
# THE PROS AND CONS OF PRIVATE EQUITY

Recapitalization and access to capital straddle opposite ends of the private equity risk/benefit ratio.

BY BRETT KATZEN, MD; STEPHEN G. SLADE, MD, FACS; ERIC D. DONNENFELD, MD; RICHARD L. LINDSTROM, MD; TAL RAVIV, MD; ROBERT J. WEINSTOCK, MD; AND GARY N. WÖRTZ, MD

**Private equity is rewriting the playbook for some surgeons in ophthalmology. Katzen Eye Group made headlines in 2014 when it was acquired by Varsity Healthcare Partners in a deal that formed EyeCare Services Partners (ESP). This past year, Harvest Partners recapitalized ESP and replaced Varsity as its private equity partner. Also this past year, Minnesota Eye Consultants partnered with Waud Capital in an agreement that formed Unifeyed Vision Partners (UVP). An informal survey of attendants at this year's annual Hawaiian Eye Meeting revealed that approximately 60% of those who responded would be willing to sell to private equity firms within the next 5 years.[1]**

**In this article, leading ophthalmic surgeons consider the pros and cons of the private equity trend and what these deals might mean for the future of the specialty.**

## FINDING THE RIGHT PRIVATE EQUITY PARTNER

By Brett Katzen, MD

I felt positive about my decision to partner with private equity back in 2014. I knew I had found the right partner because I felt that our interests, priorities, and concerns were respected and considered, which is key for anyone considering a private equity partnership. Private equity enabled me to form ESP, our physician practice management company. ESP is based on the recognition that the mission of ophthalmologists and optometrists can be fully realized with management and operational support from credible experts. Our partnership enabled the creation of a company that respects quality of care, strong patient relationships, and trust in each eye care practice.

When I consider the many benefits that I have gained through partnering with private equity, I can easily and comfortably advocate for such partnerships. I think every practice owner will agree that the increasingly complex dynamics and trends within eye care are challenging and changing how we practice. Navigating these complexities—whether they are the impact of emerging government regulations, accelerated technology and related costs, or insurance billing and collections—makes it difficult to practice medicine while remaining competitive in today's eye care industry.

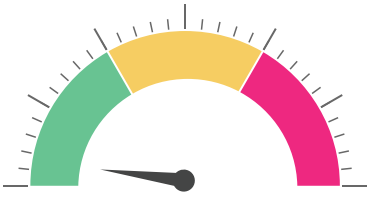
My partnership with private equity and the formation of ESP's management team gives me access to the type of business acumen and organizational infrastructure that my practice requires in order to navigate these complexities and remain sustainable over the long term. It also provides other value-added benefits that the company's national scale can afford, such as information access, patient and payer information, and compliance. As a result, we are growing and optimizing both the practice and its ambulatory surgery center (ASC).

It is still important to prepare yourself for unforeseen developments. Problems always arise, just as they would in any practice that is not partnered with a private equity firm. My advice is to hold on, relax, and let your managers *manage*. You need to trust that your partner wants your business to excel as much as you do.

It can be concerning to give up control of your practice. Finding the right partners is key, and when you find them, it will not feel like you are losing control. Instead, it should feel like you are gaining business and management expertise. My management team at ESP recognizes that successful eye care practices must efficiently manage the increasingly complex and costly realities of operating within a highly regulated and competitive environment. As my partners, they take on management duties while allowing me to foster and protect the clinical relationships that I have built over my career. They know my patients and my staff are crucial to the success of my practice—and to their business.

## PRIVATE EQUITY IS AN EXCELLENT STRATEGY FOR MANY PRACTICES

By Stephen G. Slade, MD, FACS



Private equity can offer a nice exit strategy for a physician looking to become less involved in the day-to-day management of a practice. It also offers capital and management expertise for a younger physician who is interested in rapidly growing a practice. Private equity investors will typically make an upfront payment but withhold a second payment to be made only if the new entity sells—so part of that payment is at risk for the physicians.

My practice has been approached by a surprising number of private equity firms. We have gone through the process up to the point where the next step would have been to sign a letter of intent (LOI) with one firm; however, we have not committed to any investor at the time of this writing.

My best piece of advice for a practice that is considering the risks and benefits of private equity is to find a firm that makes sense for you and at least go through the process to reach an LOI. Of course, do not sign the LOI unless you are truly interested in selling. You will learn so much from this exercise, and it is the only way to really know if that firm is the right one for you.

