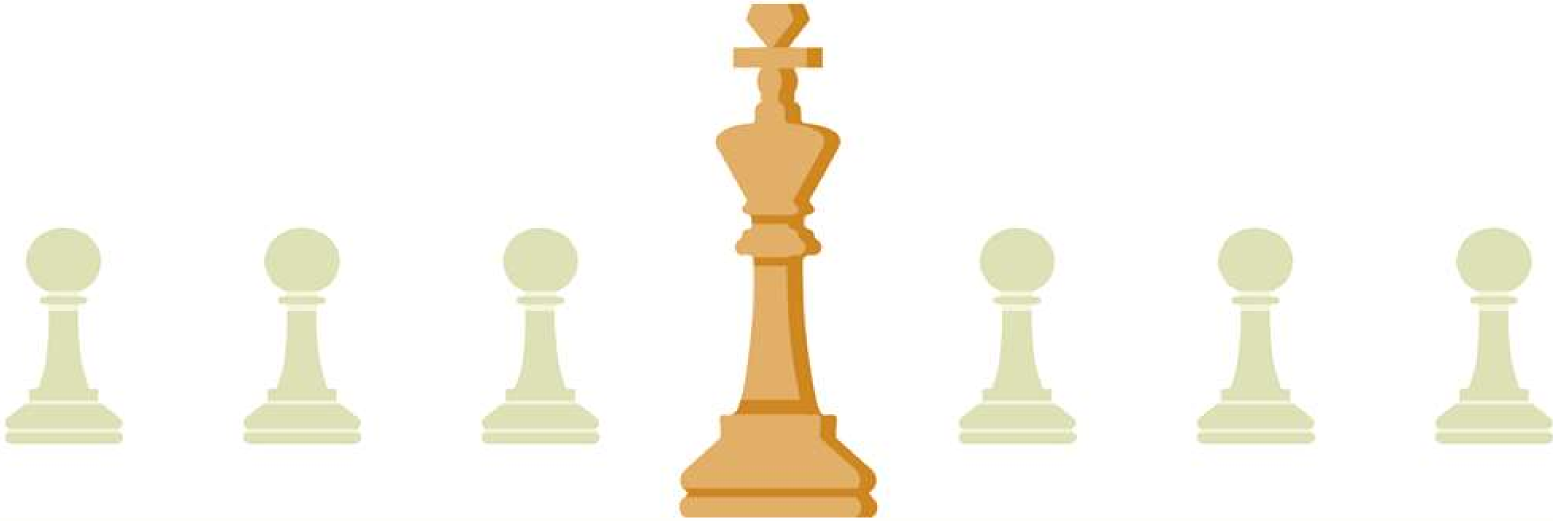


Sees Your Practice Through a Different Lens



Importance of Team Buy-in Especially with Key Providers in Practice

The Timeline: Financing and Appraisal



Ideally Conversations Begin >3 Years Out

Similarities and Differences to Buying/Selling a House

Have a Formal Appraisal Done on the Practice

Ensure Accuracy of Financial Statements

Agree on Transition on Patient Load After Purchase

Get it in Writing

Begin with the End in Mind: A Practice Owner's Lifecycle

It's important to understand what you want from your exit strategy.

Optometric Practice Example:

Family Optometric, P.C. is an optometry practice with one 55 year old optometrist and 6 other employees. The OD has been saving about $50,000 a year in her 401(k) plan, but it has only accumulated to about $500,000. Most of her money has been spent paying back school loans, buying the practice, upgrading the equipment, and putting her kids through college. In this case, about 94% of the money goes to the OD.

	AGE	COMP.	401(K)	CATCH UP	PROFIT SHARING	CASH BALANCE	TOTAL
Optometrist	55	280,000	19,500	6,500	14,375	200,000	239,375
2 Opticians	48	50,000	0	0	5,250	0	5,250
2 Techs	34	40,000	0	0	4,350	600	4,950
2 Office Staff	24	50,000	0	0	3,625	500	4,125
TOTAL =		$440,000	$19,000	$6,000	$27,600	$201,100	$ 253,700

Simplified QBI Example:

Small Town Optometry, Inc. is a small single owner optometry practice. As part of TCJA, an additional 20% tax deduction is allowed on Qualified Business Income (QBI) below $329,800. A Cash Balance Plan can be set up to contribute the amount required to get income to exactly $329,800 in order to provide the owners with the deductions on contributions plus a bonus $63,000 QBI deduction.

