

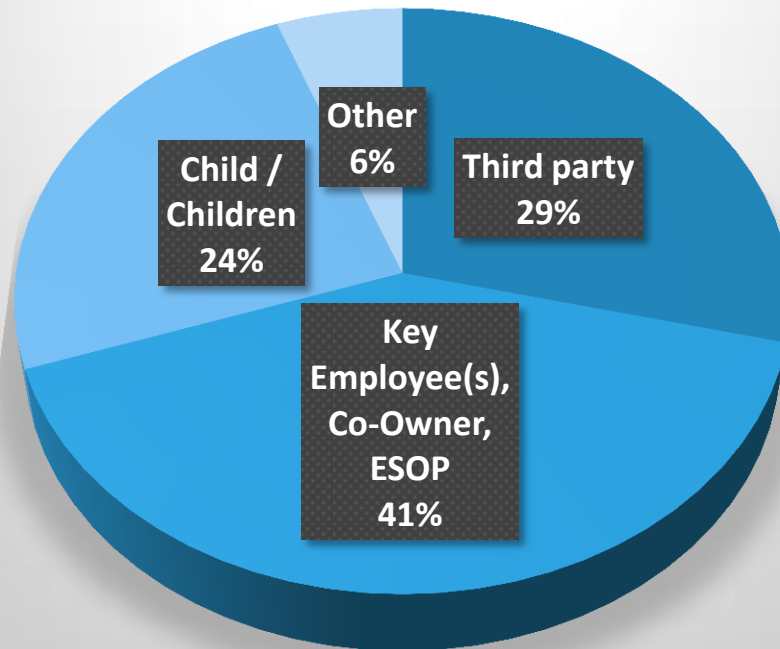
# 2015 Hawai'i Health Workforce and IT Summit

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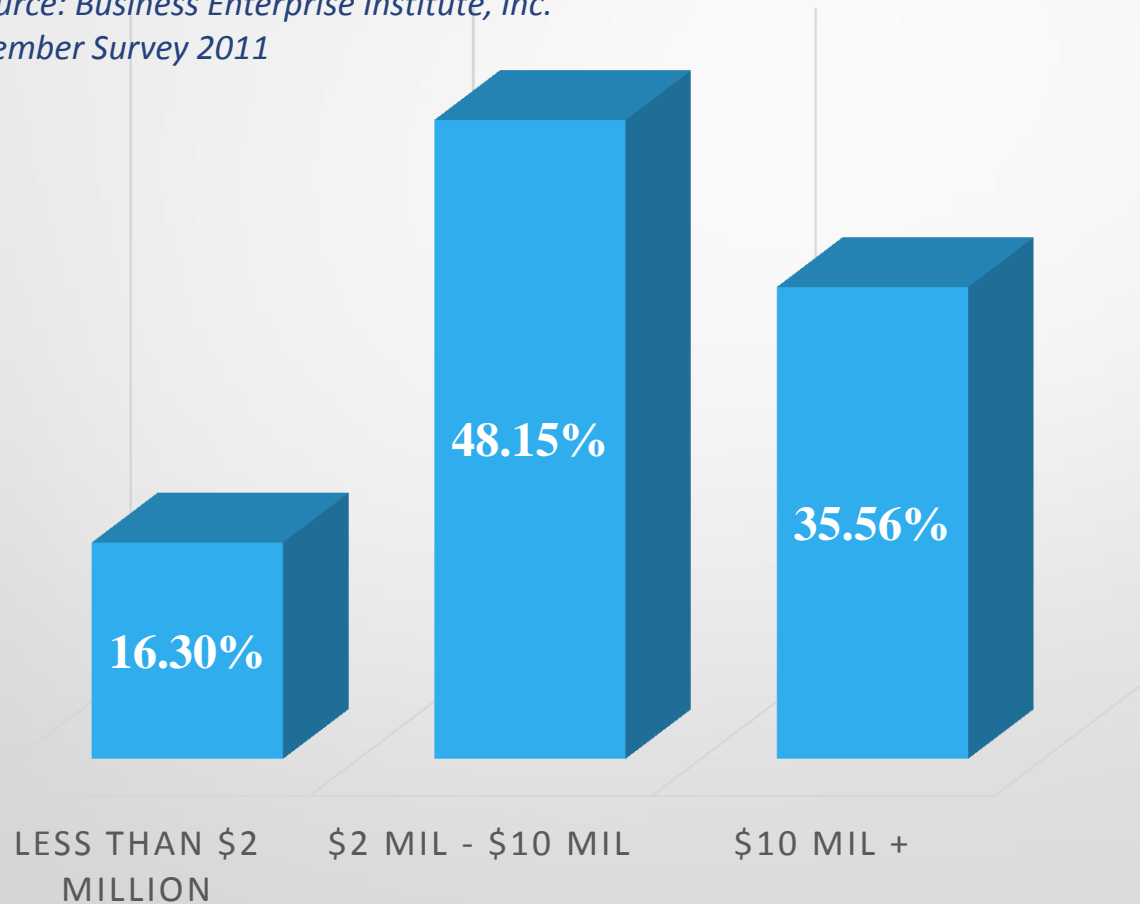
# Business Owner Market: Exit Path Choices



