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MANAGING YOUR DERMATOLOGY PRACTICE

What Is Your Practice Worth?

At least once during your career, you will probably have to put a value on your practice. The need arises more often than you might think—if you sell it, of course; but also for estate

planning, preparation of financial statements, and, unfortunately, during divorce negotiations; when an associate joins or leaves your office; or if you have occasion to combine or partner your practice with one or more others.

As you might guess, a medical practice is trickier to value than an ordinary business, and usually requires the services of an experienced professional appraiser. Entire books have been written on how to do

it so I can't hope to cover the entire subject in 750 words, but there are three basic components to a practice appraisal:

► **Tangible assets.** Equipment, cash, accounts receivable, and other property owned by the practice.

► **Liabilities.** Accounts payable and outstanding loans.

► **Intangible assets/“goodwill.”** The reputation of the physicians, the location and name recognition of the practice, the

loyalty and volume of patients, etc.

Using these components, there are three traditional approaches to determining value:

► **Asset-based valuation.** This approach uses a balance sheet to determine equity, the difference between what a practice owns (its assets) and what it owes (liabilities). (I covered balance sheets in the January 2006 column. If you missed it, you can go to www.skinandallergynews.com and click on “The Archive Collection.”) With this information, one can arrive at the book value of the practice as of a particular date. The value of intangible assets is then estimated by measuring factors such as those mentioned above.

► **Income-based valuation.** This looks at the source and strength of a practice's income stream as a creator of value, and whether that income stream under a different owner would mirror its present one. This, in turn, becomes the basis for an understanding of the fair market value of both tangible and intangible assets.

► **Market valuation.** This combines the previous two approaches and attempts to determine what the practice is worth in the local market by analyzing sales and mergers of comparable practices in the community.

Valuing tangible assets is comparatively straightforward, but there are several ways to do it, and when reviewing a practice appraisal you should ask which of them was used. Depreciated value is the book value of equipment and supplies as determined by their purchase price, less the amount their value has decreased since purchase. Remaining useful life value estimates how long the equipment can be expected to last. Market (or replacement) value is the amount it would cost on the open market to replace all equipment and supplies.

Intangible assets are more difficult to value. Many components are analyzed, including location, interior and exterior decor, accessibility to patients, age and functional status of equipment, systems in place to promote efficiency, reasons why patients come back (if in fact they do), and the overall reputation of the practice in the community. Other important factors include the payer mix (what percentage pays cash, how many third-party contracts are in place and how well they pay, etc.), and the extent and strength of the referral base.

It also is important to determine to what extent intangible assets can be transferred to another owner. Although such qualities as unique skill with a laser or filler substances and extraordinary personal charisma may increase your practice's value to you, they will be of little use to the next owner and he or she will be unwilling to pay for them.

Professional appraisers use a variety of techniques to estimate intangible asset value, and once again you should ask which were used. Cash flow analysis works on the assumption that cash flow is a measure of intangible value. Capitalization of earnings puts a value, or capital-

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Going to Court? Preparation and Records Are Key

BY ROXANNE NELSON
Contributing Writer

BOCA RATON, FLA. — Medical malpractice suits are common, and many physicians are unaware of the procedures and protocols involved in building a strong defense, Cliff Rapp said at the annual meeting of the Florida Society for Dermatology and Dermatologic Surgery.

The law is less concerned with rightness or wrongness than it is with justifiability. "You have to understand this going in. The legal system is about money, and you will be the pawn," said Mr. Rapp, vice president of risk management for First Professionals Insurance Co., in Jacksonville, Fla.

Early preparation is the key, he explained. Medical records will become evidence, and early on, the plaintiff's attorney will review the records to see if there are sufficient holes to bring it to court. In fact, a request for medical records is the first indication that something is going on.

It is essential not to ignore or be late with a request for records. "They usually ask you to provide a copy within 10 business days. And never alter your records. It's a crime, so just don't do it," Mr. Rapp said.

Keep the patient's chart separate from other records and create a separate personal file. "And never contact the patient's attorney directly," he said.

The 90-day presuit screening process begins with the notice of intent letter. During this period, the physician can admit guilt, deny any wrongdoing, or arbi-

trate. At the conclusion of the presuit, the claimant has 60 days or the remainder of the statute of limitations to file suit.

"Usually, if you don't settle, this will be the end of the lawsuit," Mr. Rapp said.

If the patient does pursue it, the physician must become his or her own best expert. Educate your defense team, Mr. Rapp pointed out. Invest the time to conduct research, evaluate medical literature, and obtain current seminar material.

You also need to work with your attor-

ney, he explained, and should be honest, up front, and participate in your defense.

"The No. 1 mistake made during the deposition is being unprepared," Mr. Rapp explained. "The No. 2 mistake is not listening to the question, and the No. 3 mistake is trying to 'outsneak' the plaintiff's attorney."

Mr. Rapp strongly suggests that the physician visit the courtroom ahead of time and scope it out. Don't let the day of the trial be your first time there, he advised.

Attendance is mandatory at the trial, and it is important to give the right impression, he said. This means appearing on time, being conservative in dress and demeanor, and not arriving at the courthouse in a flashy, expensive automobile. "Arrive and leave with your attorney," he said.

Once the trial is underway, participate in your defense. It is important to pay attention to every detail, Mr. Rapp emphasized, and to take notes as well as to alert your attorney to any mistakes. ■

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ization, on the practice's income streams using a variety of assumptions. Guideline comparison uses various publications, databases, and other records of transactions to compare your practice with other, similar ones that have changed hands in the past.

Two newer techniques that some believe provide a better estimate of intangible assets are the replacement method, which estimates the costs of starting the practice over again in the current market, and the excess earnings method, which determines the average earnings of a practice within your specialty and then measures how far above average your practice's earnings are. The theory behind the latter method is that a practice with above-average earnings is more valuable than an average one.

Whatever methods are used, it is important that the appraisal be done by an experienced financial consultant, that all techniques used in the valuation be divulged and explained, and that documentation is supplied to support the conclusions reached. This is especially important if the appraisal will be relied upon in the sale of the practice. We'll talk about that next month. ■

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