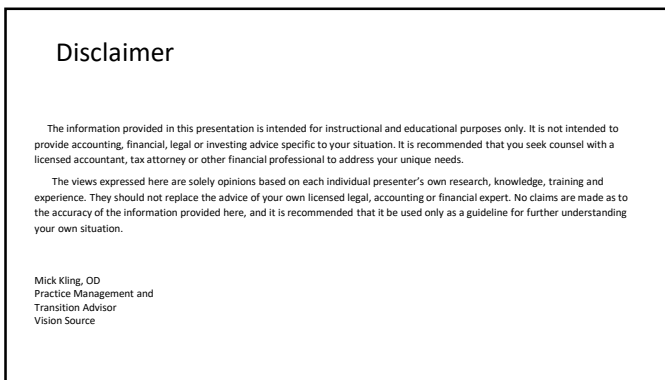
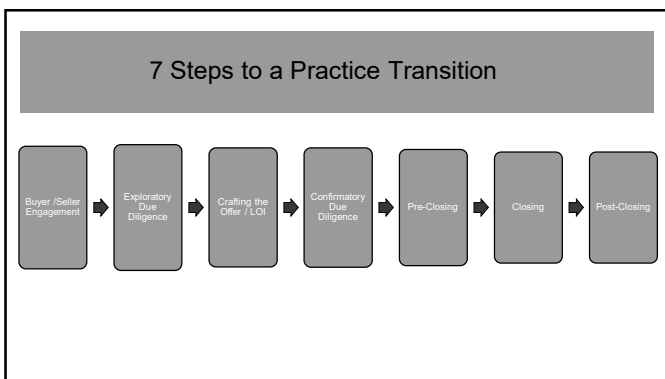




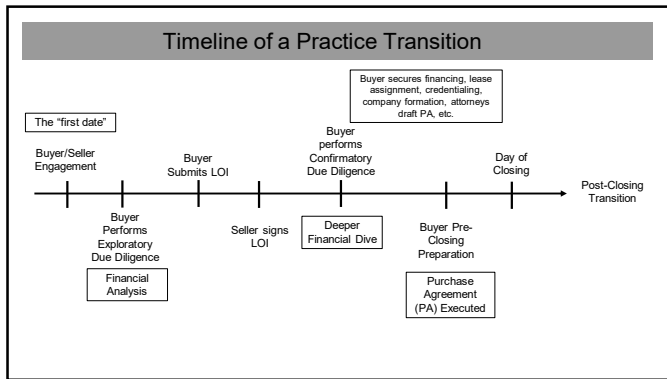
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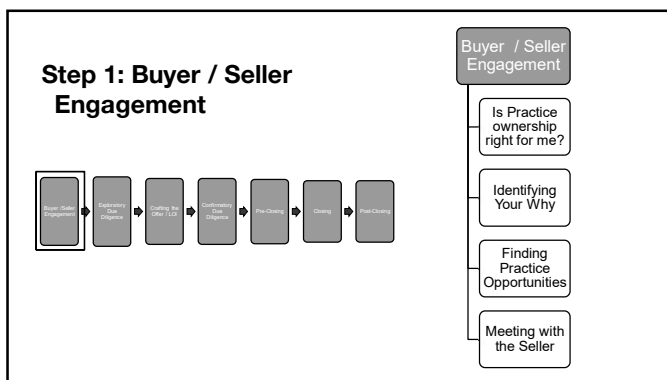
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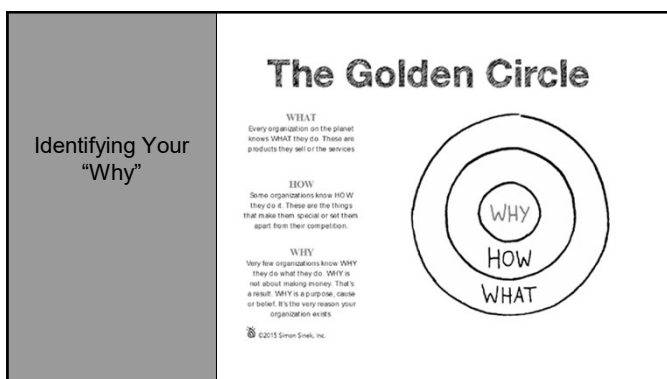
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4



