

Valuation of a Dental Practice

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Whether you have an established dental practice or you are in the process of building a dental practice, there are many reasons why understanding the value of a practice may be of interest to you. The following are instances where a business valuation of a dental practice may be needed:

- To assist a buyer in assessing whether the purchase price of the practice is reasonable;
- To assist a seller in determining the sale price to an associate or a third party;
- To assist a shareholder in understanding where value can be enhanced when planning to sell in the future;
- To determine the value of assets in a practice to be transferred from a proprietorship into a corporation;
- To determine the value of the shares of a practice for a spouse's Net Family Property value needed for matrimonial purposes;
- To determine the value of practice shares or goodwill for purposes of a corporate reorganization, succession planning or the exit of a shareholder;
- To provide information to lenders to support the value of a practice, which can assist in securing financing;
- or
- To determine the amount of life insurance needed to finance the purchase of shares after the death of a shareholder.

KEY ELEMENTS IN THE VALUATION OF A DENTAL PRACTICE

In order to determine the value of a dental practice, there are several key elements to be considered. A business valuation report prepared by a Chartered Business Valuator ("CBV") details an understanding of these key elements and how they impact the value of the underlying practice. Some of the key elements are detailed below.

Cash Flows from Operations

The most significant element considered when determining the practice value is the annual sustainable cash flows generated by the practice. The historical net income of the dental practice would be reviewed to understand the level of cash flows that is sustainable, whether there are any discretionary expenses deducted, and whether there are any non-recurring items. Discretionary expenses would be adjusted if it is reasonable to assume that another practitioner would not need to incur these expenses to operate the practice or if the amounts deducted did not represent fair market value of the services provided. Discretionary expenses may include such items as wages to family members, excess advertising and promotion expenses, rent paid to a non-arm's length party, and excess travel and professional development expenses. Non-recurring expenses would be adjusted, which may include such items as non-recurring professional fees, repairs and maintenance, and advertising costs.

Historical Billings

The historical revenue generated by the practice would be reviewed to understand the billings generated both by the practitioner and through hygiene services. The hours worked by the practitioner and average hourly billings would be reviewed to understand the efforts needed to generate these billings. This information may be reviewed by a potential buyer to assess whether the billings can be sustained relative to how the new purchaser would like to operate the practice.

Billings generated by associates and the agreements regarding associate fees would be reviewed. The potential buyer may consider whether the fee arrangement is reasonable and comparable to industry averages, as well as obtain an understanding of the terms of the agreement.

Equipment and Related Expenditures

The dental equipment and the annual capital expenditures required to maintain the operations impact the value of the practice.

If a dental practice has state-of-the-art dental equipment, the cash flows generated may be higher than a dental practice that has old equipment, as less repairs on the equipment should be needed, and the state-of-the-art equipment may allow the practice to provide additional services or perform procedures more efficiently.

The Operations of the Practice

An understanding of the operations of the practice is needed, as other key factors may impact the value of goodwill within the practice. The location, the nature of the patient base, specialty services and procedures provided, staff information, and capacity of the practice are some key factors that impact the value of goodwill which is a significant driver of the overall dental practice value.

For more information on how we can assist you in understanding the value of a dental practice, please contact your **Roth Mosey** advisor.

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