Source: Business Enterprise Institute, Inc. Member Survey 2011

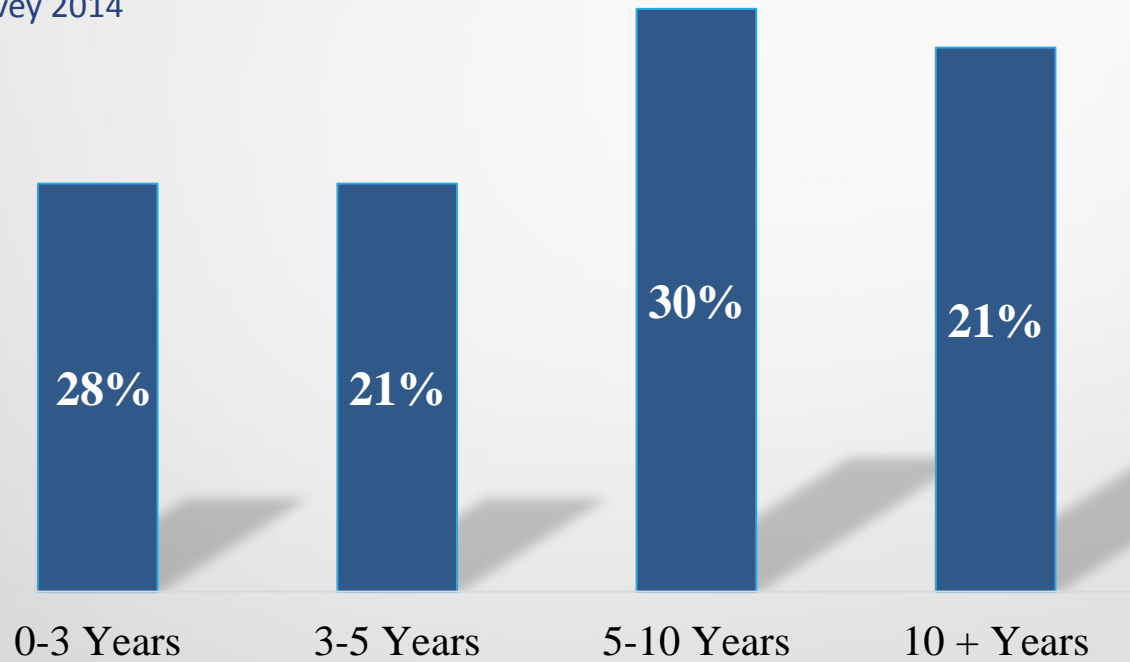
# Business Owner: Business Value

Source: Business Enterprise Institute, Inc.  
Member Survey 2011



# When Do Business Owners Want to Exit?

Source: BEI's North American Business Owner Survey 2014





# What is an Exit Plan?

- Holistic approach to a Business Exit Strategy
- Receive maximum value for life's work
- Limit the physician's tax burden
- Keep control of the process