5



6

Characteristics of a successful business owner

Check all that apply:

- | | |
|-------------------------------------------------------|-----------------------------------------------------------------------------|
| <input type="checkbox"/> Energy | <input type="checkbox"/> OK giving up company benefits |
| <input type="checkbox"/> Tenacity | <input type="checkbox"/> OK with professional isolation (loss of comradery) |
| <input type="checkbox"/> Grit | <input type="checkbox"/> Quick to make decisions |
| <input type="checkbox"/> Intelligence | <input type="checkbox"/> Enjoy leading others |
| <input type="checkbox"/> Organized | <input type="checkbox"/> Basic business acumen |
| <input type="checkbox"/> Willing to work longer hours | <input type="checkbox"/> Common sense |
| <input type="checkbox"/> Independent minded | <input type="checkbox"/> Confidence |
| <input type="checkbox"/> Responsible | <input type="checkbox"/> Positive attitude |
| <input type="checkbox"/> Open to change and learning | |

7



8

Is Practice
Ownership Right
For Me?

The biggest barrier to ownership is
often a lack of knowledge and
confidence.

"I don't know what to do!"

9

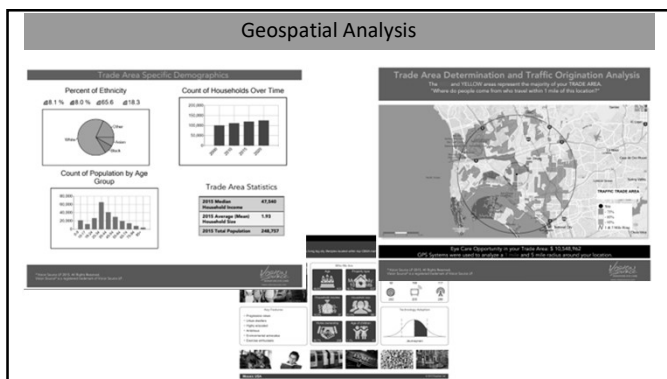
Characteristics of an Ideal Practice



10



11



12

Is Practice Size Important?

< \$1M	> \$1M
Lower risk?	Improved cash flow
Lower cost	Better facility
Fewer Hours	Faster growth
Less stress	Established Leadership
More time to make decisions	Economies of Scale
Easier funding?	Higher profit

Buy a business, not a job.

13

Rural vs. Urban Practice

	Rural Practice	Urban Practice
Practice Revenue	\$1,000,000	\$1,000,000
Cost of Goods	\$280,000	\$280,000
People Costs*	\$220,000	\$280,000
Occupancy Costs*	\$60,000	\$100,000
Other Operating Expenses	\$120,000	\$120,000
OD Compensation* (Fair Market Rate)	\$170,000	\$150,000
Practice Profit	\$150,000	\$70,000

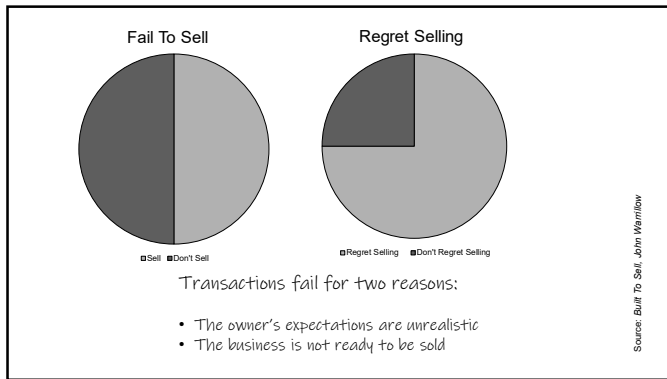
*Assumptions: COGS same for both location types; lower staff wages and occupancy costs for a rural practice; higher OD compensation for a rural practice.

14



"Successful transactions (and transitions) require both cooperation and concessions. This does not mean you are losing."

15



16

Tips for Working With The Seller

- ✓ Meet in person
- ✓ Core Values / Practice Philosophy
- ✓ Their "Why" – Pushes and Pulls
- ✓ Seller's Reputation
- ✓ Serious about Selling?