The process reminds me of some of our patients—those who spend years thinking about refractive surgery but have never even had a screening exam. Much like patients need to know if they are good candidates for refractive surgery prior to undergoing the procedure, a practice needs to know if it is a good candidate for private equity.

While there are no guarantees, private equity—with its outside funding—seems to have more long-term viability than previous physician practice management companies that have failed. This is a good thing because, for many practices, private equity is an excellent strategy.

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## EXPANDING OUR PRACTICE THROUGH PRIVATE EQUITY

By Eric D. Donnenfeld, MD

Health care is changing dramatically, and there are three major forces that dictate the way we practice: insurance companies, hospitals, and the government. The majority of internal medicine doctors have abandoned private practice, and hospitals are now in the business of primary care rather than advanced tertiary care. From my perspective, the era of the small ophthalmology practice is coming to an end, and consolidation appears to be inevitable within the next 10 years. I could work for a hospital, health maintenance organization, or insurance company and give up my autonomy and practice ownership, or, as our practice decided, attempt to grow large enough to be at the bargaining table ourselves.

In October 2017, there was a unanimous decision by the partners of Ophthalmic Consultants of Long Island—and shortly thereafter, Ophthalmic Consultants of Connecticut—to enter into a strategic affiliation with a well-respected private equity partner in Blue Sea Capital via Spectrum Vision Partners, our management services organization. This decision was made after 1 year of investigation, deliberation, and interviewing many private equity firms.

The affiliation with Blue Sea Capital represents a meaningful and positive event for the partners, associates, staff, and leadership across our 18 offices and two ASCs.

Our goals are simple: to continue to provide the highest quality of care for our patients with the most advanced technology and to have the resources necessary to expand our model into the New York market. Since this affiliation, we have added four practices, and we plan to add multiple new office locations each year going forward. This is possible due to the additional resources and capital provided by Blue Sea Capital.

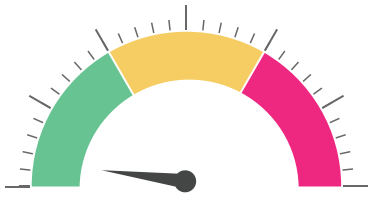
There is often concern that private equity firms will change the way a practice operates. In our case, Blue Sea Capital wanted to invest in Spectrum Vision Partners because it liked what it saw and wanted to build upon it. Our physician management team continues to run the practice in the same manner as before, and physician shareholders retain significant ownership.

Working with private equity also solved two major problems. Young ophthalmologists do not want to make large investments into a practice when the future is so uncertain, and senior partner ophthalmologists no longer expect to be bought out at

the end of their careers. Removing these impediments allows our practice to stay together and grow. All of our ophthalmologists, young and old, have monetized their investment into our practice and are now more financially diversified and committed to the growth of the practice. There is concern that history will repeat itself from 2 decades ago when practice management companies tried and failed to consolidate ophthalmology. However, there are major differences today, both philosophically and in how the deals are structured. Private equity is certainly not the best strategy for every practice, but it is the best option for our practice and for many others.

## A CATALYST FOR GROWTH

By Richard L. Lindstrom, MD



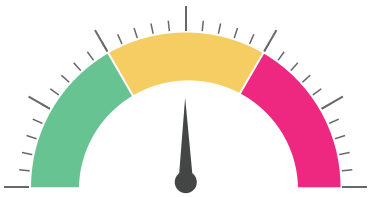
Minnesota Eye Consultants partnered with Waud Capital investors in 2017, and we continue to be happy with the decision. The 11 partners in our practice each received a personal cash infusion, accessed new capital for practice investment, and currently have no partner-guaranteed debt. Not only do we continue to practice as before, but we are growing faster than ever.

The biggest unknown in our situation regards the eventual recapitalization and the new partner, UVP, which will replace Waud Capital as majority owner in a few years.

This type of transaction is not for everyone. The desire to grow the practice is necessary in order to enjoy the benefits of increasing practice value. Some physicians may not want to reduce their current income for the potential of more long-term upside opportunities. If you believe your practice will be significantly more valuable in 5 years, then you might choose to wait to enter any agreement with private equity investors. If you are concerned that your practice might be worth the same or less in 5 years, especially in the face of significant, potential, external environmental challenges, you should look into working with a private equity investor today. It is important to realize that this is a two-sided decision—a true partnership—and a win-win outcome is necessary for both the ophthalmologist and the private equity investor. Realize that even if you want to sell to private equity, the private equity firm you want as a partner may not want *you* as a partner, or may not be working in your region.

