EXIT STRATEGY CHECKLISTS

The following checklists, materials and items have been compiled through the cooperation and effort of the following firms and individuals.

Roger Cummings, CVPM, and Lou Gatto, CPA,
Byron Farquer, DVM and Philip Homsey, Esq.

VPMG BRAKKE
VETERINARY PRACTICE MANAGEMENT GROUP
2735 Villa Creek Suite 140
Dallas, Texas 75234
Phone : 972.243.4033
Fax: 972.243.0925
vpmg@brakkeconsulting.com

Certified Public Accountants
Gatto McFerson
528 Arizona Ave. Suite 201
Santa Monica, CA 90401
Phone: 310.393.2434
Fax 310.393.8777
info@gattomcferson.com

SIMMONS & ASSOCIATES
Veterinary Practice Brokers since 1977
11737 Twenty Six Mile Rd.
Oakdale, CA 95361
Phone: 800.333.1984
Fax: 305.675.6183
pacific@simmonsinc.com

Philip R. Homsey II Esq.
Post Box 29-1970
Los Angeles, CA. 90027
Phone: 818.547.0800
Fax: 323.417.3200
philiphomseyesq@yahoo.com

Disclaimer: These lists and items are NOT intended to replace legal oraccounting advice, advocacy, or review. Each party to a purchase or sale transaction should retain independent legal, taxation and accounting advice.

Introduction

The Following material is a resource guide to assist an owner, who is contemplating selling his or her practice or one, who is contemplating buying a practice. As a resource guide it is not exclusive or all inclusive. That is, in any given transaction there may be additional issues to be considered and or other documents needed. Not all transactions will involve each of the issues discussed below and not all of transactions will require each of the documents discussed below. Additionally, it is not necessary or even expected that an owner will have ready access to all of the required information or documents. Much of the information and documents will be gathered with the assistance of your professional advisors including your Broker, CPA and Attorney. These essential advisors are necessary to the successful conclusion of any such transaction. The earlier in the process you can involve them the more they can be of service in identifying the relevant issues, which need to be addressed and the documents, which will be required in your particular transaction. However, the presenters hope that the following material will give you an advantage in knowing the range of issues involved and the types of documents you may need in your transaction so that you will be a well informed and better prepared principal in your own transaction.

Table of Contents

Terms and Definitions

Accounts Payable
Tracks money owed to others. Accounts payable flows to the liabilities section of the Balance Sheet.

Accounts Receivable
Tracks money owed by customers. Accounts receivable accounts flow to the assets section of the Balance Sheet.

Accrual Basis
The method of accounting that records income at the time of sale and expenses when they are incurred.

Actual Cash Cost
The actual amount paid by the owner/seller at the time the asset was acquired.

Adjusted Earnings (Seller's Discretionary Cash Flow)
This is a computed number representing the result of adjusting the expenses of a given period to exclude one-time or non-reoccurring expenses, owner perks and benefits, and other non-essential expenses. The amount reflects earnings above and beyond fair market compensation paid to the owner/buyer as an employee or provider of clinical services and manager of the practice.

Amortization
Payment of debt in multiple installments that include amounts of principle and interest.

Appraised Value
An opinion of value, based on an appraiser's knowledge, experience, and analysis of the property.

Assessment
The process of placing a value on an asset for the purpose of taxation. Also refers to the tax itself. Also called property assessment.

Asset
Resource owned by a business. Examples include cash, inventory, and equipment.

Asset Purchase Agreement
This is the basic sales agreement, whereby the Seller is selling the assets of the practice to the Buyer. It is distinguished from the Stock Purchase Agreement, whereby the Buyer is purchasing the Corporation, which owns the practice rather than purchasing the assets from the Corporation. Stock Purchase Agreements are generally used where there is a partial sale of the practice to an associate. In this context the Stock Purchase Agreement also involves a Shareholders' Agreement usually in one document called the "Stock Purchase and Shareholders' Agreement". The Shareholders Agreement portion contains all of the terms relevant to operating the practice after the sale including the Buy Sell provisions, management provisions, distribution of profits and losses provisions, and control issues, such are requiring a "Super Majority" Vote as to certain issues.

Assumption
The taking over of an obligation or liability from another party.

Available Cash Flow
The measure of surplus income generated from the practice's normal operations, after all costs are accounted for including owner's fair compensation. Sometimes defined as Adjusted Earnings.

Balance Sheet
The Balance Sheet is a statement detailing what a company owns (assets) and claims against the company (liabilities and owners' equity) on a particular date.

Book Value
A company's common stock equity as it appears on a balance sheet, equal to total assets minus liabilities, preferred stock, and intangible assets such as goodwill. Also, the value of an asset as it appears on a balance sheet, equal to cost minus accumulated depreciation.

Buy Sell Provisions
These are the provisions contained in your Partnership Agreement (if you are a partnership) Shareholders Agreement (if you are a corporation) or Operating Agreement if you are a Limited Liability Company (LLC). They include what happens to the stock of a shareholder (partner), who dies, becomes incapacitated, voluntarily withdraws or has his or her employment agreement terminated for good cause, files bankruptcy, looses his or her interest in the practice to a spouse in a divorce proceeding. Generally, any of these events trigger the right and in some instances the obligation of the Corporation (Partnership, LLC) or remaining Shareholders (Partners, Members) to purchase that party's ownership and the terms of that purchase.

