Physician Practice Goodwill vs. Other Intangible Assets – Clear as Mud

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The whole physician practice acquisition era of the 1990s appears to be coming full circle. During the latter part of that decade, roll-up companies such as MedPartners and PhyCor, were aggressively buying up physician practices across the country. Today, hospitals are acquiring physician practices. Apparently there is still some merit to the idea of "let physicians practice medicine and let someone else manage the practice."

For these hospitals that are aggressively purchasing family and specialty practices, it is a way to capture new patients and ensure hospital coverage for certain specialties. The benefit for physicians is a secure salary and eliminating the headaches of practice management. This movement has created a big demand for the valuation of physician practices to comply with the Anti-kickback Statute and Stark Law.

Estimating the fair market value of a physician practice can be tricky. More specifically, the concept of goodwill and intangible value is probably one of the more misunderstood concepts related to physician practice valuations. Many professionals in the industry use the term "goodwill" and "intangible value" interchangeably; however, goodwill can be one of several intangible assets of a physician practice. Furthermore, goodwill can be either professional (physician) goodwill or enterprise goodwill. Federal healthcare laws preclude hospitals from paying for physician goodwill because it often equates to purchasing patient referrals. Therefore, healthcare attorneys and appraisers take great care in ensuring that hospitals and health systems don't overpay a physician for his professional practice.

Tangible Asset Value
- Furniture
- Fixtures
- Equipment
- Cash
- Accounts Receivable
- Other

Intangible Asset Value
- Trained Workforce in Place
- Patient Medical Records
- Phone Number
- Trade Name
- Goodwill
  - Professional
  - or
  - Enterprise

Total Practice Valuation

Goodwill and other intangible assets of a physician practice can be difficult to measure. According to the *International Glossary of Business Valuation Terms*, goodwill is defined as “that intangible asset arising as a result of name, reputation, customer loyalty, location, products and similar factors not separately identified.” As a business enterprise grows in size and scope, its goodwill transitions from personal/professional goodwill to more enterprise goodwill. In general, any intangible that is not specifically identified is commonly referred to as “professional goodwill.” Fundamentally speaking, goodwill arises when an enterprise generates earnings in excess of a normal return on assets.

In order to determine whether a physician practice has excess earnings, the analyst should first compare the physicians’ compensation and productivity to industry benchmarks to determine if the physicians are underpaid or overpaid relative to their productivity. It is common for private practices to payout a majority of their earnings in bonuses and salary, leaving very little taxable income. Salary adjustments and other owner-discretionary adjustments are often needed. In general, if a practice is not generating a significant amount of excess earnings, then there is likely no significant goodwill.

Although there may not be any real measurable goodwill, there can be some value to the other intangible assets of the practice, including (but not limited to) a trained workforce, patient medical records, IT systems in place, unique phone number, and tradename. Appraisers utilize special techniques to estimate the value of such intangible assets. Each practice is different and the specific facts and circumstances of each should be considered.