# Ingredients for a Successful Exit

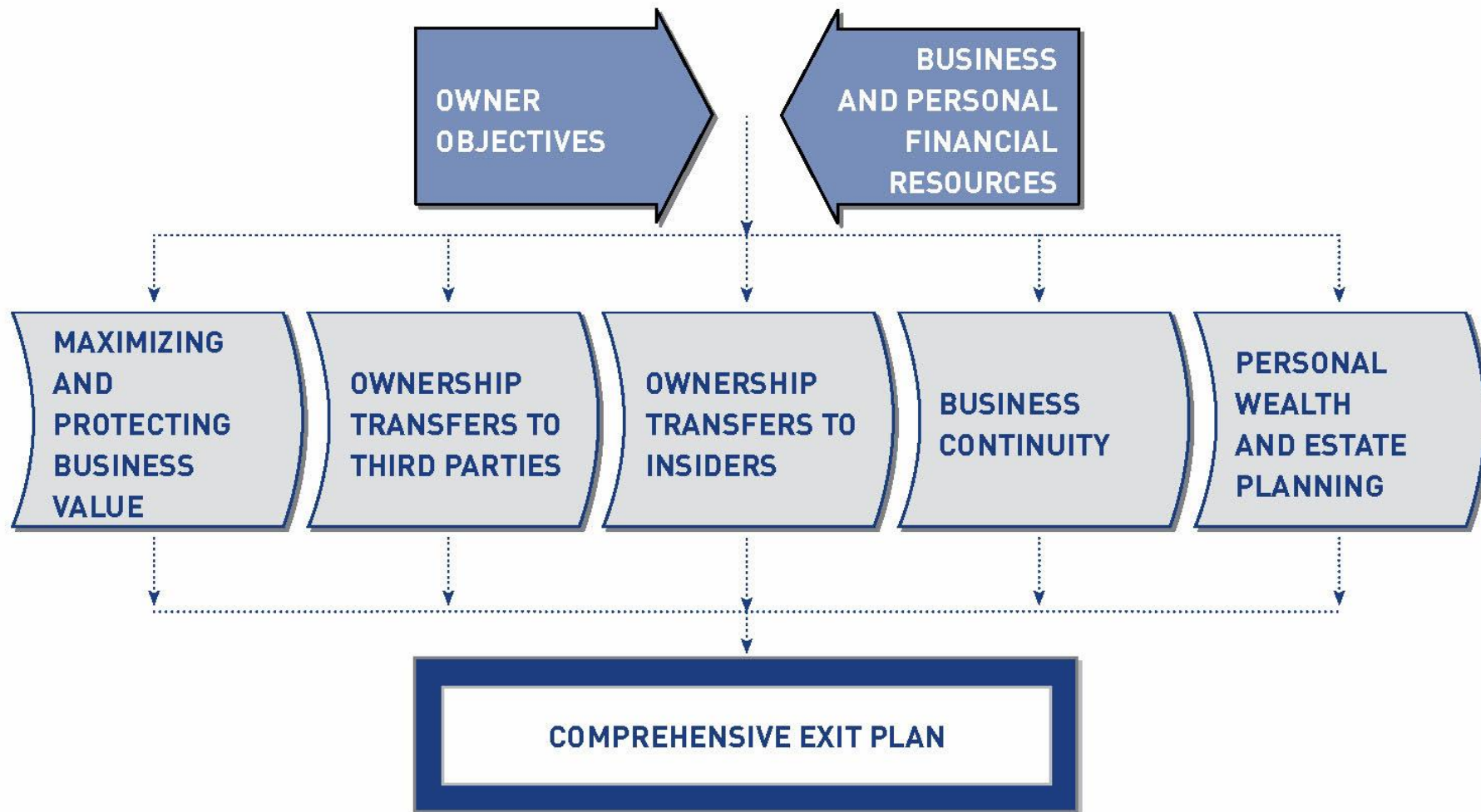
- Exit Plan based on the physician's objectives
- Experienced team of advisors to design and implement the plan
- Cash flow and a quantified business value
- Strong management team in place
- Time