Capitalizing
a valuation process which converts a single period income stream into a determination of value by dividing the income stream by an appropriate rate of return considering the risks associated with the investment.

Cash Basis
A bookkeeping method recognizing income or expenses at the time you actually receive a payment or pay a bill.

Contingencies
These are the conditions that must occur before the transaction closes. The most common contingencies are financing contingencies. The deal can't close if the Buyer can't get the financing. But there are a number of other contingencies such as Landlord's consent to transferring the lease, payment of certain debts, releases by prior lenders, contingencies relating to the condition of the practice at the time of closing and due diligence contingencies.

Cost of Goods Sold
The cost of goods and materials held in inventory and then sold. These accounts flow to the cost of goods sold section of the Profit and Loss Statement.

Covenant not to Compete (CNC)
This is a provision in your purchase contract that prevents one party (Seller) from competing with the other (Buyer). They are also used as part of the Buy Sell provisions of the Shareholder's Agreement and or Partnership Agreement. The covenants generally define a geographic area and a time restriction (such as 15 miles for 5 years) within which the covenanting party cannot work in or own a practice. States laws vary as to the enforcement of covenants not to compete. Just about every state will enforce them to some extent. In some states it is illegal to put them in an employment agreement. These are very important agreements, a must for a Buyer, but they can be complex so you need to consult your Attorney as to it's proper contents and the enforcement provisions in your state.

Depreciation
(Accounting) – Allocating the cost of an asset over its estimated useful life.
(Appraisal) – A charge against the reproduction cost (new) of an asset for the estimated wear and obsolescence. Depreciation may be physical, functional or environmental. It represents a non-cash expense of the practice and is added back to the net cashflow when establishing the earnings amount.

Discounting
A valuation process which converts a multi-period series of future income streams into a determination of value by bringing them to present value at an appropriate rate of return considering the risks associated with the investment.

Due Diligence
Due Diligence is defined as the investigation that a prudent buyer and prudent seller will undertake for their own protection before entering into a transaction. Every principal to the transaction is responsible to conduct his or her own due diligence, including investigating and evaluating the attributes and physical condition of the land, building, legal title issues, building and safety issues, permits, location and all issues pertaining to the financial condition of the practice, management (including employment) of the practice, the market place, demographic studies, environmental issues, zoning, CUP restrictions, value or stability and or growth potential of the goodwill, physical condition or fitness for use of any of the personal property including inventory, supplies, furniture, equipment, tools, or tenant improvements used in the practice, suitability of the economic terms of any loans acquired or made by a principal. It is extremely important to know what due diligence you, as a prudent buyer or seller, should conduct. Do not assume that someone else is conducting this on your behalf. Be clear in your agreement with your Lender, Broker, CPA and Attorney as to who is going to conduct what due diligence. For instance, some Buyers mistakenly believe that the presence of an appraisal satisfies the financial due diligence. This is not true. The appraisal relies on the information given to the appraiser by the owner. The appraiser does not otherwise audit or verify the information given to him or her. As part of the Buyer's due diligence Buyer needs to verify the financial information with original source documentation. This should be included in the Purchase Agreement. Thus in fact, in this case Buyer needs to discuss this with the CPA and the Attorney and come to an agreement on how this will be handled. The CPA will identify the financial documents needed. The Attorney will build this into the Purchase Agreement as a contingency to the closing. The Broker may be the person, who actually physically delivers the financial documents to the CPA for review.

Excess Earnings
That amount of anticipated economic benefits that exceed an appropriate rate of return on the value of a selected asset base (often net tangible assets) use to generate those anticipated economic benefits.

Excess Earnings Method
Excess Earnings Method determines the business value by summing the net tangible value of the business assets with the capitalized value of the "excess" earnings.

Expenses
Operating expenses other than cost of goods sold such as rent and utilities. Expenses flow to the expense section of the Profit and Loss Statement.

Fair Market Value
The price, expressed in terms of cash equivalents, which a property would be agreed upon between a willing and informed buyer and a willing and informed seller, acting at arm's length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of all relevant facts.

Financial Statements
Reports that summarize a firm's accounting data and indicate it's financial condition. The four basic financial statements are: the balance sheet, income statement, statement of retained earnings, and statement of changes in financial position.

Financial Statements-Adjusted (Normalized Financial Statements)
It is important to understand the need to make adjustments to the financial statements to identify the true profitability of the practice. Expenses in a practice fall into three general categories, necessary and ongoing, one-time or discretionary, and personal items of the owner expensed through the business. This process of adjusting the financial statements to show the true profitability of the practice is the most time consuming portion of any appraisal, and the correctness of the adjustments the most critical to the accuracy of the appraisal.

Fixed Asset
Assets that are not likely to be turned into cash within one year and includes furniture, fixtures, and computer equipment. Fixed assets flow to the assets section of the Balance Sheet.

Goodwill
The value of the name and reputation of a person or company, which will generate future earnings, based on that reputation and established or recognized marketplace presence. Goodwill has the following characteristics: Goodwill is an intangible asset, which does not usually appear on a businesses balance sheet. Intangible property, which can be defined as the capitalization of expected earnings over and above time spent as an employed staff veterinarian. Goodwill is created only with time. Goodwill may include the following elements: (Goodwill of location, Goodwill of product or service (quality, reputation, etc.),General business goodwill)

Going Concern Value
The value of a business enterprise that is expected to continue to operate into the future. The intangible elements of Going Concern Value result from factors such as having a trained staff, operational facility, and all necessary equipment, inventory, materials, supplies and procedures in place.