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Some Sellers Aren't Serious About Selling

- First time selling and don't realize how difficult it is
- They don't learn how much the business is worth until they've seen an offer
- They don't like the time commitment
- Uncertainty about life after the sale
- Concerned about their employees
- Loss of identity



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Signs of a Serious Seller

- 1 Non-Disclosure Agreement (NDA)
- 2 Confidential Information Memorandum (CIM) or Broker's Confidential Listing

Confidential Information Memorandum

June 30, 2013
Sample Industries, Inc.
(This is not a company.)

Prepared for:
John Smith, CPA
Smith & Associates, Inc.
100 North Dearborn Street
Chicago, IL 60610

Introduction
This Confidential Information Memorandum (CIM) is prepared for the exclusive use of the person or persons named above. It contains confidential information of Sample Industries, Inc. (Sample Industries) and its subsidiaries. It is not to be distributed outside the person or persons named above. It is to be held in strict confidence and is not to be used for any purpose other than the one for which it is prepared. It is to be destroyed when it is no longer needed. It is to be kept in a secure place and not to be loaned to anyone. It is to be kept for a period of 12 months from the date of preparation. It is to be kept in a secure place and not to be loaned to anyone. It is to be kept for a period of 12 months from the date of preparation.

Financial Snapshot
This Confidential Information Memorandum (CIM) is prepared for the exclusive use of the person or persons named above. It contains confidential information of Sample Industries, Inc. (Sample Industries) and its subsidiaries. It is not to be distributed outside the person or persons named above. It is to be held in strict confidence and is not to be used for any purpose other than the one for which it is prepared. It is to be destroyed when it is no longer needed. It is to be kept in a secure place and not to be loaned to anyone. It is to be kept for a period of 12 months from the date of preparation.

Item	Amount	Notes
Revenue	\$1,000,000	
Expenses	\$800,000	
Profit	\$200,000	
Assets	\$500,000	
Liabilities	\$300,000	
Equity	\$200,000	

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4 Common Seller Types

- **Highly Motivated Seller** - will do (just about) anything to get a deal done
- **Irrational Owner** - thinks he knows what his practice is worth, is anchored that number, and is sticking to his price without compromise
- **Chronic Negotiator** - finds any reason to drag out the deal. They often don't really want to sell.
- **Constant (Bad Faith) Negotiator** - wants to change the terms of the deal based on new information or circumstances.

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Additional Tips for Engaging with the Seller

- Understand the Seller's motivation
- Be thinking of your ideal practice. Consider location, practice size, culture, specialties, etc.
- Be prepared with questions
- Give the Seller your "Why"
- Advise the Seller on how you are going to pay for the practice
- Be prepared to sign a *Non-Disclosure Agreement (NDA)*
- Utilize your own legal and accounting team

Deals get complicated because of the people involved!

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Working With Practice Brokers

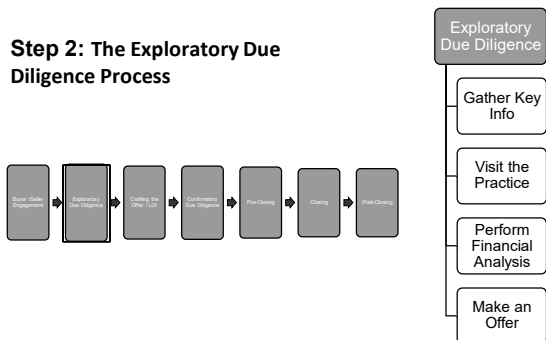
Remember...

where their loyalty lies
who is paying their fee
they often don't have your best interests in mind
may lack knowledge unique to optometry



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Step 2: The Exploratory Due Diligence Process



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Exploratory Due Diligence Information

- General Practice Information
- Operational Information
- Insurance Information
- Employee Information
- Equipment and Practice Debt
- Facility Information (Lease vs Building Ownership)
- Retail Data
- Financial Data



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Practice Acquisition Tools

- ✓ *Exploratory Due Diligence Questionnaire*
- ✓ *Practice Buyer's Checklist*
- ✓ *Forma Template*

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Visiting The Practice

External Appearance:

- Location - parking, visibility, ease of entry, security
- Exterior Appearance
- Parking Lot location and size
- **Ease of Parking**
- Traffic into and out of the parking lot
- Busy intersections nearby?
- Office Signage
- **What kinds of businesses surround the office?**