# COMPONENTS OF A COMPREHENSIVE EXIT PLAN

*within*

The Seven Step Exit Planning Process™



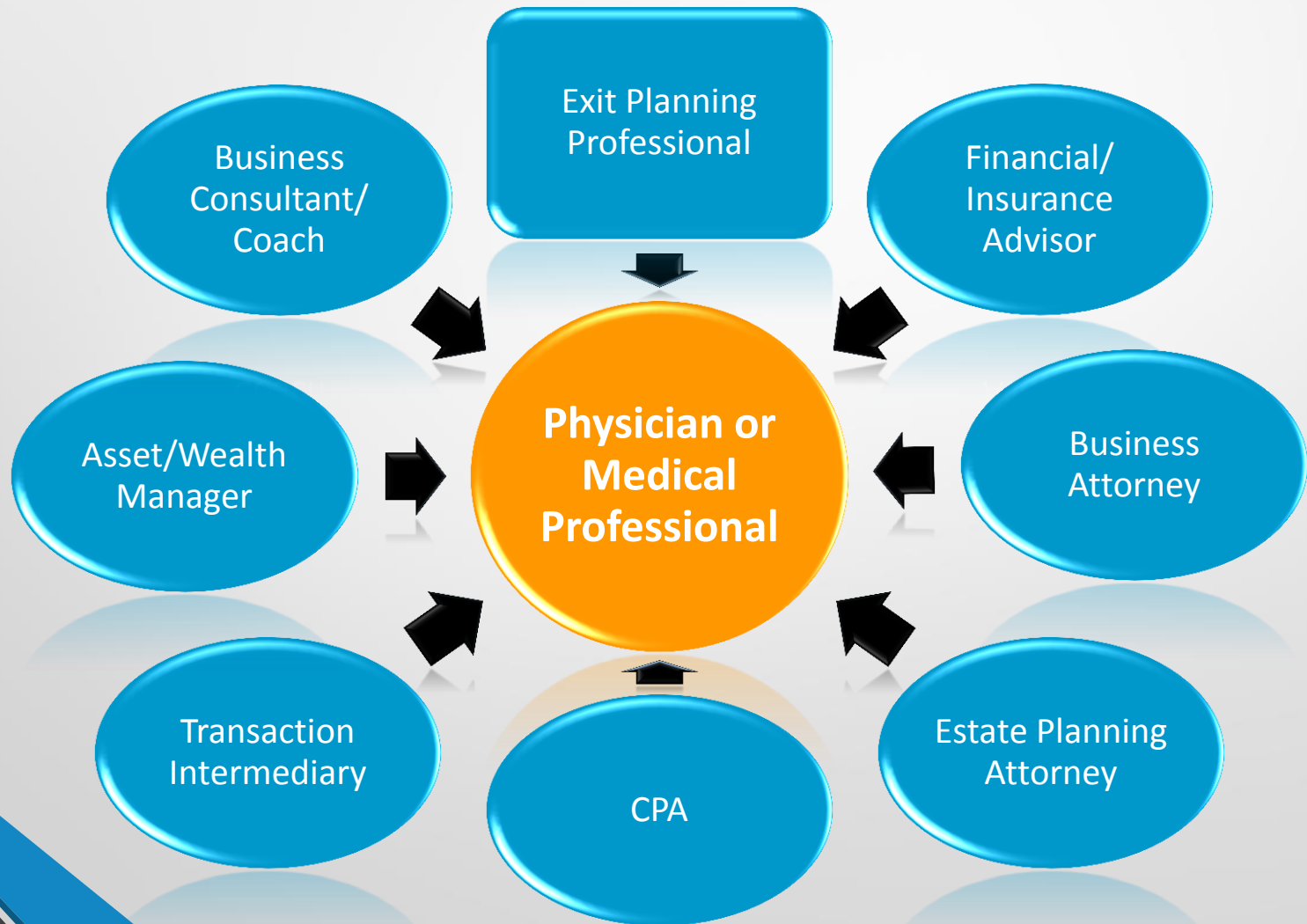


## Team of Professional Advisors

- Financial Planner
- Insurance Advisor
- Investment Advisor
- Business Attorney
- Estate Planning Attorney
- CPA
- Valuation Specialist
- Business Broker
- Investment Banker
- Business or Management Consultant
- Banker



# Advisor Team Relationships





# The Seven Step Exit Planning Process™

Step 1 – Identify Exit Objectives

Step 2 – Quantify Business and Personal Financial Resources

Step 3 – Maximize and Protect Business Value

Step 4 – Ownership Transfer to Third Parties

Step 5 – Ownership Transfer to Insiders

Step 6 – Business Continuity

Step 7 – Personal Wealth and Estate Planning

# Why Do I Need a Business Valuation?

Step 2 – Quantify Business and Personal Financial Resources

Your practice could be a valuable asset!



+



+



+



# Value of a Business Valuation

An independent business valuation can...

- Help you know what your practice is worth, aid in planning
- Provide prospective buyers with an independent opinion of value
- Help buyer/seller comply with Stark Laws and Anti-Kickback Statutes