Income Approach or Capitalization of Earnings
The Income Approach is a technique that takes into consideration the adjusted cashflow or profit multiplied by a rate of return or factor.

Intangible Assets
Intangible assets are nonphysical valuables, such as contracts or mortgages, employee loyalty or customer goodwill. The most significant intangible asset is economic goodwill. It is usually the single largest component of the valuation in most profitable businesses, far exceeding the tangible asset value. When something is intangible it is defined by the following: 1. Something that cannot be touched. 2. That which cannot be easily defined, grasped or formulated.
3. Without material body or substance.

Income Statement
The Income Statement shows a firm's revenues and expenses, and taxes associated with those expenses for some financial period.

Investment Value
Value to a specific individual based on the needs and conditions of that individual's finite set of circumstances.

Liabilities
Amounts owed to others. Examples include accounts payable, credit card debt, and loans.

Limited Liability Company (LLC)
A limited liability company is recognized by the State, in which it is created, as separate legal entity much the same as a Corporation. Some states (ie. California) do not allow professionals including Veterinarians to practice as a LLC. In the states that do allow veterinarians to practice as a LLC there are certain restrictions and definitely tax consequences to be considered in deciding to form a LLC to own a veterinary practice. Additionally, LLC's are a relatively new entity structure in the United States, compared to Corporations. Discuss with your Attorney whether an LLC meets your liability needs in addition to consulting your CPA about its tax ramifications.

Opportunity Costs
When assets like equipment are purchased for a practice, it is not only a purchase, but also an investment. Since these funds could be used elsewhere as an investment, there is an expected return on such funds and the necessity to account for loss of residual value of the investment. Current money investments are yielding in the vicinity of 3-7%. Professional medical practices typically consider 5% adequate for short term tangible assets and 10-12% for long term assets, and those amounts are commonly used for the purposes of the appraisal estimate, to arrive at an opportunity cost for the tangible valuation estimate.

Replacement Cost
Valuation of property according to the cost of replacing it with property of a like kind and quality; the cost to replace property at its current price with no deduction for depreciation.

Rules of Thumb
Shortcuts or formulas, including “guesstimates” used to determine a number or value. None of which are accurate or exact in nature.

Sales Comparison Method (Comparables)
Method of appraising property, especially real estate, based on a market comparison of neighboring properties having similar characteristics to ascertain what it could cost to substitute a similar property for the current one. Although this is not an absolute method to establish fair market value, the theory of process is understood by most buyers and sellers of veterinary practices.

Stock Purchase Agreement
Stock Purchase Agreements are generally used where there is sale of part or all of the stock of a Corporation. It is commonly used in a partial sale of the practice to an associate. In this context the Stock Purchase Agreement also involves a Shareholders’ Agreement usually in one document called the “Stock Purchase and Shareholders’ Agreement”. The Shareholders Agreement portion contains all of the terms relevant to operating the practice after the sale including the Buy Sell provisions, management provisions, distribution of profits and losses provisions, and control issues, such are requiring a “Super Majority” Vote as to certain issues.

Tangible Assets
Anything that has physical substance and form. It would include such items as real estate, medical equipment, drugs and supplies, and personal property.

Terms of Sale
The amount of down payment, tax allocation, and interest rate can increase or decrease the number of qualified purchasers and the sale price. Terms can include such items as interest rates, repayment time periods and transition costs. Post sale tax implications continue to be a major determining factor on the terms acceptable to sellers.

Transferability
The likelihood that the change of possession of an asset from one person to another will experience the least loss of its original characteristics. Specifically important to practice valuations is the transferability of goodwill from seller to buyer.

Valuation Process
A valuation is the estimated worth of a property as determined through an appraisal or analysis, rendered by a competent professional. The valuation must be based on real and truthful information, and is only as good as that information from which it is based. Since every veterinary practice is unique, there are certain basic steps in the valuation process, and a series of refinement steps. There are many variables which must be taken into consideration during the process of the valuation.

Warranties and Representations
These are a very important part of any transaction for the sale of a practice. They are clauses that define what either party is “promising” to the other. It will limit what the Buyer or Seller is relying upon in terms of records, statements by buyer or seller, disclosures, and other information, etc. They may limit and or extend the Seller’s or Buyer’s liability beyond that which the law would other wise impose.

Worth
A personal opinion of value based on a person’s belief systems, personality, and experience as an individual within the context of the item under consideration.

Seller's Checklist for a Practice Sale; *from Decision to Closing*

Read the following "steps" checklist to get a general overview of the sale process. Additionally its recommended that a more detailed and sale-type specific checklist be consulted for further information.

- ❑ Decision:
  Deciding if and when to sell a practice is one of the most important decisions a veterinarian will make. It should be made only after careful consideration, with input from legal and business advisors, reinforced by close friends and family.

- ❑ Establish a Fair Market Value:
  It is very important to have the fair market value of your practice determined. Fair market value is defined as "the cash or cash equivalent price at which a business or practice would change hands between a market buyer and a seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of the relevant facts and the practice having been exposed to the market for a reasonable length of time." This is best done by a professional appraiser for several reasons. The professional appraisal will add credibility and authority to your asking price, as well as provide supporting data for the potential buyer to aid in obtaining financing. Proper pricing cannot be overemphasized. An under priced practice is of course unfair to the seller, but so is an over priced one which risks unfairness to the buyer or becoming 'shopworn' on the market.

