

**Question:**

**Under what circumstances should I have my dental practice appraised? What elements are included in a professional practice appraisal?**

**Answer:**

You've worked long and hard to build your practice into a successful, profitable one. Besides your home and retirement savings, it is undoubtedly your most valuable asset. And just as you would appraise your home before selling it, you should also determine the fair market value of your practice before making important decisions about it.

A dental practice appraisal is the best way to determine fair market value. When we talk about fair or current market value, we really mean the highest price that a practice will bring when offered for sale by a willing seller and purchased by a willing buyer within a reasonable period of time. You should keep in mind that market value and selling price are not necessarily the same number. The selling price can be lower than the value an appraiser places on the practice due to such special considerations as the need of a dentist to sell quickly or inadequate marketing of practice selling points to prospective buyers.

The most common reason a dentist calls us to do an appraisal is because he or she is selling their practice. If you're a sole practitioner, it's best to have your practice appraised at the time you want to sell it, so that its fair market value reflects today's marketplace. If you're in a dental partnership, it's a good idea to appraise the practice periodically. An up-to-date appraisal can be very helpful for surfacing and resolving issues related to partner buyouts at a later date. Some dentists will have a practice appraised for financial and estate planning purposes, even though they plan to continue practicing for a number of years.

**Elements of an Appraisal**

When we list a practice for sale, conducting an appraisal is always the first step. It's our blueprint for developing the selling price and the written practice description that are used to sell a practice successfully.

Here are the key components of a professional appraisal:

1. **History of practice:** This section provides background on the doctor and the practice, including details about how long the practice has been established, current and previous locations, and any special attributes of the practice, like specialized procedures the doctor performs.

2. Gross/net income: Derived from the tax returns of the practice, this section discloses reported gross income for the last three years and the year-to-date. The net income is derived by restructuring practice expenses to reflect the true profit and cash flow of the practice. To calculate the true profit, non-cash deductions (i.e. depreciation and amortization) and personal expenses not necessary to run the practice (i.e. the owner's medical insurance or car lease payments) are added back to profits. This part of the appraisal is key to assessing practice value. If the practice is being sold, it will be used by the purchaser's accountant and financing source to determine how the purchase price is to be funded and the remaining cash flow for the practitioner.

3. Patient profile: Discussed here are the demographics of the patient base, including age range and relevant socioeconomic factors. The number of patients treated weekly by the dentist and the hygienist should be indicated. The number of active (an individual treated within the last two years) and new patients are important barometers of practice vitality and growth.

4. Description of the facility: Included here is information about the size and layout of the office, including the number of operatories, staff areas, and condition of equipment. If the space is leased, information should be provided about the lease term and monthly rent. If the facility is owned, the price of the real estate and/or terms of the lease should be noted.

5. Community profile: Demographics about the community include descriptions of the type of community, i.e. urban, suburban or small town, whether it's working, middle or upper middle class, and positive features about the area.

6. Office hours: This section lists practice office hours for the owner, associates, hygienist(s) and office staff.

7. Fee structure: Included is a breakdown of fees by procedures, as well as by fee-for-service and reduced fee plans. If available, the percentage of the dentist's income produced by each procedure should also be noted.

With this information in hand, the appraiser's job is to derive the practice value. One appraisal model we use is known as the composite valuation method (see sidebar for example). This industry-accepted method is heavily weighted towards practice income and patient base, which we believe are the two most critical determinants of the value of a practice. The dentist's salary, which is part of net earnings, is also a factor in the valuation. The composite valuation method compares the common elements found in dental practices to an ideal practice, or model, in order to develop a percentile rating. That rating is then multiplied by 1.0 to 1.5, a standard market factor for net receipts, or profitability. The assignment of the market factor is an appraiser's subjective judgment, based on valuation variables like the desirability of the practice location and comparisons with similar practice sales in the area. The resulting percentage is then multiplied by practice net earnings and the value derived is added to the value of the tangible assets, i.e. equipment, leasehold improvements, to obtain the fair market value of the practice.

You should keep in mind that while an appraisal is an important tool, all appraisals use subjective valuation criteria to arrive at their conclusions. Also, an appraisal is only as reliable as

the professional who's conducting it. The appraiser should be a practice broker or transition consultant who is knowledgeable about the dental marketplace and has firsthand information about actual sales in similar areas. Otherwise, the value derived is no more scientific than you arbitrarily assigning a percentage of your practice gross income and calling it the fair market value—a valuation technique we've seen some dentists use in lieu of a professional appraisal. While it's true that most practices sell for half to three quarters of their gross income, establishing a selling price this way doesn't tell potential buyers anything about your practice and how you arrived at the price. In effect, this approach makes it sound like all practices are the same.

When you sell your practice, you are entitled to receive its maximum value and the purchaser is entitled to have sufficient information about your practice and its key features to understand what makes it an attractive opportunity. A professionally conducted appraisal that establishes a rationale for your practice selling price by clearly explaining and valuing its special features will go a long way towards helping you market your practice successfully when the time comes.

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