# Other Benefits of a Business Valuation

Benchmark your practice to similar types of practices

Determine reasonable compensation

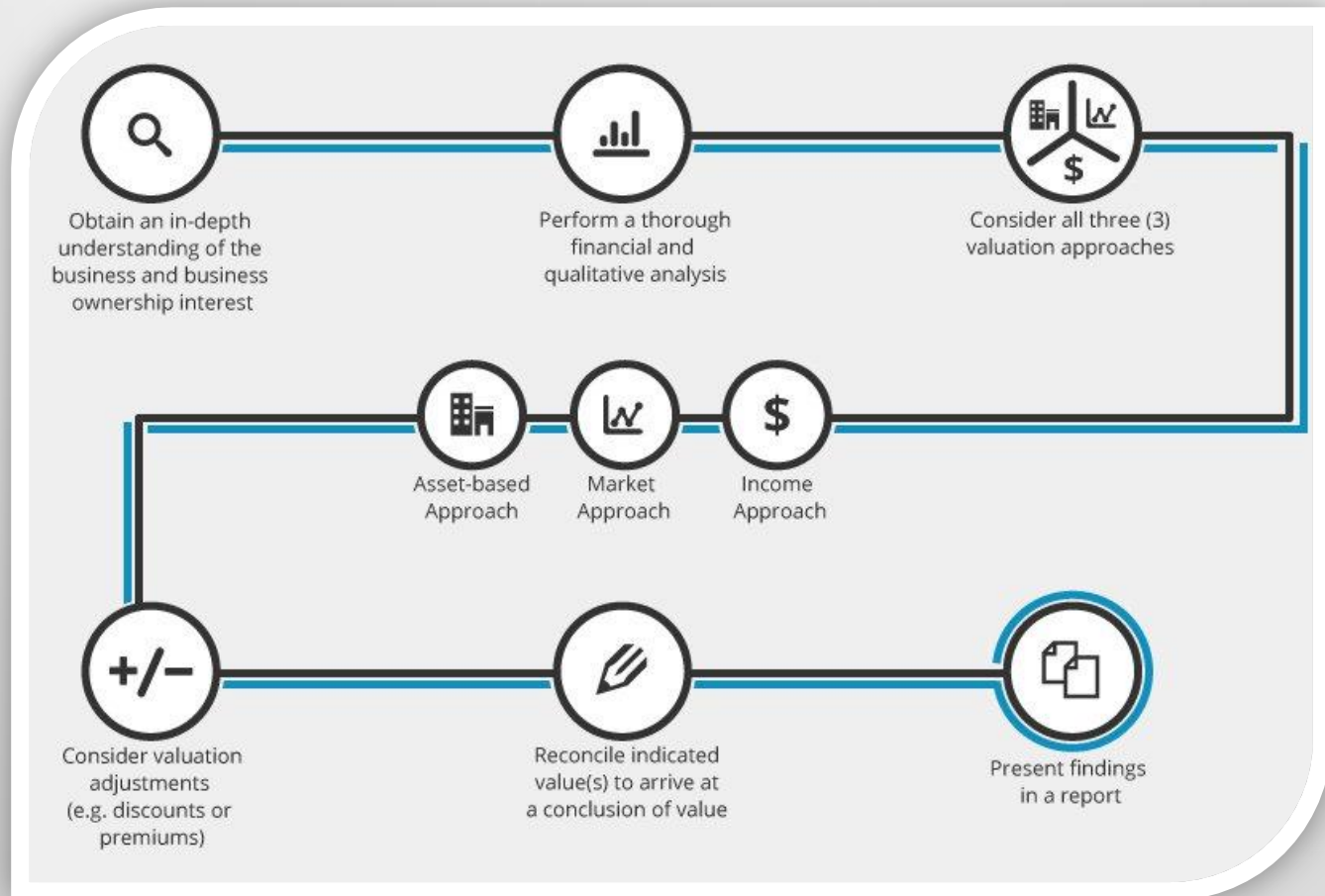
Quantify goodwill

Maximize the value of your practice

Satisfy IRS appraisal requirements

Continuity planning

# Business Valuation Process



# Business Valuation “Simplified”

Value = Earnings / Risk

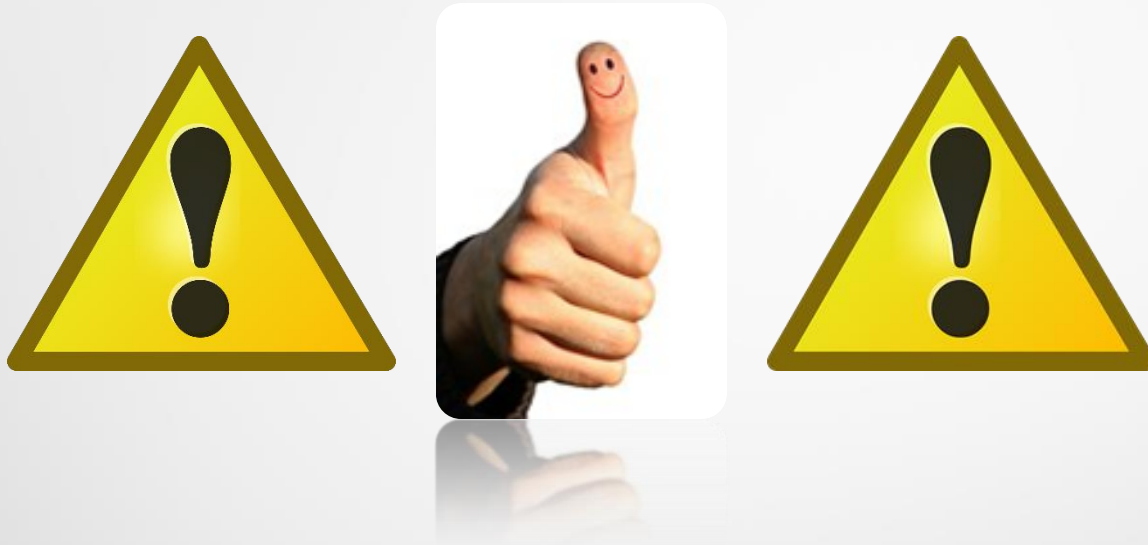
$$\$200,000 / 20\% = \$1,000,000$$

Or

Value = Earnings X Multiple

$$\$200,000 \times 5 = \$1,000,000$$

# Beware of Rules of Thumb!



- A rule of thumb is a principle with broad application that is not intended to be strictly accurate for every situation (Source: Wikipedia)



# A Tale of Two Physician Practices



- Both practices had “earnings” of \$200K in 2014



- Physician practices sell for 5X earnings



- So both practices are worth \$1 Million, right?

