

## What's My Practice Worth?

Chris Bentson, President of Bentson Clark

At Bentson Clark, we often get the question prior to a valuation, "What do you think my practice is worth?" Obviously, value depends on many items and varies based on the financial and operational, as well as other, characteristics of the individual practice. IRS Revenue Ruling 59-60 defines fair market value of a closely held business, such as an orthodontic practice, as:

*The amount at which property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell, both parties having reasonable knowledge of relevant facts. Court decisions frequently state in addition that the hypothetical buyer and seller are assumed to be able, as well as willing, to trade and to be well informed about the property and concerning the market for such property.*

Where can you go to become "well informed" and get "reasonable knowledge of relevant facts" on the orthodontic market? Several transactional databases track and report sales prices of dental practices based on actual sales transactions. These databases include Pratt's Stats, The Goodwill Registry and the Institute of Independent Business Appraisers (IBA Database), among others. This data is often lacking key pieces of practice information, is often not specialty specific, and therefore is generally not meaningful for reviewing the orthodontic market.

Another way to know what your practice is worth is to have an independent valuation completed for your practice. This process analyzes key financial and operational characteristics of your practice and adheres to a defined valuation methodology. While the chart below presents only a few statistics for orthodontic practices recently valued by Bentson Clark, primarily overhead rates, it can give you some benchmarks to measure where you might be with regard to practice value:

Practice	Net Collections	Practice Income	Overhead Rate	Value Before Debt	Value as % of Collections
1	\$554,561	\$352,268	64.40%	\$249,167	44.93%
2	240,444	85,741	63.60%	124,587	51.82%
3	855,093	276,246	65.20%	458,494	53.62%
4	856,237	351,346	58.30%	497,490	58.10%
5	2,591,988	1,045,915	56.60%	1,554,000	59.95%
6	825,180	388,600	52.90%	556,563	67.45%
7	2,495,865	1,032,049	55.40%	1,717,000	68.79%
8	864,668	334,111	61.36%	610,000	70.55%
9	1,523,404	585,654	61.70%	1,084,375	71.18%
10	1,596,822	785,769	51.20%	1,173,000	73.46%
11	765,696	386,629	49.30%	608,000	79.40%
12	2,153,372	1,222,388	43.60%	1,750,000	81.27%
13	1,206,283	666,651	45.00%	981,566	81.37%
14	900,210	526,877	42.50%	734,436	81.58%
15	3,374,879	2,090,029	38.70%	2,835,771	84.03%
16	833,726	531,650	36.80%	707,513	84.86%
17	1,160,566	594,689	48.80%	986,000	84.96%
18	1,997,500	964,724	40.70%	1,736,986	86.96%
19	1,422,248	985,632	40.50%	1,245,000	87.54%
20	1,805,187	1,038,779	45.40%	1,583,572	87.72%
21	897,724	524,759	40.00%	788,000	87.78%
22	926,255	496,128	44.30%	816,000	88.10%
23	2,447,216	1,337,156	45.20%	2,185,000	89.29%
24	1,543,097	926,248	39.97%	1,395,000	90.40%
25	1,098,342	543,679	40.50%	996,000	90.68%
26	1,275,302	739,866	42.00%	1,177,278	92.31%
Average	\$1,392,764	\$715,238	49.00%	\$1,098,108	76.85%

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Gross collections in this sample range from \$240,000 to \$3.37 million. While this is a very large range, the average practice we valued in this sample is collecting just over \$1.39 million per year with an average practice net income of \$718,238. Many of these are multiple location, multiple doctor practices.

Since the value of a professional practice is largely dependent on the amount of income available to the owner, the practice's level of operating expenses, or overhead rate, has a significant impact on practice value, which can be noted in the previous table. In the data provided on page one, overhead rates range from 40% to 65% of net collections. This rate has been adjusted to remove non-operating practice expenses, personal expenses of the owner-doctor and the owner-doctor's compensation, retirement contributions and perks.

Notice the direct relationship that exists between practice overhead and practice value. To maximize practice value, it is essential to drive practice overhead towards 50% or below. As a guideline, we recommend staff expense (payroll, uniforms, health insurance, pension/profit sharing, etc.) range from 22-25% of net collections; orthodontic expense (lab, ortho supplies, instruments, etc.) range from 9-10%; business management expense (computer, general office, marketing, etc.) from 9-10%; and occupancy expense (rent, utilities, janitorial, repairs and maintenance, etc.) from 8-9%.

In the data given in the previous table, the value of practices as a percent of collections range from 45% to 92%, with the average being 77%. While many factors are taken into account during the valuation process, including operating expenses, additional factors that play a significant role in value include location, current trends in collections, accounts receivable and contracts receivable levels, orthodontic fees, number of active patients, number of paid in full accounts, number of patients beyond their estimated length of treatment, recall list, referral patterns, competitive environment and the condition of fixed assets.

Determining what your practice is worth takes an extensive review of your current and recent past financial and operating results. The exercise is exhaustive and needs to be completed by a competent and experienced valuation expert, such as a CVA (certified valuation analyst) or someone with similar nationally recognized valuation credentials. When it comes time to bring in an associate or partner, or to sell outright, you want to maximize the value of the practice you have built over your professional career. Focusing on lowering your overhead rate and increasing your profitability through efficiency and expense control budgeting and monitoring is a great place to start. ♦

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