- ❑ Review Tax Implications:
  Once your practice valuation is complete, you will need to discuss the post-sale tax implications with your CPA. You want to be sure that the money after taxes you will be receiving from the sale is what you need and expect. The last thing you want is to get to the closing table and not have enough money to do what you want to do.

- ❑ Review Sale Proceeds Strategy:
  Once you and your CPA have determined the post-sale tax implications consult your investment or retirement planning advisor. Use a plan to direct the post-sale funds rather than simply dropping a check in your planner's lap last minute. If your plan involves the use of a 1031 exchange for a real estate sale, discuss and select a qualified 1031 exchange intermediary.

- ❑ Prepare Information Packet for Potential Buyers:
  When a buyer shows interest in your practice you will need to have an extensive packet of information ready. This packet should include a brief practice history, reason for selling, a description and pictures of your facility, community and equipment, a description of the services provided, demographic information of your area, community information and web links to law enforcement and school system websites, a list of the current staff along with their positions and salaries, as well as bios on key staff members, an extensive equipment list, estimated consumable inventory value, financial data to include tax returns, corresponding financial

statements, most recent balance sheet, a breakdown of the income by category (vaccination, surgery, radiology), an estimated after-debt cashflow analysis, an expected post-sale buyer income analysis, explanation of any growth or decline trends, the practice and real estate price, the appraisals to support the prices, lease agreements and assignment paperwork for any equipment or real property, and descriptions of opportunities for a new owner. The packet should look sharp, be easy to read and present the information in an organized manner.

- ❑ Prepare a Marketing Plan

  Decide how and where to best advertise your practice. Minimally, you should place an ad in your local and state association newsletters. You also might want to consider national ads, websites, convention postings, or even a direct mail letter if you want to be aggressive. If confidentiality is a requirement, you will need to create and use a non-disclosure form for inquiring buyers.

- ❑ Pre-Qualify Practice with Lenders:

  Contact a few practice acquisition lenders and ask them if you can pre-qualify your practice. This will shorten the time needed to get to closing once a buyer has come forward. Be sure to investigate with your advisors the basics of the acceptable terms for owner financing. At least partial owner financing is often required, and can be a good elective choice for post-sale income and tax deferment strategies.

- ❑ Prepare Additional Support Data:

  Often, additional information will be required by the commercial lender, and the buyer and the buyer's advisors. Become familiar with your practice computer system so that additional reports can be created, and be willing to assist the buyer with obtaining information from municipal and regulatory agencies, zoning boards, and licensing agencies. Additional documents may be required of your appraisers, accountant and attorney throughout the process.

- ❑ Locate a Buyer and Settle on a Price:

  Once a buyer makes an offer then you must negotiate a price and terms that will work for both buyer and seller. Strive for a win-win with each party getting most, but not likely all of what they want. The actual sale price is only one term that must be agreed upon. All parties must agree on all other terms and conditions including warranties and representations by both parties, contingencies (most important of these is the Seller's and Buyer's opportunity, terms and conditions upon which to complete their respective "Due Diligence", any owner financing terms, the inventory counting and value process, accounts receivables and payables, components of the purchase agreement(s), closing date, responsibility for associated closing costs, non-compete agreements, transition period and plan, and allocations of purchase price, employment and employee issues, including accrued benefits, employee retention and other HR issues to name a few. All of your advisors should be in the loop at this point including your broker, CPA and Attorney. Once you have made a firm commitment to the Buyer it is often too late to renegotiate a substantive term. Seek the input of each professional before making a firm commitment to the Buyer.

- <u>Obtain Financing:</u>
  This can be the most frustrating part of your whole ordeal. Once you have a basic agreement, the buyer needs to approach a lender or lenders to obtain financing. You will need to assist the buyer by providing the lender with any of the information needed and be prepared to explain and defend your stated profitability. You will likely need to engage your appraiser and CPA in the explanatory process. Note: More often than not, veterinary specialty lenders are more successful at approving veterinary acquisition loans than the local hometown bank. They understand cashflow lending, and have the experience and expertise to analyze a veterinary transaction.

- <u>Final Contract:</u>
  Once everything has been agreed upon, it is time to get all the agreements in writing, via the "Final Contract". Here, an attorney is a must. Once an attorney has drawn up the agreement you will also need to have your CPA, and other advisors, review the contract until all parties are satisfied. The buyer will be doing the same, so expect a number of revisions.

- <u>Satisfy All Contingencies in the Contract:</u>
  All the contingencies of the contract must be met in order for the contract to be valid. Contingencies might include obtaining or completing financing, completion of a non-compete agreement, property and equipment inspections, lease agreement transfers, property title and taxation related tasks.

- <u>Contact Title and/or Escrow Company:</u>
  If the sale includes real estate, then a title company will need to draw up a commitment of title insurance. They will also set the closing date and be the third party to handle the escrow money and draw up a settlement statement. East coast closings are typically handled by attorneys and west coast closings handled by escrow or title companies. An escrow company can also be invaluable in doing title searches for tax liens and other liens against the practice as part of Buyer's due diligence and to record the Personal Property Security Instruments ("UCC-1 Financing Statement") on behalf of the Lender and/or Seller. Check your local area for the process used.

