

Associates in Equity Positions



Leslie Mamalis, MBA, MSIT, CVA
Summit Veterinary Advisors

Leslie

AAHA – 1st set of specialty standards (1999-2000)

MBA – thru lens of management consultant

Credentialed Valuation Analyst – thru lens of appraiser

Since 1998, Summit has worked with more specialists than other
veterinary financial consulting firms

Consulted with veterinarians for over 17 years



Agenda

01. Market Trends

02. Associate Buy-Ins – Seller &

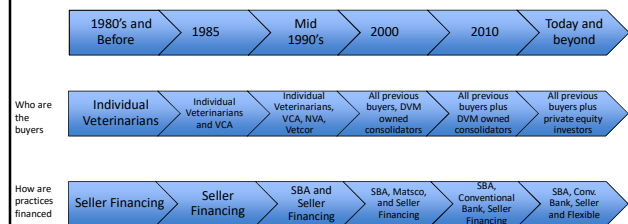
Buyer Perspectives

03. Creative Financing

04. Q & A



Timeline of Veterinary Practice Financing and Value



A NONPROFIT ASSOCIATION OF VETERINARY BUSINESS SPECIALISTS
Marketing | HR | Valuation | Finance | Legal | Practice Management | and more

VetPartners®
For the good of the profession.
VetPartners.org

	2000	2010	Now – Phased Buy-Out
Asking Price	\$1.5 MM	\$2.0 MM	VC Offer - \$3.0 MM
FMV	\$1.5 MM	\$1.75 MM	\$2.0 MM
Sales Price	\$1.5 MM	\$1.875 MM	\$2.2 MM, 20%/yr for 3 yrs. 40% yr 7 @ \$2.5 MM
Financing	Bank financed, 10 yrs., 10.59%, Seller holds 15%	100% Bank financed, 10 to 15 yrs., 4.5 - 5%	100% Bank – or seller financed for 5 or 6 yrs.
\$ to Seller	\$1.275 MM at sale. \$225K + \$260K interest over life of loan	\$1.875 MM	\$2.847 MM to \$3.205 MM total price + earnings

Tax Impact: This is a variable item that will depend upon personal financial situations.

A NONPROFIT ASSOCIATION OF VETERINARY BUSINESS SPECIALISTS
Marketing | HR | Valuation | Finance | Legal | Practice Management | and more

VetPartners
For the good of the profession
VetPartners.org

Through the Years..... The Price of Veterinary Practices was Driven by:

- **Terms of Debt**
 - Seller Financing-Term of financing could range from 7 to 20+ years
 - Price is set and term adjusted to allow cash flow to support price
 - SBA/Bank-Term is generally 7 to 10 years
 - Term is set and price is adjusted to allow cash flow to support price
- **100% Financing as Industry Standard**
 - Based upon *cash flow*; this requirement provides a cap on value
 - Valuation models incorporated into determining value
- **Corporate Buyers and Private Equity Buyers**
 - Purchase price based upon *return*; prices not directly tied to cash flow
 - Expense reduction opportunity in consolidating operations

A NONPROFIT ASSOCIATION OF VETERINARY BUSINESS SPECIALISTS
Marketing | HR | Valuation | Finance | Legal | Practice Management | and more

VetPartners
For the good of the profession
VetPartners.org

Conclusions and Opportunities for Veterinarians

- Supply of practices < current demand, creating higher prices
- Certain groups of buyers are purchasing practices without debt, resulting in practice values that can be higher than when 100% financing is required
- The terms and structures of veterinary practice purchases have evolved over time and will continue to evolve
- Partnership structure can provide opportunity for associate clinicians to become owners at a higher price under a structure that can support the debt

A NONPROFIT ASSOCIATION OF VETERINARY BUSINESS SPECIALISTS
Marketing | HR | Valuation | Finance | Legal | Practice Management | and more

VetPartners
For the good of the profession
VetPartners.org

Bringing an Associate into Partnership

Seller Perspective



Partnership? Seller Perspective



Why take on a partner?

