Practice mergers: the financial implications

SUPPORTING GENERAL PRACTICE | Practice mergers – financial implications

To help address patient demand, recruitment and changing Government requirements, many practices are contemplating a merger. However, the financial implications need to be clearly understood, as Bob Senior, Head of Medical Services at Baker Tilly Tax and Accounting Limited discusses.

When practices involved in a potential merger are discussing plans with each other, they need a clear idea of their long-term objectives. While one may be looking for a 'rescue' or a clear succession path, the other may be planning to increase business opportunities and generate greater profits.

Therefore, in order for the merger to work effectively, both sides need clearly identified tangible benefits – ideally ones that can be measured. By assessing at the outset what the value of these benefits are, it is easier to gauge whether it has been a success during future review meetings.

FINANCIAL IMPORTANCE

It's also important to look at financial issues and the steps needed to ensure clarity and understanding for all parties.

1

The starting point is a schedule of each practice's profits, so all costs and income can be dealt with in the same way by the two practices. Areas to clarify include:

- Which items of income are already allocated to partners rather than being shared by everyone?
- How expenses, such as superannuation, professional subscriptions and loan interest costs are dealt with? Whereas one practice may pay these costs directly, in the other they may be paid by the partners personally.

2

Having identified the operating differences between the practices, adjustments are needed to identify a comparable profit per partner for each practice.

3

It is also worth recognising how any future funding changes will affect each practice over the next five years. Will they:

- win or lose from changes to the minimum practice income guarantee (MPIG) or global sum funding?
- be at risk of losing funding or services following a review of PMS contracts?
- suffer any differences from their present profits per session rate once GMS/PMS funding changes have been introduced?

4

If there are significant financial differences, the lower earning practice could accept a reduced parity arrangement for a time, depending on the scale of the difference, until such time as the full business benefits are reflected in increased profits. However, this approach tends to be impractical for a period in advance of four years.

MAKE A FINANCIAL PLAN

When creating a financial business plan, it will need to show:

- what additional income can be generated from the merger?
- what cost savings can be achieved and how long will they take to achieve?
- what additional investment will be required?
- what will be the share profit per partner over each of the next five years?

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PREMISES

The financial implications relating to premises should also be considered very carefully when discussing mergers. The questions to be asked, and the steps to be taken, will depend on the ownership model of the different premises.

Practice owned surgeries

- What is the basis of the present valuation? Is the value as a GP surgery based on rental income or is it an open market value?
- How much does the difference between those two methods of valuation amount to?
- Is the surgery likely to remain fit for purpose and commercially viable?
- Is the surgery funded under cost rent rather than notional rent?
- Are there any long-term fixed rate loans with high interest rates in existence? What are the potential redemption penalties if the loan is cleared early?
- Are any retired partners still involved in the ownership of the property? If so, are they willing to be bought out?

Surgeries owned by GP-owned companies or property partnerships

- Are the present owners/investors happy to treat this as a commercial investment for the long-term, or do they expect new partners to buy them out in due course?
- If a buy-out is expected, how much would be required?
- Is the income generated from the investment sufficient to fund the necessary bank loan?

NHS Health Centres

- Is there a lease in existence? How long does it have to run?
- What does the lease say about service charges? Have they been agreed?
- Are there any unresolved discussions about earlier years' service charges? If there are, what is the potential scale of the arrears?

Surgery rented from commercial investors

- Is there a signed lease in existence? How long does it have to run?
- Is it a full repairing and insuring (FRI) lease, or simply an internal repairing and decorating lease?

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- If it is a FRI lease, does it include any dilapidations provisions? If so, is there an adequate reserve being built up on the practice balance sheet to cover that liability?

The number of practice mergers will undoubtedly increase over the next five years. The successful ones will be those with clear objectives and business plans that are robust and fair to all involved.

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