- <u>Inform Staff:</u>
  Some owners like to have their staff in on the sale from the very beginning, while others do not want to worry them unnecessarily until the deal is a sure thing. Regardless on when you believe the staff should be informed, you need to do it. It is best to include the new owner in the announcement. It is also a good idea for the new owner to send some goodies to the clinic, have a combined staff dinner expressing the buyer's interest in working with them.

- Tie Up All Loose Ends:

  Go over all of the small details. Make sure the loan is on track, confirm the buyer has all needed insurance and loan contingency documents submitted, ensure the lender's survey and real estate appraisals are scheduled and then completed, confirm the closing date and time, notify all venders and utility companies of the ownership transfer, review the settlement statement for errors, review the inspections with the buyer, and confirm the inventory amount and equipment operational status with the buyer prior to closing. (see pre-closing checklist)

- Closing

  Go to the closing or complete documents remotely via overnight courier. Be flexible, the closing date is a target date not a guarantee. Murphy's Law is always active, especially if there is outside financing involved. It is important to stay in constant contact with the Lender's Closing Department (this is separate from the Lender's Loan Agent) It is the Closing Department, who will be asking for last minute items such as copies of Seller's Trust, Business License, documents and resolutions relating to any entities involved such as corporate By Laws, Resolutions, proof of Buyer's insurance coverage, executed copies of the Purchase Agreement(s), lease assignments, etc… These items can delay the funding, which will delay the closing. These are critical functions your Broker, Escrow and Title Agents, and your Attorney can assist with or perform for you.

Practice Appraisal – (Needed Documents) Checklist

Financial

1. Tax returns filed for the prior three years
   a) If sole proprietor, Form Schedule C, with all relevant attached schedules, including depreciation schedules
   b) If C Corporation, Form 1120, with all other attached forms and schedules, including depreciation schedules
   c) If S Corporation, Form 1120S, with all other attached forms and schedules, including depreciation schedules
   d) If Partnership, Form 1065, with all other attached forms and schedules, including depreciation schedules
2. Financial statements for the same prior three years as above
3. Interim financial statements for the current year
4. Details on all existing loans and leases of the seller, whether you will be assuming them or not. Original loan date, term, interest rate, and, if a lease, buy-out information.
5. Copies of prior year W-2s for all employees (including owners if paid as an employee) and 1099s, including relief veterinarians or any contractual service providers.
6. Current year payroll register, showing employee name, hourly wage or salary, date of hire, wages paid year-to-date, and position.
7. Employee and Owner benefits schedule
8. Revenue reports from veterinary software for prior three years, summarizing the following information:
   a) Breakdown of gross revenues, subtotaled by revenue or service code. For example, office visits, lab, anesthesia, surgery, etc.
   b) Breakdown of gross revenues, subtotaled by doctors
   c) Rate per patient, by month
   d) Gross collections, by month
   e) Number of clients seen, by month
   f) Number of new clients seen, by month
   g) Number of procedures done, per year

Operational

9. Copy of existing leases on premises and/or equipment
10. Copy of fee schedule
11. List of assets being purchased
12. Estimation of value of inventory on hand
13. Copy of employment contracts with associate veterinarians
14. List of all operational and/or management manuals present
15. Floor plan and photos of the facility and equipment
16. Copies of any recent premises or practice appraisals

Seller's "To Do" List – Pre-Post Closing

Use this list during the last month prior to closing to ensure you catch the little things.

PRE-Closing

1. Controlled Substance Transfer form— You may need to call the DEA, this form is not always available on the website. The form must be filled out and sent back immediately. This can only be done by the veterinarian under which the drugs were originally obtained. (you will need to have your DEA license number and mailing address ready when you call).
2. Review inventory again within 48 hours of closing. Review adjustment plan based on contract specifications.
3. Schedule time to change/transfer services and utilities including telephone, trash, alarm monitoring.
4. Credit card machine- If leased: terminate lease, transfer lease or return machine based on machine contract.
5. Notify Vendors to either close accounts, or at least request a password or identify a specific party as the only ones authorized to make future orders. It's not unusual for a couple of orders to be mistakenly place on your account after closing if the account remains open. Simply take the invoice to the buyer, or have the vendor move the charges to the correct account. If you perceive a potential problem, include a statement requiring cooperation of the buyer in your purchase agreement.
6. Contact the Veterinary Medical Board and ensure the premises permit has been issued in the new buyer's name. This is especially important for those that own but will be now leasing the building.
7. If you are financing part or all of the transaction or leasing the property to the buyer, request a copy of the building hazard and general liability insurance policy issued to the buyer showing current coverage. If you have required life and disability coverage for carry back loans now is a good time to ensure the buyer has coverage in place.
8. Fulfill all obligations with employees: pay, vacation, sick leave. Once you leave the practice, you cannot monitor safety and behavior. Make sure your responsibilities are completed.
9. Keep your professional liability insurance in force. If you are retiring, drop it to a lower level if desired, but do not cancel it for at least 1 year following the sale.
10. Review final drafts of the Escrow/Title paperwork one week before closing to ensure accuracy and enough time to make corrections. Provide all pro rated items to escrow (rents, property taxes, utilities, other pre-paid expenses).