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Visiting The Practice

Internal Appearance

- First Impression
- Office odors
- Entryway
- Size of optical
- Location of reception desk
- **Frame inventory and displays**
- Exam room layout
- **Type of equipment**
- **Functionality of equipment**
- Patient flow and efficiency
- Ancillary testing space
- Room for growth/expansion

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The Financial Analysis

- P&L for the last 3 years
- Current Balance Sheet
- Tax returns for the last 3 years
- Bank statement last 3-6 months
- Aging report for any outstanding A/R's (120 days or <)
- Create a practice Pro Forma

ABC Optometry Profit and Loss January - December	
Income	
Net Patient Revenue	480,000
Net Insurance Revenue	21,000
Net Other Revenue	10,000
Net Interest Income	1,000
Net Investment Income	1,000
Net Other Income	1,000
Total Income	514,000
Cost of Goods Sold	
Net Cost of Materials	11,000
Net Cost of Labor	80,000
Net Cost of Supplies	10,000
Net Cost of Other Expenses	1,000
Total Cost of Goods Sold	102,000
Gross Profit	412,000
Expenses	
Net Insurance Premiums	10,000
Net Medical Malpractice	10,000
Net Other Insurance	10,000
Net Rent & Lease Expenses	10,000
Net Telephone & Internet	1,000
Net Travel & Entertainment	1,000
Net Utilities	1,000
Net Depreciation & Amortization	1,000
Net Other Expenses	1,000
Total Expenses	44,000
Net Profit	368,000

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Creating A Practice Pro Forma

10-Year Pro Forma: Only enter data into cells with BLUE text

INCOME		Year 1 Assumptions									
OD Lines Days Per Week	\$										
Exams Per Day	20										
Exams Per Month	200										
Exams Per Year	2,400										
Projected Revenue Per Exam	\$400										
Projected YOY Growth	5%										
PROJECTED ANNUAL REVENUE		\$ 998,400	\$ 1,048,320	\$ 1,100,736	\$ 1,155,770	\$ 1,213,561	\$ 1,274,240	\$ 1,337,951	\$ 1,404,849	\$ 1,475,092	\$ 1,548,846
EXPENSES											
Cost of Goods Sold (COGS)	28%	\$ 279,552	\$ 293,530	\$ 308,206	\$ 323,616	\$ 339,797	\$ 356,787	\$ 374,626	\$ 393,358	\$ 413,026	\$ 433,677
Gross Margin	72%	\$ 718,848	\$ 754,790	\$ 792,530	\$ 832,154	\$ 873,764	\$ 917,452	\$ 963,325	\$ 1,011,491	\$ 1,062,066	\$ 1,115,169
Non-OD Staff Payroll	25%	\$ 249,600	\$ 262,080	\$ 275,184	\$ 288,943	\$ 303,390	\$ 318,560	\$ 334,488	\$ 351,212	\$ 368,779	\$ 387,212
Occupancy	7.5%										
Annual Increase											
Rent	\$	\$ 65,000	\$ 66,950	\$ 68,959	\$ 71,027	\$ 73,154	\$ 75,353	\$ 77,613	\$ 79,942	\$ 82,340	\$ 84,810
Repair/Maint	\$	\$ 2,500	\$ 2,500	\$ 2,500	\$ 2,500	\$ 2,500	\$ 2,500	\$ 2,500	\$ 2,500	\$ 2,500	\$ 2,500
Security	\$	\$ 600	\$ 600	\$ 600	\$ 600	\$ 600	\$ 600	\$ 600	\$ 600	\$ 600	\$ 600
Utilities	\$	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000
Marketing	5%										
Advertising/Referring		\$ 9,984	\$ 10,483	\$ 11,007	\$ 11,558	\$ 12,136	\$ 12,742	\$ 13,380	\$ 14,048	\$ 14,750	\$ 15,488

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Creating A Practice Pro Forma

