

Collins Forensic and Valuation Services

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Valuing Dental Practices

Dental practices are valued based on their net tangible assets and goodwill.

NET TANGIBLE ASSETS

A practice's net tangible assets are determined by totaling the value of the practice's assets (such as cash, accounts receivable, work in progress, equipment and furniture) and subtracting the practice's outstanding debt. Accounts receivable are valued at their expected collection amount.

GOODWILL

Goodwill is derived from a dental practice's ability to generate future cash flow based on its reputation, client list, location, affiliation, previous advertising, etc.

Business appraisers often determine a practice's goodwill by utilizing the market approach. To value a dental practice under this approach, the practice's annual revenues and cash flow after expenses must be determined. This financial information can be obtained by reviewing the practice's prior year tax returns and financial statements.

A practice's true cash flow is the cash flow the practice could provide to a prospective owner. Adjustments are often made to increase or "addback" the owner's perquisites to the practice's stated book income to determine the practice's true cash flow.

MARKET APPROACH

Dental practices are routinely bought and sold across America. The financial information from these transactions is compiled by companies that maintain transactional databases such as the Goodwill Registry and Pratt's Stats.

By sorting these transactions by their attributes such as the practice type (general or specialty) and their revenues, cash flow, profit margins, years in business, etc., business appraisers can determine the revenue and cash flow valuation multiples at which a dental practice is likely to sell.

The valuation multiples from these transactions, after other factors are considered, are then applied to the revenue and cash flow of the practice being valued.

FACTORS AFFECTING VALUATION MULTIPLES

General dental practices sell at higher valuation multiples than specialty dental practices. Also, practices with higher earnings and productivity sell at higher multiples while practices relying on managed care, capitation plans, Medicaid, etc. sell at lower multiples.

On average, general dental practices are often sold at goodwill multiples of roughly 50% of their annual revenues and roughly 100% of their annual cash flow. These multiples assume the dental practice has a gross profit margin (before owner's compensation) of approximately 40% of revenues.

DENTISTS' EARNINGS

Average earnings and productivity for general and specialty dentists can be found in publications produced by the ADA (American Dental Association). These studies allow business appraisers to determine if the dental practice at hand is more profitable and hence more valuable than similar practices in the industry.



QUESTIONS OR COMMENTS

Please call me with your questions or comments at 916.756.5622.

— Thomas Collins, CPA / ABV, CFA