POST-Closing

Ensure your buyer has completed the following:

1. Payroll obligations with employees and payroll service completed

2. Buyer’s applicable business license and premises permit is in place
3. Fictitious Name Abandonment completed
4. All applicable final paperwork filed with Sales Tax and Employment Boards
5. Merchant and Vendor accounts closed, or deactivated
6. Utilities transferred
7. Copy of final contracts and settlement statements (HUD) to seller’s attorney and CPA

Partial-Sale to Associate Checklist

1) Establish timeline—__/__/__closing date
2) Review sale structure and tax consequences with individual personal tax accountants and attorney (will this be a shareholder sale or Corporation to issue additional shares?)
3) What is tax year-end for the new business entity? 12/31/___??
4) Consult with your Accountant and Attorney to select entity structure: Partnership, LLC, Corporation, etc.
5) Must reach agreement on
   a) Price agreement for __% of practice. Who has to have first right of refusal for remainder of practice?
   b) Buy Sell Provisions including first right of refusal for remainder of practice?
   c) Commitment, if any, and Time Table for selling additional shares
   d) Provisions for bringing in additional owners in the future
   e) Management and control issues (super majority voting requirements)
   f) Provisions relating to the distribution of profits (reserves, owners' salaries, benefits, etc.)
   g) Terms if owner financed.
   h) How will real estate be handled(is sale of real estate part of the deal, if not, option to buy in the future, first right of refusal, etc.)
   i) Real estate lease--rent appraisal to be done to help establish rent value (beware, a change in the rent amount will affect the valuation of the practice, so it must be consistent with the appraisal of the practice)
   j) Equipment and inventory values—issue in formation, but not in sale—reasonable value to be determined between parties
   k) Term of non-compete covenant
   l) Schedule and Confirm Closing date—__/__/__
   m) Closing costs—split?
   n) Allocations of purchase price—a tax question to be negotiated between parties
   o) Future compensation methodology—salary for each—need to set—will include management and medical/surgical work—can be adjusted if significant changes in time put into practice occur (must be consistent with Distribution of Profits provisions of the Partnership/Shareholder's Agreement)
6) Financing
   a) Acquisition lenders
   b) Owner financing—may be essential for some purchases
   c) Personal savings and verification of funds
7) Draft documents
   a) Stock Purchase and Shareholders' Agreement including Buy Sell provisions (if entity is a Corporation)
   b) Asset Purchase and Partnership Agreement including Buy Sell provisions (if entity is a Partnership)
   c) Promissory Note and Security Instruments (if seller financed)

   d) LLC or Corporation documents (including By Laws and various entity Resolutions authorizing the transaction)
   e) Non-compete agreement
   f) Confidentiality agreement
   g) Employment Agreements for all owners (and non-owners)
   h) Personal Guarantees, if any
8) Determine which assets & liabilities will transfer with sale - obtain a detailed list
9) Equipment and inventory count should be done near sale date if purchase price is to be adjusted—needed for entity formation
10) Loan requirements--practice purchase only at this time
11) Need transfer of
   a) Computer software license
   b) Telephone number and account
   c) Utility accounts
   d) Answering service
12) Transfer of financial and accounting records
   a) Location, condition, availability of old records
   b) Need current equipment lists (tax and actual)
13) Review past tax returns
   a) Corporation if other than Sole Proprietor (1040 Schedule C)
   b) Form 941, Form 940, Unemployment report returns
   c) State franchise tax returns
   d) Sales tax
   e) W2s and W3
   f) 1099s and 1096
14) Buyer needs to establish
   a) SUI account—transfer of experience rating?
   b) State sales tax account
   c) Franchise or state income tax account
   d) New tax ID number
   e) Vendor accounts
   f) DVM license for state practicing in
   g) Radiology license
   h) State controlled substance license
   i) Change address on DEA license
   j) Local banking relationships
   k) Credit card merchant accounts
15) Insurance needs
   a) Transfer PLIT
   b) Business overhead
   c) Employee acts
   d) Workers comp (optional in Texas, but highly recommended)—transfer of experience rating?
   e) Commercial package
   f) Life insurance for buy/sell
16) Lease

    a) Insurance and other requirements of lease
17) Order initial inventory if needed
18) Review and transfer any agreements practice has entered into
    a) Service agreement
    b) Equipment rental agreements
    c) Loans to practice
    d) Loans from practice
    e) Payroll service
    f) Employment
19) Obtain payroll records from practice if buying corporation/obtain and file new forms if business entity changes
    a) W4
    b) I9
    c) Texas New Hire reporting
20) Notify city/county about previously paid property tax
21) Preparation of partial year financial statements for each party
22) Termination/transfer of benefit plans
23) Identify and discuss contingencies
    a) Environmental issues
    b) Past due taxes
    c) OSHA
    d) Pending or potential lawsuits
    e) Accounting methodology for tax purposes
24) Operations issues
    a) Accounting software/system and personnel
    b) Who does payroll—when due next
    c) Any work done for hospital for free?
    d) Hospital forms and flow of operations

Supporting Documents Needed For a Sale

You will want to have certain documents, reports, and other items accessible during the sale process. Assembling, or at least knowing where they are, can make accessing them much less stressful during the sale process. Being able to produce and deliver items quickly upon request instills confidence in the buyer and the buyer's advisors that you are prepared and organized.

1. Copies of certificate/articles of incorporation (organization), by-laws, and shareholder/partnership/owner employment/operating agreements. Review, and make sure you have consent of anyone with an ownership right or interest

2. All minutes of meetings of the board of directors (or other similar governing body) and written consents of the board (or similar governing body), stockholders, partners or members of the practice

3. All buy-sell or other agreements to which the practice or its owners are subject relating to the purchase, sale, voting or other related activities of its stock or interests or asset. Is there a first right of refusal in place? Be sure to clear any of these contingences well in advance, and in writing.