NET OPERATING INCOME (\$)		\$ 255,372	\$ 268,695	\$ 284,984	\$ 303,678	\$ 324,817	\$ 348,446	\$ 374,610	\$ 403,358	\$ 435,840	\$ 472,009
		25.6%	25.7%	25.9%	26.0%	26.2%	26.4%	26.5%	26.6%	26.8%	26.9%
OD FM Comp	16.0%	\$ 159,744	\$ 167,732	\$ 176,118	\$ 184,924	\$ 194,170	\$ 203,878	\$ 214,072	\$ 224,776	\$ 236,015	\$ 247,815
NET +/- CASH FLOW (EBITDA)		\$ 95,628	\$ 101,964	\$ 108,866	\$ 116,154	\$ 123,887	\$ 131,968	\$ 140,518	\$ 149,582	\$ 159,125	\$ 169,193
Debt Service (Int)**		\$ 63,639	\$ 63,639	\$ 63,639	\$ 63,639	\$ 63,639	\$ 63,639	\$ 63,639	\$ 63,639	\$ 63,639	\$ 63,639
Tax Rate											
Tax Liability	20%	\$ 19,088	\$ 20,393	\$ 21,779	\$ 23,231	\$ 24,769	\$ 26,394	\$ 28,108	\$ 29,916	\$ 31,825	\$ 33,839
NET CASH FLOW (\$ After Tax + Debt)		\$ 12,703	\$ 17,932	\$ 23,454	\$ 29,284	\$ 35,488	\$ 41,935	\$ 48,791	\$ 56,027	\$ 63,663	\$ 71,715
NET +/- (After Tax + Debt)		1.3%	1.7%	2.1%	2.5%	2.9%	3.3%	3.6%	4.0%	4.3%	4.6%
Debt Analysis											
Total Cash Required		\$ 82,725	\$ 84,032	\$ 85,413	\$ 86,870	\$ 88,409	\$ 90,033	\$ 91,747	\$ 93,556	\$ 95,464	\$ 97,473
OSCR (Target > 1.25)		1.35	1.21	1.27	1.34	1.40	1.47	1.53	1.60	1.67	1.74
Pre-Tax Cash Flow (After Debt)		\$ 31,789	\$ 38,325	\$ 45,227	\$ 52,515	\$ 60,208	\$ 68,328	\$ 76,899	\$ 85,943	\$ 95,480	\$ 105,554
Pre-Tax Return		3.2%	3.7%	4.1%	4.5%	5.0%	5.4%	5.7%	6.1%	6.5%	6.8%
ASSUMPTIONS:											
Loan Amount	\$500,000										
Interest Rate	5.00%										
Term	10										
Monthly Payment	\$61,639.31										
Loan - Revenue	10.3%										

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Key Metric	Formula
Revenue Per Exam (\$)	Total Revenue / Total Comprehensive Exams
Exam Capture Rate (%)	Exams Performed / Exam Slots Available
Frame Capture Rate (%)	Frames Sold / Total Comprehensive Exams
Lens Pairs Capture Rate (%)	Lens Pairs Sold / Total Comprehensive Exams
Average Eyewear Sale (\$)	Optical Sales / Lens Pairs Sold
CL Material Sales (\$)	CL Sales / CL Exams Performed
Exams Per Doctor Hour	Exams Performed / Total Doctor Hours
Revenue Per Doctor Hour	Total Revenue / Total Doctor Hours

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[illegible]

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- Loans must be **retired** at closing.
- Some **leases** may not be transferable.
- Assumed debt will **reduce** the purchase price.
- **Pre-pay penalties** may apply.



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Office Lease / Real Estate Considerations

[illegible]

Additional Exploratory Due Diligence Considerations

- Professional and Retail Fee Schedule
- Assessing the competition
- Assessing the Practice Culture
- Insurance considerations
- Accounts Receivable Considerations
- Assessing the Reputation of the practice
- Doctor/Owner transition plans



Post-Exploratory Due Diligence Considerations

- Is this a good cultural and lifestyle fit for me?
- Is the owner serious about selling?
- Does this make financial sense? (Does the math work?)
- Is the landlord likely to cooperate?
- Am I comfortable with the risk?
- Am I ready to make an offer?



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Step 3 (Part 1): Crafting Your Offer / Submitting the Letter of Intent (LOI)

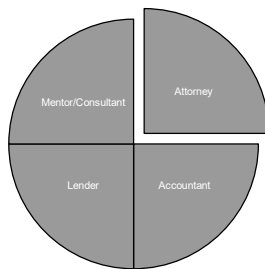


Crafting Your Offer

- Assembling Your Team
- What is this practice worth?
- What am I buying?
- Valuation Considerations
- Engaging the Lender

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Assembling Your Team



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What is this practice worth?

Fair market value (FMV) is the **price** an asset would sell for (the practice) on the **open market**.