# A Tale of Two Physician Practices

## Additional Facts...

- Practice 1 has one physician and one office support staff employee
- Physician 1 takes a \$100K salary
  
- Practice 2 has one physician, four nurse practitioners, and 2 office support staff employees
- Physician 2 takes a \$700K salary
  
- Both practices are C corporations
- Reasonable salary for both physicians is \$200K

# A Tale of Two Physician Practices

Effect of reasonable salary adjustment on value





	Practice 1	Practice 2
Historical earnings	\$200K	\$200K
Salary adjustment	<u>-100K</u>	<u>+500K</u>
Adjusted earnings	\$100K	\$700K
Times: Value Multiple	<u>x 5</u>	<u>x 5</u>
Value of Practice	<u>\$500K</u>	<u>\$3.5 Million</u>

# Maximizing the Value of Your Practice

## Primary value drivers

- Earnings
- Risk

## Ways to increase value

-  Earnings
-  Risk
-  Earnings AND  Risk

# Maximizing the Value of Your Practice

## “Controllable” Physician Practice Risk Factors

- Reliance on key providers (you?)
- Key referral relationships
- Payer mix
- Procedures / services mix
- Depth of management

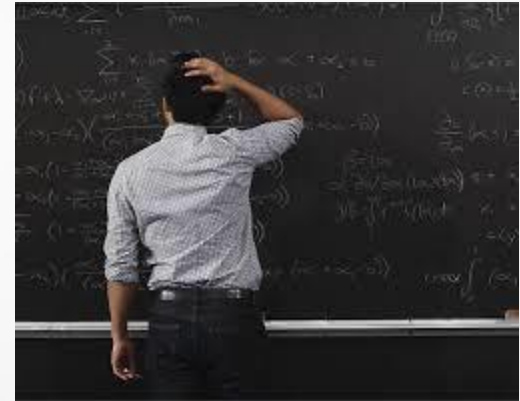
# Reasons for Exiting

- Resignation
- Termination
- Death
- Disability
- Death
- Divorce
- Bankruptcy
- Disqualification
- Default
- Disagreement



