



WHAT'S NEXT FOR DENTAL AND PHYSICIAN PRACTICE MANAGEMENT?

Like every sector of the healthcare industry, dental and physician practice management companies (PPM) were hit hard by the coronavirus pandemic as patient volumes decreased and elective procedures were postponed during the spring and summer of 2020. The year-end surge in M&A volume appears to be continuing into 2021 with strong tailwinds across all sectors of the practice management industry.

TOP TRENDS IN DENTAL AND PHYSICIAN PRACTICE MANAGEMENT FOR 2020

- In the spring and summer of 2020, COVID-19 dramatically suppressed deal activity in practice management, with few lenders willing to finance aggressive M&A activity initially. The few deals that did close were either opportunistic, or required creative structures with substantial earnouts, holdbacks and seller notes (sometimes with convertible debt).
- By late summer, the pressure to invest idle cash drove significant interest in acquisitions by private equity companies. Despite this pressure, M&A activity during this time was notable for its cautious pace as lenders and representation and warranty insurance underwriters insisted on extensive due diligence and, in many cases, heavier use of earnouts, holdbacks and risk-mitigating deal structures.
- By the end of 2020, with the looming prospect of tax reform, PPM buyers and sellers rushed to close deals in a boom of M&A activity and sudden acceleration of pace in deal flow.
- COVID-19 brought to light, and accelerated, underlying trends in the industry, such as the growth in interest for home-based care and telehealth. In addition, COVID-19 revealed surprising “winners” in healthcare service segments that not only survived, but in some cases

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thrived relative to other specialties during quarantine. These “winners” include optometry, veterinary medicine and mental health counseling.

WHAT WE EXPECT IN 2021

- **Market conditions will continue to drive strong M&A activity.** Industry momentum, availability of capital and the expected re-emergence of attractive seller platforms who postponed going to market in 2020 should drive strong M&A activity in practice management in 2021. We continue to see demand for deals in traditional areas such as dental, dermatology, vision care, behavioral care, orthopedic surgery, ENT and gastroenterology.
- **Consolidators will increase their focus on acquiring other consolidators.** In spaces such as dermatology, dental and ophthalmology, we expect the larger consolidators to focus more of their M&A resources on multi-site acquisitions of competitor platforms. We expect this to continue driving high EBITDA multiples and seller-favorable deal terms. This shift in focus may reduce buyer competition for single-site practices, which in turn creates a buying opportunity for smaller (or new) private equity and family office-backed platforms.
- **Private equity is increasingly interested in specialties traditionally dominated by hospitals.** Continued reimbursement support for ASCs — and trends to move services such as cardiology outside of hospitals — could see

“2021 will be a banner year for consolidators, but one day we may see it as an inflection point from ‘get big’ to ‘get better.’ There is a hunger for new models – from risk-based contracting and concierge medicine to employee ownership – driven by macro trends in healthcare consumerism and ESG.”



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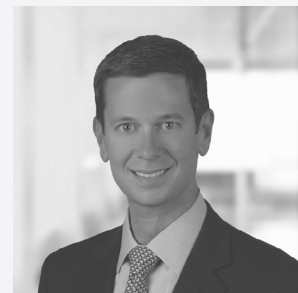
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significant growth in private equity interest relative to prior years. These changes in reimbursement, and a growing focus on cost reduction, make specialties traditionally dominated by hospitals and health systems increasingly attractive for practice management platforms.

- **Telehealth is here to stay; strategic decision-making is key.** The emergency expansion of telehealth services covered by Medicare is expected to continue under the Biden administration. We expect some tightening of the rules, but Medicare payments for telehealth are likely here to stay. PPMs that dabbled in telehealth as revenue replacement during mid-2020 will need to decide what role telehealth will play in their long term strategic plans, and whether they will compete with companies whose primary focus is on healthcare technology solutions.
- **Earnouts will continue to be an important tool.** We expect the use of earnouts and holdbacks to decrease over time as practices that were previously impacted by COVID are able to point to recent financial results showing established recovery trends for patient volume. Earnouts, however, may be a useful tool for solving uncertainty over the distribution of vaccines and the availability and expense of personal protective equipment (PPE). Regional spikes in COVID, especially, are causing dramatic geographic differences in revenue loss in early 2021, which may result in greater and continued use of earnouts in states such as California through the spring of 2021.

“Scale mattered when the coronavirus pandemic hit and volumes disappeared. Those with scale were able to survive and ramp up effectively when patients returned. Valuations came back along with the patients.”



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- **Shift to value-based healthcare is coming.** Changes to federal **fraud and abuse** laws and statutes may also lead to new physician compensation and collaboration models as the transition to **value-based healthcare** continues. The focus on improving quality and outcomes across the continuum of patient care, and reducing the cost of providing that care, may further drive interest and valuations for primary care and women's health platforms.
- **Continued opportunities for distressed investing.** Although we expect strong PPMs to continue to have ready access to debt capital for M&A and working capital needs, COVID-19 revealed weaknesses in some platforms that were unable to adapt or restore revenue post-COVID. We expect that lenders may be less willing to extend credit for continued expansion to groups that struggled to restore revenue, resulting in opportunities for distressed investors.
- **Tax law changes may impact valuation expectations.** If and when the Biden administration pushes tax reform, we expect the prospect of proposed tax rate increases on capital gains to cause some sellers to insist on higher valuations to preserve their "take home" payout.
- **Growing interest in employee ownership.** We expect growing interest by large group practices in alternatives to private equity transactions, with fresh looks at creative and tax-efficient structures such as ESOPs and other employee-ownership models.
- **Representation and warranty insurance is here to stay.** The growth of representation and warranty insurance (RWI) in practice management deals necessitates that buyers and sellers allocate more attention to data security and HIPAA compliance. Platforms, whether founder or private-equity-backed, that anticipate a sale process should undertake a close review with counsel of their compliance and insurance policies with the specific goal of facilitating the RWI underwriting process down the road.

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DENTAL & PHYSICIAN PRACTICE MANAGEMENT CLIENT HIGHLIGHTS



Served as lead counsel to KKR-backed **Covenant Physicians Partners** in its strategic partnership with the **Texas Eye Care Network**. A growing national network of leading physician practices across the outpatient care continuum, Covenant has established 60 physician partnerships spanning 19 states.



Advised **NAPA Management Services Corporation** in its acquisition of **American Anesthesiology, Inc.** The largest provider and manager of anesthesiology services in the United States, NAPA Management Services Corporation serves nearly 3 million patients annually in more than 500 healthcare facilities.



Represented **South Florida ENT Associates** in its partnership with **Texas ENT Specialists** and the creation of a combined entity, backed by Audax Private Equity, to support the collective 60 ear, nose and throat centers.



Advised **Tru Dental Partners** in its sale to **Heartland Dental**, the largest dental support organization in the country.



Served as lead counsel to **Axia Women's Health** in its acquisition of Cincinnati-based Seven Hills Women's Health Centers.

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