

# Chapter 12: Health, Education, Legal and Social Service Businesses

**This major group includes establishments primarily engaged in furnishing medical, surgical, legal advice/services, academic/technical instruction, or social services and rehabilitation services to those persons with social or personal problems requiring special services and to the handicapped and the disadvantaged.**

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## Medical Practices

**SIC: 8011 NAICS: 621111**

Establishments of licensed practitioners having the degree of M.D. and engaged in the practice of general or specialized medicine and surgery.

### Description of Business

Operations of small medical practices may offer general care, but most provide specialty services. Business is largely generated from referral services of hospitals and HMO/PPO networks that the physician may be associated with.

### General Industry Information

Offices of doctors and medical practitioners have undergone significant industry-wide changes in terms of organization. The litigious 1990s dealt a heavy blow to the medical community, which faced an increase in medical malpractice suits. In turn, insurance premiums rose to unexpected levels, thinning the margins for operators of this type. Many doctors moved away from self-employment and joined hospitals or other large providers of care. Approximately 192,000 businesses were engaged in this industry in 2002; a slight decrease from 1992 totals of 197,000.

Typically, operators of medical clinics will employ several administrative staff members. Medical assistants, secretaries, nurses, and processing staff are the key to maintaining order and functionality. Doctors who accept patients with Medicare and Medicaid typically employ an individual knowledgeable with filing requirements and billings procedures.

The \$6 billion dollar medical office industry is expected to maintain increasing revenues, due to several factors. An aging population parallels the need for

increased medical attention, while new technologies continue to provide doctors with improved methods of treatment.

**Financial Performance Ratios** **Table 12-1: Medical Practices**

Margins	
Manager/Owner Salary (% of revenue)	14-30% depending upon specialty, practice size and reputation
Operating Expenses (% of revenue)	80-92% with a median of 90%
EBITDA/Operating Margin (% of revenue)	1-3%
Ratios	
Working Capital (% of revenue)	4-10%
Current Ratio	0.3-2.0
Quick Ratio	0.5-1.7
Accounts Receivable Turnover	6-20 times
Profit & Growth	
Return on Invested Capital	1-3%
Prior Years' Annual Growth (% of revenue)	+/- 1%

 **Business Valuation Formulas** 20%-50% of annual revenues. Establishments selling prescriptions to patients may consider using a multiple on the higher end of the range.

 **Equipment Valuation and Real Estate Rental Formulas**

*Equipment*  
OLV is typically 20-30% of retail value, depending upon condition and quality.

*Real Estate*  
Rent as a % of Sales: should be 5-7% of sales. Rental spaces for these businesses tend to fall between 1,100-10,000 sq ft, with a median of 2,700 sq ft. The typical lease is a gross expense lease for secondary locations and full service gross expense lease for primary locations. Medical spaces typically have higher rents due to the significant use of utilities relative to other professional users.

 **Red Flags and Risks** This industry has several risks, due to the inherent human interests involved. Governmental regulation can affect key items, such as Medicare/Medicaid disbursements. Litigation is a lingering threat to professionals in this industry and can devastate the bottom line of a practice. If considering acquiring a medical practice, it is advised to visit the National Practitioner Data Bank, which provides background queries on the status of medical doctors. Inquiry into the history of key medical personnel should be top priority. In assessing a proper value for a medical practice, it would be useful to review the patient list. Repeat patients are a positive attribute, and often a function of office location. Further, a buyer should obtain employment agreements to determine if popular employees plan to depart prior to the acquisition. Finally, a concerned buyer should go through accounts receivables. Frequently, the complex billing processes will result in large revenues that have not been realized. As customers rely on public