4. All reports filed with any state authority by the practice (e.g. annual reports, etc.) for the last three years

5. All reports and applications filed with, significant correspondence with, and transcripts of any significant proceedings before, any state or federal regulatory agencies and self regulatory authorities, including, without limitation, the EPA, EEOC, DEA, applicable state department of human rights or workforce issues, OSHA, state veterinary board. Any letters documenting correction or clearance of a previous infraction or violation.

6. All federal and state income tax returns filed by the practice for the most recent period and as far back as readily available (at least three years), all communications between the practice and the Internal Revenue Service, including notices of assessment and reports of revenue agents, with respect to matters raised by the IRS in the course of any audits

7. Most recent year's property tax (real, personal and intangible) and returns or invoices

8. Copies of all current federal, state and local business permits and licenses, qualifications and all correspondence relating to such permits or licenses for the practice including all information regarding any actual, pending or threatened suspension or termination of such permits, licenses or qualifications

9. Copies of all current federal, state and local veterinary licenses, drug enforcement authority licenses, and any other permits or licenses for equipment, supplies, materials or drug use, for all veterinarians employed by the practice and all veterinarians contracting with the practice and any information regarding any actual, pending or threatened suspension or termination of such licenses or qualifications.

10. All federal and state payroll tax returns filed by the practice for the most recent period and as far back as readily available (at least three years), all communications between the practice and the Internal Revenue Service or state taxing authority, including notices of assessment and reports of revenue agents, with respect to matters raised in the course of any audits

11. All state sales tax returns filed by the practice for the most recent period and as far back as readily available (at least three years), all communications between the practice and the state taxing authority, including notices of assessment and reports of revenue agents, with respect to matters raised in the course of any audits

12. Copies of all W2s, W3s, 1099s, and 1096s filed by the practice for the most recent period and as far back as readily available (at least three years) as well as all communications between the practice, the IRS and the Social Security Administration regarding related matters

13. All documents and agreements (including amendments) regarding any financing, merger, sale, lease (property and equipment), sale and leaseback, loan or other transaction to which the practice was a party together, with any related "closing binders" or collations of documents and related "due diligence memoranda."

14. All documents and agreements (third party or inter/intra-company) evidencing borrowings, whether secured or unsecured, by the practice, including loan and credit agreements, promissory notes and other evidences of indebtedness and all guarantees.

15. All letters or agreements confirming or terminating any Practice lines of credit and any Practice letters of credit.

16. All correspondence with lenders of the Practice, including all compliance reports submitted by the Practice or its independent public accountants.

17. All results from any UCC searches undertaken by the Practice.

18. Income statement, balance sheet, notes and accountants’ report for the practice prepared by the practice’s certified public accountants for the past three years

19. Year-to-date income statement and balance sheet for the current year

20. Trial balance and general ledger for the past three years as well as year-to-date for the current year (a QuickBooks disk covering this period may be submitted in lieu of hard copies of the documents

21. Bank statements, with accompanying bank reconciliation

22. Aged accounts receivable trial balance as of the most recent accounting year-end and the most recent month-end

23. Analysis of prepaid or deferred expenses (if applicable)

24. Listing of all fixed assets (i.e. equipment, furniture, fixtures, etc.), including original cost, accumulated depreciation, net book value, location and serial numbers (if readily available)

25. Listing of open accounts payable items/invoices

26. Copies of the most recent three (3) months statements for credit cards in the practice's name and merchant services in respect of the practice

27. Revenue breakdown reports by month for the most recent accounting year and by service type for the most recent accounting year

28. A schedule of partner, executive and key employee compensation

29. Description of significant accounting policies and changes in these policies

30. Summary of unusual or non-recurring items affecting the operating results

31. Details of any uncompleted purchase orders for materials or services

32. All invoices, day sheets, appointment books, PMS computer reports or other documents supporting the revenue and expenses reported on the practice's tax returns for the past five years

33. Financial and operating projections for the next five years

34. Budgets or business plans prepared for the practice during the past five years

35. Dollar amount and list of current inventory on hand

36. List copies of all software maintenance contracts used in connection with the operations of the practice

37. All documents relating to any receivables from or payables to partners, directors, members, officers or owners of more than five percent of the practice during the past five years

38. All personnel policies and procedure manuals, including employee handbook, safety manual and new employee orientation material

39. All documents relating to both current and previously terminated employees bonus, retirement, profit sharing, incentive compensation, deferred compensation, stock option, stock purchase, pension and other employee benefit plans or agreements of the practice or other funds, programs or arrangements maintained for the benefit of employees, including any 401(k) program

40. List of all loans or other arrangements (including guaranty and indemnification arrangements) between the practice and its employees

41. All documentation relating to disciplinary action and the termination of any employees during the last three years

42. List of all Workers' Compensation and unemployment compensation claims alleged against the practice in the last five years

43. Names of all employees bound by non-compete agreements and copies of such agreements

44. Copies of all charges or complaints against the practice filed with or by any state or federal court or governmental agency dealing with any form of employment or employment discrimination matter within the past two years

45. All employee personnel files including, all Employment Agreements, W4s, I9s, and state new hire reporting documents together with current payroll information, including a copy of the last payroll run; a report of the payroll year-to-date by class code (i.e. totals for veterinary and for non-veterinary employees);

46. Any environmental audits or other reports relating to the properties owned or occupied by the practice at any time, not otherwise provided.