Succession planning
"Lock-in" associate for long-term
Shared ownership responsibilities



Partnership? Seller Perspective



1. Succession Planning
2. Can be difficult to find private buyers
3. Helps ensure transfer of goodwill



Partnership? Seller Perspective



4. Valued associate has existing relationship with:
 - Practice
 - Staff
 - rDVMs
 - Clients



Partnership? Seller Perspective



Succession Planning

It may be difficult to find outside buyers for your practice

Transitioning an associate to ownership
be your only reasonable option

Transition



Partnership? Seller Perspective



"Lock-In" Associate

You may have the perfect person to buy your hospital some day...but you are not yet ready to retire

Sell a small portion now to increase the odds that the associate will be around to buy the rest when you are ready to exit



Partnership? Seller Perspective



Shared Responsibilities

Management –
Operations, HR, Inventory, Finance
Decision-Making



Partnership? Seller Perspective



Stop Dangling the Carrot!

A true ownership-minded associate will not stay indefinitely on the "promise" of future ownership!



Becoming a Partner: Buyer Perspective



Partnership? Buyer Perspective



Practice ownership

Numerous benefits

Increased responsibility / risk



Partnership? Buyer Perspective



Benefits of Ownership

- Increased financial return
- Increased impact on the operations & future path of the practice
- Potential for increased flexibility in work schedule, etc.



Partnership? Buyer Perspective



Financial Return

- Must service debt on purchase
- Appropriate purchase price should allow debt service from profit distribution



Partnership? Buyer Perspective



Appropriate purchase price should allow debt service from profit distribution

Ownership is a very attainable financial goal, even with a high student loan burden

In fact, the profit you receive as practice owner may allow you to repay those loans faster!



Partnership? Buyer Perspective



Responsibility / Risk

Management / Leadership Responsibility
Financial Responsibility



Partnership? Buyer Perspective



Responsibility / Risk

Need to learn wide variety of information re:

- Leadership
- Human Resources
- Customer Service / Marketing
- Financial Management
- Legal
- Regulatory
- Etc., etc.



Partnership? Buyer Perspective



Responsibility / Risk

You don't have to know "everything" but you need to have enough knowledge to "know what you don't know" and how to find the help you need!



Partnership? Buyer Perspective



Responsibility / Risk

Your share of the business profits SHOULD support your ownership debt payments
But what if they don't?
You are liable for those payments!



How Much to Sell?

Or Buy?



How Much to Sell? Or Buy?



.....

This is a difficult decision where the interests of the buyer and seller can differ



How Much to Sell?



.....

From a strictly financial perspective, you are essentially "giving away" a share of your practice!

What????



How Much to Sell?



.....

With an appropriately valued practice, the profits should pay the debt payments

If you sell 40% of your practice, then your partner has the right to 40% of the profits

They use this profit to service the debt on the loan you have given them for the purchase



How Much to Sell?



Essentially, you will receive the same amount of money, but you will now only have 60% of the equity in the business



How Much to Sell?



The goal of selling this first piece is not to make a killing.

But there is no reason to lose more than is necessary!

Sell the smallest piece possible to accomplish your goals

If you sell 10%, you are securing a buyer for the other 90%!



How Much to Buy?



The profits of the business SHOULD pay your debt service

Debt payments for purchase SHOULD NOT have to come out of your normal clinical compensation

Therefore, you SHOULD be able to afford as big a piece of the practice as you want



How Much to Buy?



Should \neq Guarantee



How Much to Buy?



What if...
Profits decline?

Distributions decrease due to other needs?

You are still "on the hook" for your debt payments, whether or not you get profit distribution!



How Much to Buy?



The larger the percentage of ownership, the larger the debt payments

Larger payments = more risk, if profits decline!

Strongly consider how much "wiggle room" you have in your personal financial condition

Could you support debt payments out of your "regular salary" during times of decreased profitability?



