Building Value: An Ongoing Priority

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1. Introduction
If your goal is to sell your practice for a future financial benefit, your practice is an investment and should be treated as one. All too often, practice value is made a priority when it is too late...when it comes time to cash in on the investment and sell the practice. Building value should be an ongoing priority.

For many veterinarians, their practice is their greatest financial asset and one that is relied on to help fund their retirement. How do we treat this significant investment compared with our other investments? Do we monitor our practice value as closely as we monitor our other investment values? Chances are you monitor your other investments on a regular basis for any increase or decrease in value.

We have significantly more control over the value of our practice investments than the value of our other investments because we have decision-making authority in our practices. We can make decisions that will impact value. Compare this to our ability to make decisions that affect the value of our stocks or bonds. There isn't much comparison. Why do we spend so much time monitoring the value of investments that we have little control over and so little time monitoring the value of our investment that we do have control over?

2. Practice Value
Practice valuation is a specialized field, and it continues to become more specialized. Methodologies vary greatly, and there are inconsistencies in the field. The Veterinary Valuation Resource Council (VVRC) of VetPartners (www.VetPartners.org) is working toward more standardization in the field of veterinary practice valuations to reduce these inconsistencies.

A basic understanding of practice valuation will help you make the right decisions regarding your practice investment. Practice value is primarily a function of two components: profit and risk.

Risk involves the risk of receiving profits in the future. As an owner, you can improve your practice value by making decisions that affect your profit and by reducing the risks of receiving those profits in the future.

3. Profit
Profit from a business valuator's perspective is different from the profit reported to the government for tax purposes. By reporting lower profits, business owners can save tax dollars. As a result, the profit reported for tax purposes may not be totally representative of the true profit potential in the business.

The goal of a business valuator is to determine the amount of profit that would flow through to you as a result of owning an investment.
Consider yourself as a silent partner in your practice. What money would flow through to you as a result of owning the practice? This does not include your salary as a practicing veterinarian, nor does this include rent money that you may receive as a result of owning the real estate used to deliver veterinary services.

Several adjustments may be necessary to determine your true profit for valuation purposes versus your profit reported to the government for tax purposes. The VVRC continues to work toward agreement on the types of adjustments that should be considered.

4. Risk
There are several risks associated with a business owner’s ability to receive future profits. Business valuators go through a methodical process to determine the specific risks associated with your particular practice.

The VVRC has also identified key risk factors to be considered in valuing veterinary practices. These risk factors are continually evolving and require each business valuator to use their personal judgment. The process of evaluating a practice for each risk factor developed by the VVRC builds consistency into the valuation process.

5. Equine Practices: How Do They Differ?
Equine veterinary practices share many of the same risk factors as small animal practices; however, there tends to be more personal goodwill present in equine practices, which has no commercial value. This type of goodwill cannot be transferred during a sale.

There are a larger number of single doctor equine mobile practices than there are single doctor small animal mobile practices. This has implications as far as the transferability of goodwill and practice value. A larger practice with multiple veterinarians can transfer commercial goodwill more successfully than a single doctor equine practice. There is less risk involved in receiving future profits (implying higher value) with the sale/purchase of a multi-doctor practice than the sale/purchase of a single-doctor practice.

Practice “location” is a risk factor examined during a practice valuation. How does a practice location affect the risk of receiving profits in the future in light of a practice sale? A small animal practice with a good location is considered a lower risk, implying a higher value, than a small animal practice with a poor location. What about an equine mobile practice with no fixed location? A mobile practice without a fixed location to operate from carries with it a higher risk (implying lower value) than a practice with a fixed location. The main reason for the difference in risk involves “locational goodwill.” This type of goodwill has commercial value. An equine practice operating from a facility at a specific location provides a new purchasing owner with some assurance that clients will return to the same location to purchase products and services regardless of who owns the practice. The location provides a draw for clients and not just the individual veterinarian.

Additional considerations for valuing your practice investment include revenue and profitability trends, quality and tenure of staff, marketability of the practice, types of services offered, degree of competitiveness in the environment, leasing terms, integration of management systems, demographic profile of the area, and overall stability of the practice. Probably the most significant difference between most equine practices and most small animal practices is the ability to transfer goodwill.

6. Conclusion
As an owner of a practice investment, it is important for you to understand how your decisions affect the value of your investment. If you plan to sell your practice in the future for some financial benefit, your practice is an investment and should be treated as such.

You should expect an ongoing return and expect an increase in value.

Decisions that maximize your profits and minimize the risk of receiving future profits will help you build value in your long-term investment.