# Types of Buy-Sell Arrangements

- Redemption
- Cross-Purchase
- Hybrid



# Valuation Mechanisms

- Agreed Value
- Formula Agreements
- Appraisal
- Insurance buy-out





# Financing a Sale

- Cash
- Seller-financed buy-out
- Company-financed buy-out
- Insurance buy-out



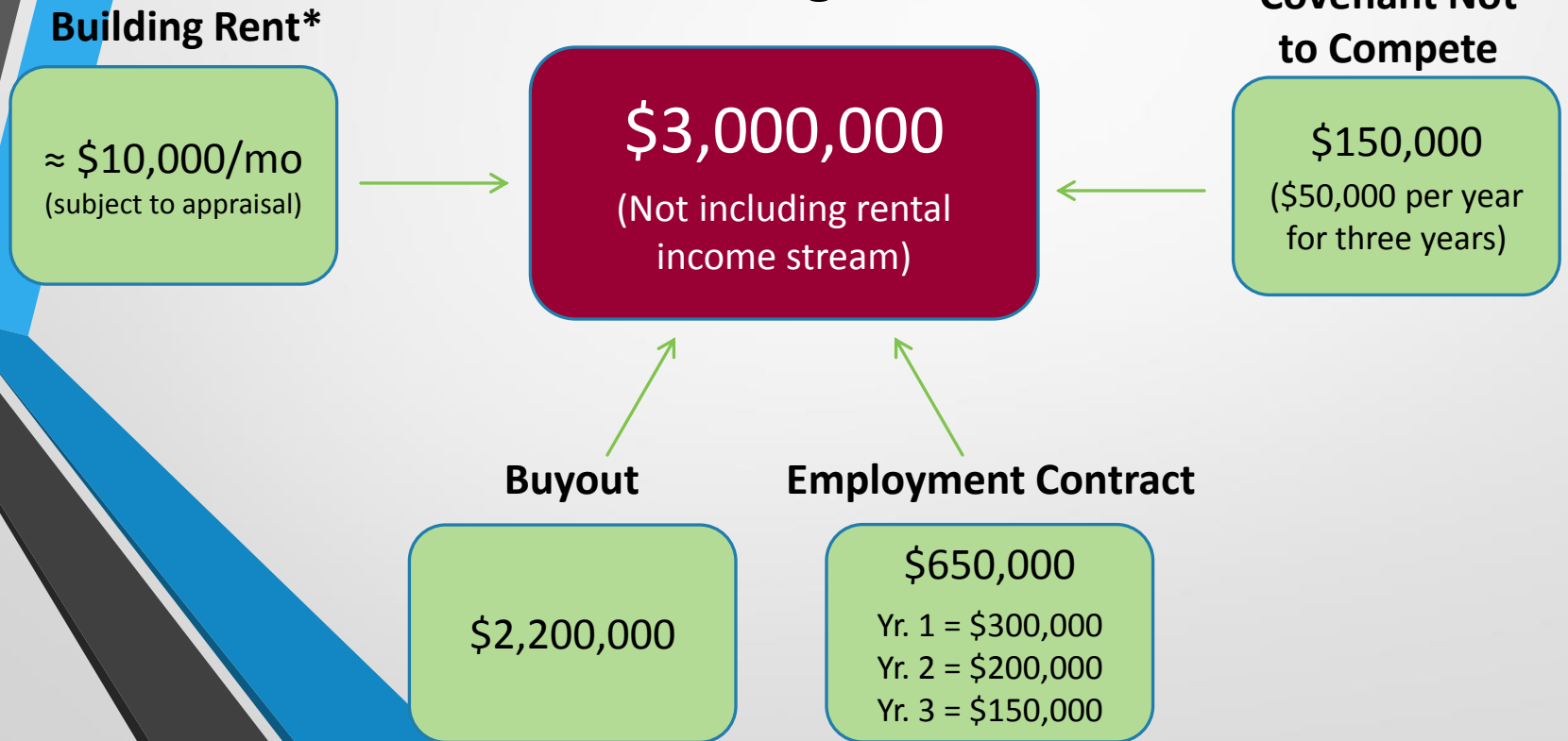
# Estate Planning Considerations

- Most wealth tied up in the business
- Different types of practices will implicate different considerations
  - Owner-dependent
  - Multigenerational
  - Marketable
- Gift & Estate Taxes