47. Copies of the most recent utility bills (gas, electric, telephone, water, sewer)

48. Describe any environmental, business, or regulatory liabilities of the practice

Adjusted Earnings – Adjusted Cashflow Worksheet

It is important to understand the need to make adjustments to the financial statements to identify the true profitability of the practice. Expenses in a practice fall into three general categories, necessary and ongoing, one-time or discretionary, and personal items of the owner expensed through the business. Each of the reported example expenses were reviewed to find the non-essential, non-reoccurring and personal items. These were removed resulting in a new "adjusted earnings" number. This number more clearly represents the true profit generated by the operation of the business.

Task: Create a similar table for your practice (next page). Adjust similarly and track your change in adjusted earnings over time. You should strive for an increase in adjusted earnings, along with any increase in gross revenue. Do not misinterpret increasing revenues as a sign of corresponding increasing profitability and corresponding increased value.

EXAMPLE PRACTICE		**As Reported**	**As Adjusted**	
GROSS INCOME		**$ 500,000**	**$ 500,000**	
income from:	services	$ 450,000	$ 450,000	
income from:	inventory	$ 50,000	$ 50,000	
EXPENSES				
Salaries and Wages		$ 100,000	$ 120,000	spouse was an unpaid receptionist
Repairs and Maintenance		$ 50,000	$ 27,000	new flooring and HVAC this year
Rent – Building		$ -	$ 30,000	fair market rent rate adjustment
Taxes		$ 12,000	$ 13,200	includes payroll taxes for new hire
Insurance		$ 1,500	$ 1,500	
Interest		$ 4,500	$ -	current owner's debt expense
Depreciation		$ 5,500	$ -	non-cash expense
Advertising		$ 1,350	$ 1,350	
Pension Plans		$ 10,000	$ 2,000	remove owner's portion
Employee Benefits		$ 14,600	$ 4,600	remove owner's health insurance
Auto		$ 6,200	$ -	non-essential personal vehicle
Entertainment		$ 5,000	$ 200	remove non-practice expenses
Seminars & Education		$ 6,500	$ 1,500	remove Hawaii Vacation/CE trip
Supplies				
	Medical	$ 90,000	$ 90,000	
	Office	$ 10,000	$ 8,000	remove personal home computer
Outside Services		$ 8,000	$ 8,000	
Bank Fees		$ 4,500	$ 4,500	
Utilities		$ 7,500	$ 6,800	remove home cable tv
Owner's Compensation				
22% of production as a	DVM	$ 99,000	$ 99,000	
2-3% of Gross as a	Manager	$ 10,000	$ 10,000	
Total Expenses		**$ 446,150**	**$ 427,650**	
Reported Business Net Income		**$ 53,850**	**$ 72,350**	**Appraiser's Adjusted Earnings**

All numbers contained in the table above are for discussion purposes only.

Simplified Cashflow Analysis Worksheet
Period ________to________

Adjusted Earnings/Cashflow/Business Profit: Essentially this is a computed number representing the result of adjusting the expenses of a given period to exclude one-time or non-reoccurring expenses, owner perks and benefits, and other non-essential expenses. The amount reflects earnings above and beyond fair market compensation paid to owners as providers of clinical services and leadership roles in the practice. It more accurately depicts the "net profit" of the Business Itself after all necessary expenses are satisfied. This residual amount of money left over is available to the practice owner(s) as additional take-home profit and is also utilized by a buyer for debt service of a purchase. The importance of understanding this process is for the practice owner to segregate the "collective money" received as the owner into a) the fair DVM compensation of the owner acting as a clinical doctor, b) reasonable leadership/management compensation and c) the residual profit. The residual profit is the driving force behind practice value and debt service capacity. Use this chart to analyze your general profit trends. It reflects your success in balancing expense control and revenue growth. It provides a better illustration of the business' profit, and will dramatically reduce the confusion of misinterpreting increasing gross revenues as being synonymous with increasing profitability, and/or increasing practice value.

Income – Necessary Expenses = Adjusted Earnings/Cashflow (Business Profit)

Income/Revenue (all sources)		$______________
Necessary Expenses Only[1]		
Wages and Salaries		
Staff	$________	
Associates	$________	
Owner's (fair wage)[2]	$________	
Repairs and Maintenance	$________	
Rent or Mortgage	$________	
Taxes & Licenses	$________	
Drugs and Supplies	$________	
Other Costs (Lab)	$________	
Advertising	$________	
Required Vehicle	$________	
CE & Dues	$________	
Utilities	$________	
OTHER		
__________	$________	
__________	$________	
	- Total Expenses	**$________________**
	= CASHFLOW	**$________________**

[1](EXCLUDED COSTS)

Personal Vehicles	
Travel and Entertainment	(Vacations)
Interest	(debt expenses)
Depreciation & Amortization	(non-cash expenses)
Personal perks and benefits	(non-working spouse compensation)
Personal items expensed	(golf membership)
Infrequent or non reoccurring costs	(new HVAC, flood damage repair)
Other non-essential costs	(non-working child salary)

[2] Calculate and include ONLY the fair wage for the owner(s) based on a percentage of the owners' production (20-25%), or a salary rate commensurate with an industry acceptable number, and a reasonable leadership/management stipend, usually 1-3% of gross revenues.