It is the price that would be agreed on between a **willing buyer** and a **willing seller**, with neither being required to act, and both having reasonable knowledge of the relevant facts.

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A Balance Sheet Perspective

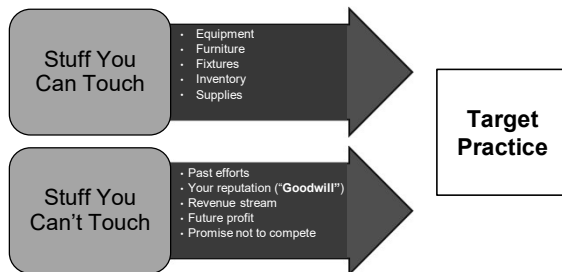
Assets (Stuff you own)
- Liabilities (Stuff you owe)

Equity (What's left)

If you were to sell everything, and pay off all your debt,
 it's what's left over.

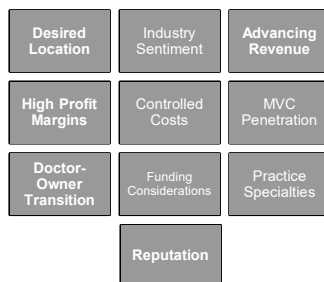
40

What Are You Buying?



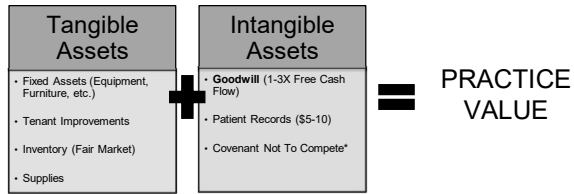
41

What creates value beyond the Balance Sheet?



42

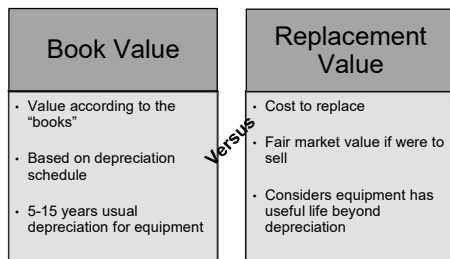
Understanding Practice Value



**The value of a non-competition agreement is represented by the present value of the cash flows that would be lost if the covenantor were to compete, adjusted for the effective probability that the covenantor would compete, and compete successfully.* Source: GBQ Consulting.com

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Tangible Assets



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Intangible Assets

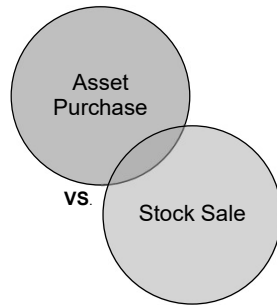
Goodwill. The "glue" to value.



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Transaction Types

- **Asset purchase** buys both tangible and intangible assets.
- **Stock sale** acquires the company's stock.
- Stock sale transfers **liability** to new owner.
- Most **healthcare** practices are sold as an asset sale.
- There are **tax advantages** to the **Seller** with a stock sale, and advantages to the **Buyer** in an asset purchase.



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Stock Sale vs. Asset Purchase

Stock Sale	Advantage	Disadvantage
Seller	Decreased liability; Tax advantages	May be some liability transferred
Buyer	Assumes third party contracts; TIN established; Simplified process; Avoids recredentiailling	Increased liability; Lost tax benefits
Asset Purchase	Advantage	Disadvantage
Seller	Negotiating leverage?	Reduced tax advantages
Buyer	Decreased liability; Choose which assets to purchase; Tax advantages	Must reapply for third party payors and TIN

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Allocation of the Purchase Price

- Both Buyer and Seller are required to report to the IRS the purchase price (**Form 8954**) of each asset type.
- The report must be the **same** for both the buyer and seller.
- The asset purchase price allocation must be **negotiated prior to the sale**.
- The reported price must be "**fair market value**", what a Buyer is willing to pay to a Seller.

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Tax Consequences of a Practice Sale*

Asset Type	Ordinary Income	LT Capital Gain
Supplies	X	
Equipment	X	
Inventory	X	
Tenant Improvements	?	?
Non-Compete	X	
Patient Records		X
Goodwill		X

*NOTE: Not intended as tax advice. Always consult your tax advisor.