# John Doe Physician, Inc. Exit Strategy Payout Option #1

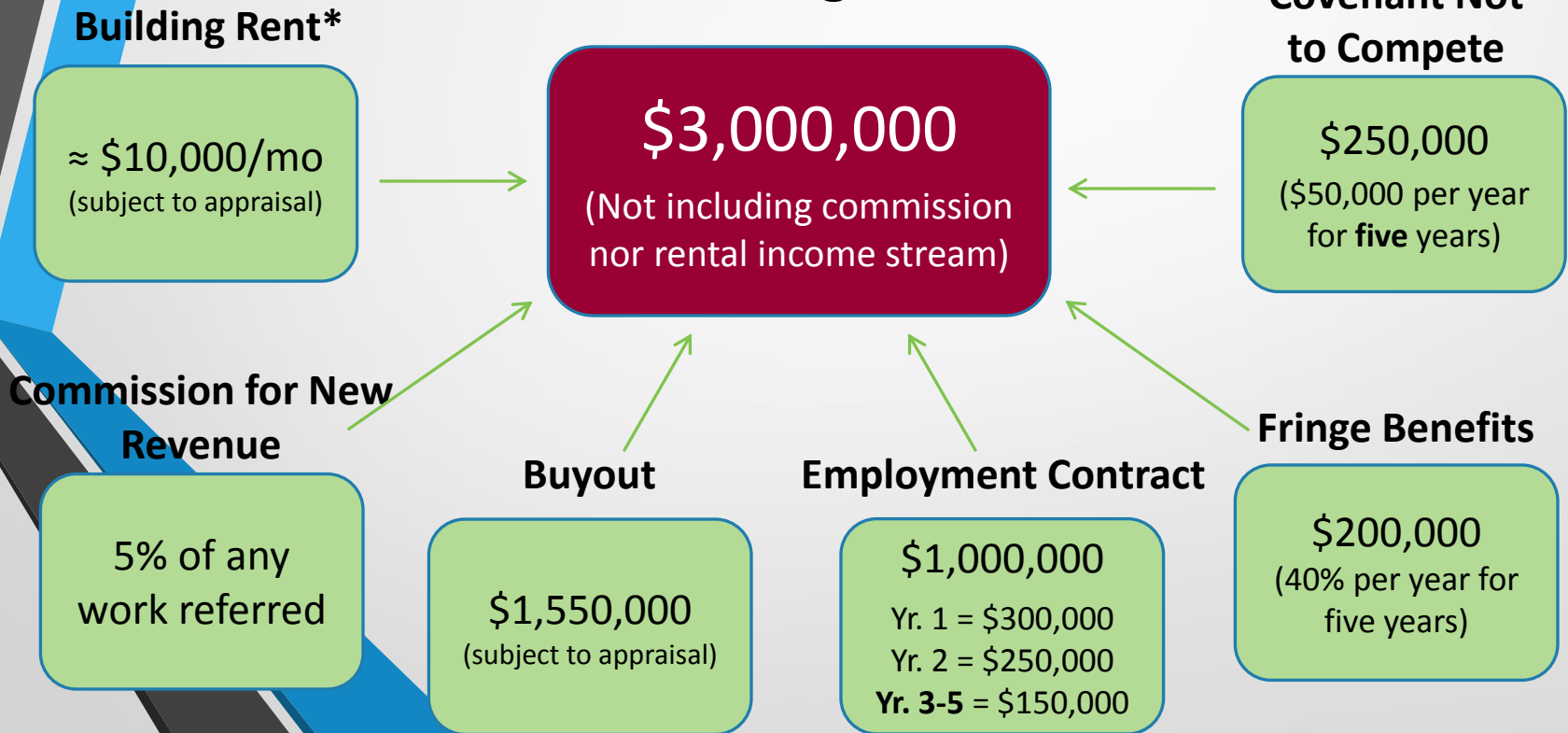
## Total Exit Package for Owner



\*Based on RE market conditions

# John Doe Physician, Inc. Exit Strategy Payout Option #2

## Total Exit Package for Owner



\*Based on RE market conditions

# John Doe Physician, Inc. After-tax Cash Flow – Stock Purchase

<b>Buyout</b>	\$3,000,000
<b>Salary</b>	-
<b>Noncompete</b>	-

	<b>Corporation</b>	<b>Seller</b>	<b>Buyer</b>
Buyout at \$3.0M	-	(\$1,065,000)	-
Employment K	-	-	-
Noncompete	-	-	-
Tax benefit / (cost)	-	(1,065,000)	-
Total cash inflow / (outflow)	-	3,000,000	(\$3,000,000)
After-tax cash flow	-	\$1,935,000	(\$3,000,000)

# John Doe Physician, Inc.

## After-tax Cash Flow – Exit Strategy #1

<b>Buyout</b>	\$2,200,000
<b>Salary</b>	650,000
<b>Noncompete</b>	150,000

	<b>Corporation</b>	<b>Seller</b>	<b>Buyer</b>
Buyout at \$2.2M	-	(\$ 781,000)	-
Employment K of \$650k	\$212,875	(316,225)	-
Noncompete of \$150k	60,600	(61,500)	-
Tax benefit / (cost)	273,475	(1,158,725)	-
Total cash inflow / (outflow)	(800,000)	3,000,000	(\$2,200,000)
After-tax cash flow	(\$526,525)	\$1,841,275	(\$2,200,000)

# John Doe Physician, Inc.

## After-tax Cash Flow – Exit Strategy #2

<b>Buyout</b>	\$1,550,000
<b>Salary</b>	1,000,000
<b>Noncompete</b>	250,000
<b>Fringe Benefit</b>	200,000

	<b>Corporation</b>	<b>Seller</b>	<b>Buyer</b>
Buyout at \$1.55M	-	(\$ 550,250)	-
Employment K of \$1.0M	\$ 327,500	(486,500)	-
Noncompete of \$250k	101,000	(102,500)	-
Fringe benefits of \$200k	80,800	(82,000)	-
Tax benefit / (cost)	509,300	(1,221,250)	-
<b>Total cash inflow / (outflow)</b>	<b>(1,450,000)</b>	<b>3,000,000</b>	<b>(\$1,550,000)</b>
<b>After-tax cash flow</b>	<b>(\$ 940,700)</b>	<b>\$1,778,750</b>	<b>(\$1,550,000)</b> <sup>31</sup>

# John Doe Physician, Inc.

## After-tax Cash Flow – Summary

<b>Stock purchase vs Option #1</b>	<b>Corporation &amp; Buyer</b>	<b>Seller</b>
Stock purchase	(\$3,000,000)	\$1,935,000
Option #1	(2,726,525)	1,841,275
Net benefit / (cost)	\$ 273,475	(\$ 93,725)

<b>Stock purchase vs Option #2</b>	<b>Corporation &amp; Buyer</b>	<b>Seller</b>
Stock purchase	(\$3,000,000)	\$1,935,000
Option #2	(2,490,700)	1,778,750
Net benefit / (cost)	\$ 509,300	(\$ 156,250)



# Getting Started and Maximizing Value

- Hiring a Team
  - All of the necessary skill sets are represented
  - Professionals are familiar with each other and overlap of services are minimized
  - Pricing is generally better
- Formalize the Process
  - Engages professionals who understand the process
  - Keeps everyone on task and committed to the solution
  - Minimizes physician's time away from their practice
- Sharing the News
  - Communicates your commitment to the transition
  - Provides an independent, third-party source of information to stakeholders
  - Offers one measure of value which may be used in other financial planning for the owner

# Questions?