How Much to Buy?



Buying a larger percentage means you are assuming a higher degree of risk.

Make sure that you fully consider this risk before negotiating for a larger piece of the ownership pie.



Creative Financing Options



	2000	2010	Now – Phased Buy-Out
Asking Price	\$1.5 MM	\$2.0 MM	VC Offer - \$3.0 MM
FMV	\$1.5 MM	\$1.75 MM	\$2.0 MM
Sales Price	\$1.5 MM	\$1.875 MM	\$2.2 MM, 20%/yr for 3 yrs. 40% yr 7 @ \$2.5 MM
Financing	Bank financed, 10 yrs., 10.59%, Seller holds 15%	100% Bank financed, 10 to 15 yrs., 5.18%	100% Bank – or seller financed for 5 or 6 yrs.
\$ to Seller	\$1.275 MM at sale. \$225K + \$260K interest over life of loan	\$1.875 MM	\$2.847 MM to \$3.205 MM total price + earnings

Tax Impact: This is a variable item that will depend upon personal financial situations.

A NONPROFIT ASSOCIATION OF VETERINARY BUSINESS SPECIALISTS
Marketing | HR | Valuation | Finance | Legal | Practice Management | and more

VetPartners
For the good of the profession
VetPartners.org

Getting to \$3,000,000



Initial FMV = \$2.0 million
\$2.2 million sales price
Sell 20% per year for 3 years
Remaining 40% at Year 6
Updated valuation of \$2.5 million



Getting to \$3,000,000



Assumptions:

- Gross income = \$2.2 million
- 15% profitability
- Year 1 Earnings = \$330K
- Earnings grow 3% per year
- 50% of earnings are distributed



Staged Buy-In, Bank Financed



	Principal	Earnings	Total
Year 1	\$440,000	\$132,000	\$572,000
Year 2	440,000	101,970	\$541,970
Year 3	440,000	70,119	\$510,119
Year 4	0	72,120	\$72,120
Year 5	0	74,284	\$74,284
Year 6	0	76,512	\$76,512
Sale	1,000,000	0	\$1,000,000
Total	\$2,320,000	\$526,905	\$2,846,905



Getting to \$3,000,000



Assumptions:
Seller financed
3 separate loans of \$220k each
5.4% interest, 10 year term



Staged Buy-in, Seller Financed



	Principal	Interest	Earnings	Total
Year 1	\$34,117	\$22,924	\$132,000	\$189,041
Year 2	70,122	43,959	101,970	\$216,041
Year 3	107,953	\$63,169	70,119	\$241,241
Year 4	113,965	57,157	72,120	\$243,242
Year 5	120,311	50,811	74,284	\$245,413
Year 6				
Balance	873,532			\$873,532
Sale	1,000,000			\$1,000,000
Total	\$2,320,000	\$238,020	\$450,393	3,008,413



Staged Buy-in, Seller Financed



	Principal	Interest	Earnings	Total
Year 1	\$34,117	\$22,924	\$132,000	\$189,041
Year 2	70,122	43,959	101,970	\$216,041
Year 3	107,953	\$63,169	70,119	\$241,241
Year 4	113,965	57,157	72,120	\$243,242
Year 5	120,311	50,811	74,284	\$245,413
Year 6	127,011	44,111	76,512	\$247,634
Balance	746,521			\$746,521
Sale	1,000,000			\$1,000,000
Total	\$2,320,000	\$282,130	\$603,417	\$3,205,547



Projections include:



Conservative growth projections
Conservative profit distributions



Recap

- Reality – Outside interests buying specialty & general practices
- Private veterinarian specialists CAN and SHOULD become practice owners
- Total payments to the seller may be higher than VC's are willing to offer with *better* employment terms



Questions?



Thank you!

Leslie Mamalis
Leslie@SummitVeterinaryAdvisors.com
Strengthen Your Foundation for Success



summit
VETERINARY ADVISORS

SummitVeterinaryAdvisors.com