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Purchase Price Allocation Tax Advantages*

Asset Type	Buyer	Seller
Supplies	✓	
Equipment	✓	
Inventory	✓	
Tenant Improvements	?	?
Non-Compete	✓	
Patient Records		✓
Goodwill		✓

*NOTE: Not intended as tax advice. Always consult your tax advisor.

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Valuation Methods

% of Revenue	Summation of Assets	Capitalization of Earnings
Multiple of Practice Earnings	Multiple of EBITDA	Available Debt Service

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Valuation Method: Multiple of EBITDA

- Used by **private equity (PE)**
- Earnings Before **Interest, Taxes, Depreciation and Amortization**
- Multiple** applied to EBITDA to determine value
- Multiples range from **4-8X** (sometimes higher)
- Owner **“add backs”** critical in determining value

Example:

Practice Revenue	\$800K
Practice Net	\$224K (28%)
OD FM Comp	\$140K (17.5%)
EBITDA	\$84K
Multiple	6X
Practice Value	\$504K
The Math:	$\$84K \times 6 = \$504K$

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What are Add Backs?

- Auto expenses
- Donations
- Continuing Education
- Personal cell phone
- One-time repairs
- Travel and meals
- Depreciation/Amortization
- Interest
- Personal Taxes
- Excessive owner compensation
- Adjustment to staff wages
- Certain legal fees
- Non-recurring income and expenses



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Valuation Method: Available Debt Service

- Value based on what's left to **service the debt**.
- This is what the **banks** care about.
- Practice size and **control of expenses** greatly affect what's left to service debt.
- Every expense bucket has a **HUGE** impact on practice value.
- It's all about **cash flow**.

Example:

Practice Revenue	\$800K
Practice Net	\$224K (28%)
OD FM Comp	\$140K (17.5%)
Free Cash Flow	\$84K
Available for Debt Service	\$67K (P+I)
Amortization	10 years
Practice Loan	\$560K

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Pro Tip: Debt Service Coverage Ratio

- A measure of a business's available **cash flow** to cover its debt obligations.
- Indicates whether a company has the income available to **cover its debt**.
- Banks often use it to determine cash flow available to determine **loan amount**.
- Most banks require a **1.20 DSCR or >** as a minimum to lend.

Formula:

$$\text{DSCR} = \frac{\text{Available Cash Flow}}{\text{Total Debt Service}}$$

Practice Free Cash Flow	\$84K
Debt Service (P+I)	\$67K

$$\text{DSCR} = \$84K / \$67K = 1.25$$

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Managing A/Rs Post-Closing

Day of Closing

Dr. Seller (or associates) provides eye care services and sells products. All revenue generated belongs to **Dr. Seller** through day of Closing.



Dr. Buyer (or associates) provides eye care services and sells products. All revenue generated belongs to **Dr. Seller** after day of Closing.

Revenue collected Post-Closing that belongs to **Dr. Seller**

Bills due (mostly vendors) Post-Closing that belong to **Dr. Seller**



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Managing A/Rs Post-Closing

Possible Solutions	Advantages	Disadvantages
Include A/Rs in Purchase Price	Simple and easy for Seller. Transfers risk of collecting to Buyer.	Collectable A/Rs difficult to determine. May create a negotiation stumbling block with Buyer.
Buyer and Seller Track A/Rs and reconcile monthly	Clean and fair. Each party receives it's share of revenue and expenses it deserves.	Requires detailed recordkeeping, tracking and <u>trust</u> between the parties.
Buyer assumes both Receivables and Payables Post-Closing	Simple and easy to manage. Transfers risk of collecting to Buyer and avoids bookkeeping tasks.	If Receivables exceed Payables, Seller may be leaving cash on the table.

57

Should I pay for an appraisal?

58

How much Working Capital should I have?

59

The practice value must be based on past performance, not future potential.

A buyer should only pay what the **cash flow** will support. Anything more rewards the Seller for the Buyer's **future efforts**, and potentially sets the Buyer up for **failure**.