## APPROACH PRIVATE EQUITY WITH CARE

By Tal Raviv, MD



There are many forces causing the consolidation of medical practices in the United States. Some practices merge together, some get acquired by hospital systems, and some sell to private equity to better weather the storm. In the current market, if a practice is looking to sell, private equity may be the best option offering the highest earnings before interest, depreciation, taxes, and amortization multiple valuation—this is the basis for the price a private equity firm will pay for a practice.

A young, growing practice whose primary physician owners have many productive years ahead of them is at the highest risk to the unknowns of private equity. Private equity funds are looking for undervalued assets (practices) that they can combine and grow with the aim of selling them for profit in a short number of years.

Selling one's practice to private equity must be approached with care, as would any transaction that results in change of practice ownership. Physician owners in the first half of their careers may not want to risk giving up autonomy to a third party, especially when there is no way to know if a second equity event will transpire or who their ultimate owners will be.

## UNDERSTAND THE RISKS

By Robert J. Weinstock, MD

There are certainly positive aspects to private equity investment in ophthalmology practices. First, you get to partner with an entity that has access to substantial financial capital. If you want to grow your practice, buy new equipment, or open an ASC, having access to capital is a major advantage over incurring personal debt. Second, some private equity firms offer management solutions that can lighten your burden, particularly if the investor has talented leaders who know the eye care industry well. Third, private equity investors can help eliminate some of your debt, and tax ramifications are quite favorable for the money that comes to you.

An important aspect to consider is that if you sell to private equity, you give up some control of your practice. A board or executive committee will be responsible for the financial decisions in the practice. Therefore, when it comes to large acquisitions in equipment or building out a new satellite office or ASC, those decisions can only be *recommended* by the doctors—ultimately they are not *in control* of that decision. Additionally, the doctors become employees of the new entity, so they must negotiate an employment agreement with the new owner. As an employee, one is mandated to work under a certain set of rules for a certain amount of time, and there are penalties if you exit the agreement sooner than agreed upon.

There is also a concern regarding recapitalization. Most private equity deals are structured in such a way that the original investors will not earn much money until they sell again. If things go well, your company will be sold to a larger private equity or venture capital firm, and you will face a new employment agreement, a new ownership structure, and another transition after which you will be answering to a new set of financial managers.

At the end of the day, the reason private equity investors are interested in ophthalmology is money—not eye care or the quality of that care. The goal of private equity investors is to profit from buying companies and selling them to larger private equity firms. The only way to accomplish this goal is to make the company more valuable than it was when they bought it. Ultimately, it is all about how that happens and making sure that it does not happen in a format that affects patient care or your ability to enjoy doing what you do.

Although I once considered selling to private equity investors, I realized that it was not the right move for me at that time. My focus is on delivering the best quality of care, and I want to be in control of that care. I want to grow the practice and be in charge of decision-making. I am concerned about who the second owner (after recapitalization) could be and what their philosophy would be, particularly with respect to the decision-making process. There are some other models—larger holding companies, for instance—on the horizon that I believe might be better than private equity. With that in mind, we decided to wait, take it slow, and look at other options.

## YOUNGER SURGEONS HAVE LITTLE TO GAIN FROM PRIVATE EQUITY

By Gary N. Wörtz, MD

The risks in partnering with private equity generally revolve around misaligned interests (profit vs care) and loss of control and autonomy. The tradeoff is the benefit of having access to capital and management resources that may be superior to what you currently have. It is important to note, however, that although access to capital may mean access to better technology, the better technology could be less cost effective and worse for profitability in the short term.

I do not believe that younger surgeons have much to gain from private equity—but they have much to lose. Being subjugated to a financial institution that might see you as a cog in a machine is generally not a great recipe for professional enjoyment.

Unless the private equity firm has a balanced ownership structure that rewards the physician partners, I do not think these relationships will work over the long term; if they do, they may be bad for our profession as a whole. Removing a large portion of decision-making power from the ophthalmologists who have expertise in patient care will create a new class of *doctor technicians* who simply show up, do what they are told to do, and go home. For our profession to move forward, we need ophthalmologists to be actively engaged in ways that improve the specialty. ■

1. Simerson CS, et al. The changing ophthalmic practice environment. Presented at: Hawaiian Eye; January 13-19, 2018; Wailea, Hawaii.

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