Income	401(k) PS	Cash Balance	QBI Deduction	Tax Savings*
$300,000	$0	$0	$60,000	$24,000
$400,000	$30,000	$55,000	$63,000	$59,200
$500,000	$30,000	$155,000	$63,000	$99,200

* Tax Savings assumes 40% state and federal tax brackets

Cash Balance Plan Combined with a 401(k) Profit Sharing Plan:

- Advantages
  - Highest maximum contribution
  - Largest discrepancy between owner contributions and employee contributions
  - Relatively easy to understand
- Disadvantages
  - Highest cost to administer since there are 2 plans
  - Contributions can vary based on demographic changes

Questions To Ask Yourself…

The government has very generous tax savings opportunities for companies who sponsor and contribute to qualified retirement plans. The above examples are ideal candidates for a plan, but many other practice structures can benefit as well. The following list contains questions to ask business owners to determine if their company is a good candidate for a Defined Benefit or Cash Balance Plan:

Questions To Ask Yourself…

1. Does the business provide enough cash flow to support additional contributions to a retirement plan?

2. Are the only employees of the company the owner, spouse, children, and/or parents of the owner?

3. Do any of the owners feel they are behind on retirement savings?

4. Is the ratio of employees to owners less than 10 to 1?

5. Is the owner at least 10 years older than the youngest employee?

6. Are profits going to be stable enough for the next 3 to 5 years to commit to funding a retirement plan?

7. Is someone at the company willing to spend up to 5 hours per year to deal with retirement plan related issues?

8. Are the employees or recruits asking for additional plan contributions?

9. Does the owner feel that a retirement plan would help to recruit and retain the best employees?

10. Is the owner desperately looking for tax deductions?

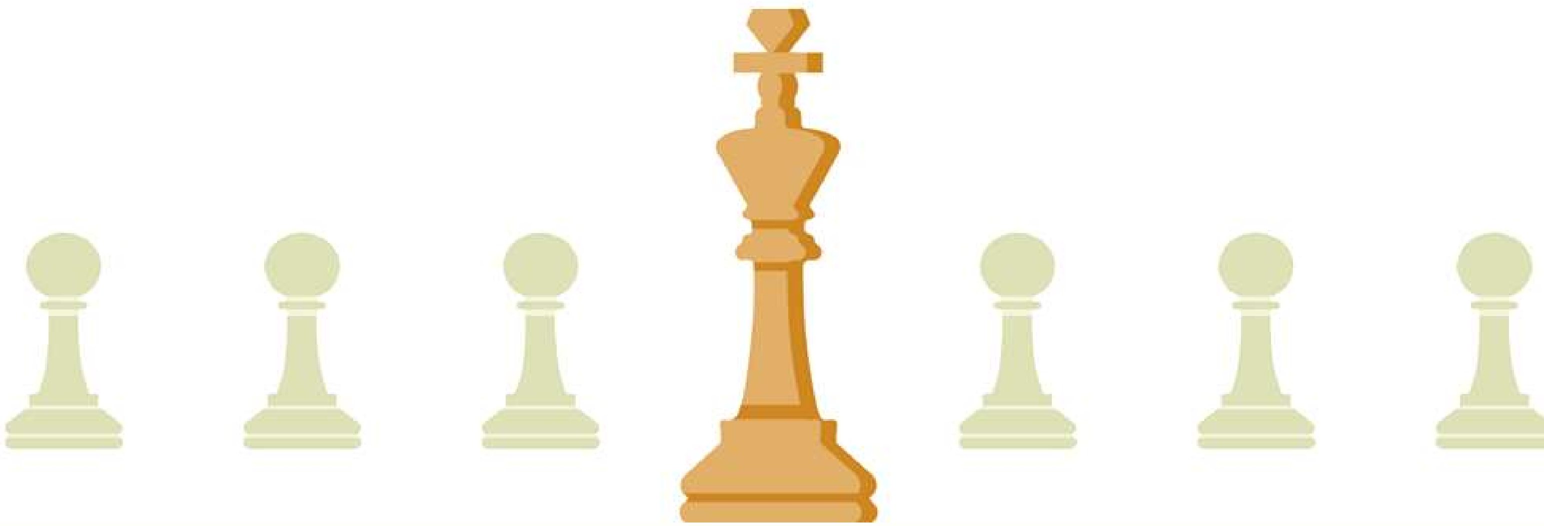
Cash Balance Plan Investments

1. Participants don’t direct investments, only trustees
    A. Therefore, no fee disclosure
    B. No participant meetings
2. Guaranteed Rate in the plan
    A. Almost always a fixed rate these days
    B. Importance of hitting it depends on how many owners and their cash flow
    C. Actual rate of return plans are legal but not often practical
3. Generally the most conservative part of a business owner’s portfolio
    A. Use BOY valuations to control contributions from year to year
    B. Don’t get more than 1 year ahead or behind

Cash Balance Plan Investments (continued)

1. Generally invested in readily tradable stocks, bonds, mutual funds, etc.
2. Insurance doesn't usually work as the employee cost is much higher
3. No recordkeeper required since all assets are pooled and trustee directed, similar to a solo(k) from that standpoint
4. Participant statements generally prepared by the TPA only once per year

Conclusion



You Will Leave Your Practice at Some Point

Will it be on your terms
or on someone else’s terms?