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Options for Bridging a Valuation Gap

Seller Carried Note

- Seller earned interest
- Usually higher interest rate

Earn Out

- Shifts some risk to Seller
- Provides opportunity for higher value

Consulting Agreement

- Paid expertise over/above OD Comp
- Varied term

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Seller Carried Note

Advantages

- Easier/faster transaction
- May increase purchase price
- Default returns asset to you
- Possible tax advantages

Disadvantages

- You take the risk
- Low Yield: May earn better return elsewhere
- Ties up your cash for other opportunities
- Default could create challenges

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Buying Into A Partnership

Advantages

Usually larger practices
Less initial costs
Lowers risk?
Collaboration
Greater borrowing capacity
Talent Sharing
Emotional support

Disadvantages

Relationship complexities
Loss of control/autonomy
Future exiting complications
Compromise required

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Step 3 (Part 2): Crafting Your Offer / Submitting the Letter of Intent (LOI)



Submitting the LOI

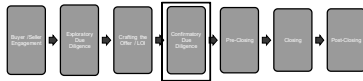
What is the
LOI?

Elements
of the LOI

Engaging
the
Attorney

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Step 4: The Confirmatory Due Diligence Process



Confirmatory Due Diligence

Legal

• Drafting the PA

Financial

• Finalize Funding

Finalize the
Lease

Employment
Agreement

PM/Operational
Considerations

Create
Purchasing Entity

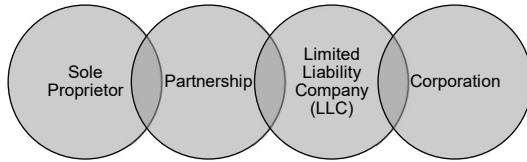
65

Additional Due Diligence Tasks

- UCC Filings
- Tax Clearance from the IRS

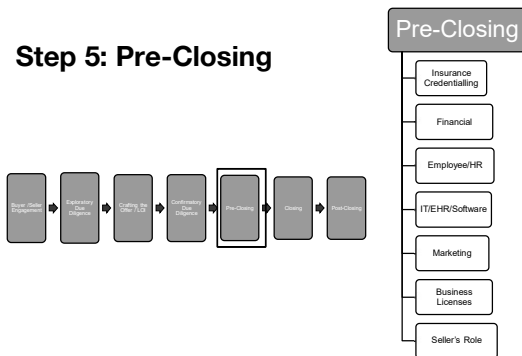
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Creating the Purchasing Entity



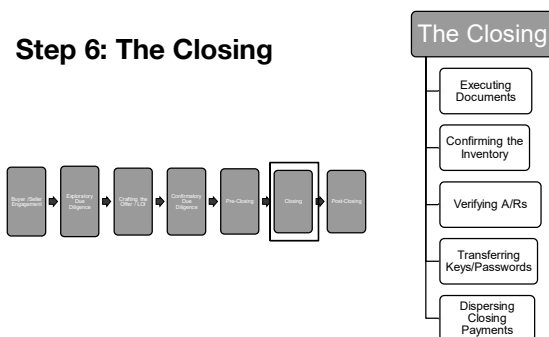
67

Step 5: Pre-Closing

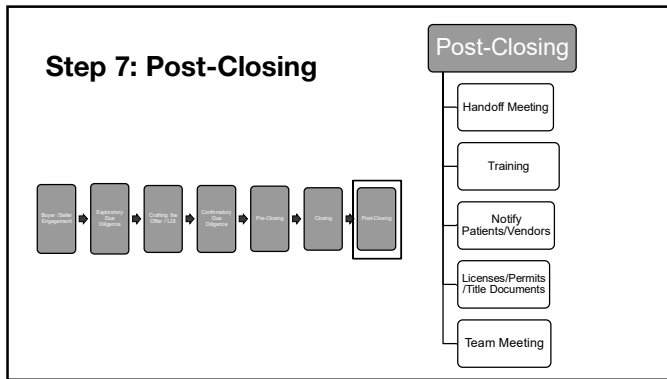


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Step 6: The Closing



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Employees and Culture

Power Distance

Direct vs Indirect Communication

- Introduce yourself
- Share your goals
- Be consistent with your actions and words
- Discuss how decisions are made
- Learn from the existing business systems
- Clarify expectations and lines of communication
- Don't get hung up on minor issues
- Communicate where to go with questions
- Do what you say you are going to do
- Remember that you are the most contagious personality in the office
- Be sensitive to existing office traditions
- You will lose patients and employees over time – and that's OK
- Communicate all new expectations clearly

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Dealing with Uncooperative Sellers

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Thank You!



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