

# CALIFORNIA ORTHOPAEDIC ASSOCIATION APRIL 17, 2010



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## Real Estate Investment Strategies

*Presented by:*  
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**Health Care Team**



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# Real Estate Investment Strategies



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# **Can Real Estate (Owning your Own MOB) be a Good Investment?**

## **How do we do it?**



# MEDICAL OFFICE BUILDING (MOB)

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- If Owned by Owners of Medical Practice
  - Incorporate in medical practice agreements mandatory buy-in & buy-out of real estate with the buy-in & buy-out of medical practice



# MEDICAL OFFICE BUILDING (MOB)

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- Key Considerations
  - Location & Demographics
  - Alternative Uses
  - Hospital Involvement
  - Health Care Corridor
  - Ancillary Limitations



# MEDICAL OFFICE BUILDING (MOB)

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- Key Considerations
  - Number of Locations
  - Age Mix of Physicians in the Group
  - Financial Health of the Physicians in the Group
  - Ownership needs to be inclusive of all physicians in the group



# MEDICAL OFFICE BUILDING (MOB)

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- Even if Real Estate is Joint Ventured  
(Own Piece of a Larger Building)  
Set Up Your Own Entity to Hold the  
Group's Interest



# **MEDICAL OFFICE BUILDING (MOB)**

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**Never Own Real Estate  
in a  
C Corporation**



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# **MEDICAL OFFICE BUILDING (MOB)**

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**California –  
Limited Partnership with  
Corporation as 1%, General Partner**



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# MEDICAL OFFICE BUILDING (MOB)

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- Succession Planning
  - Is Buy-in Price too Expensive?
  - What is the Exit Strategy?
    - Hospital buyer
    - REIT
    - Fellow partners



# MEDICAL OFFICE BUILDING (MOB)

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- Avoid Fair Market Value Appraisals
  - Single use, special purpose property
  - Limited market, thus limited value on resale
- Only Use Appraisals to Test Book Value/Cost Approach



# MEDICAL OFFICE BUILDING (MOB)

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- Recommend either Book Value Approach for Real Estate Entity, Building, Land & Improvements (i.e., Valued at Cost, Excluding Depreciation Valuation)

Or

- Capitalization of Net Operating Income with Cap Rate Predetermined and set in your Legal Documents



# MEDICAL OFFICE BUILDING (MOB)

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- What is the Dollar Threshold on a Per-Physician Basis where Cost is Prohibitive – \$100,000 - \$75,000 - \$50,000 per physician?



# MEDICAL OFFICE BUILDING (MOB)

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- What Do You Do if Buy-In is Too High?
  - Refinance & increase debt with financial institutions & distribute cash to current owners
  - Offer purchasing physician 5–10 years to pay for buy-in having entity issue note



# MEDICAL OFFICE BUILDING (MOB)

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- What Do You Do if Buy-In is Too High? (Cont'd)
  - Sell partial interest each year until equal ownership achieved
  - Convert existing equity to debt by issuing notes to current owners & pay interest on notes (mo./qtrly. interest), lowers buy-in, but no change to buy-out obligations

*Buy-out = equity + notes payable*



# MEDICAL OFFICE BUILDING (MOB)

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- Equity to Debt Conversion – Priority of Cash Flow
  - Operating obligations
  - Debt service on bank debt
  - Debt service on other debt
  - Payment obligations related to purchasing interest of terminated or retired member
  - Pre-payment of debt approved by Board of Managing Members





# MEDICAL OFFICE BUILDING (MOB)

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- Equity to Debt Conversion (Cont'd)
  - Discretionary distributions to member for purposes of assisting with annual tax obligations
  - Remaining available cash shall be applied to members' equity promissory notes in proportion to value of each member's note to all members' notes



# MEDICAL OFFICE BUILDING (MOB)

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- Equity to Debt Conversion (Cont'd)
  - Remaining available cash paid to each member according to the combination of their equity & equity note in proportion to all members' equity & equity notes



# MEDICAL OFFICE BUILDING (MOB)

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- Equity to Debt Conversion (Cont'd)
  - If members' equity notes paid in full & cash remains for distribution, Board of Managing Members may elect to distribute cash to members based upon each member's capital account as a % of total member's capital account



# MEDICAL OFFICE BUILDING (MOB)

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- Additional Value on Exit
  - Based on years of service, age & proper notification of intent to retire, allow physician to maintain real estate ownership for some years beyond retirement (1,2,3 yrs.)
    - Leave physician in ownership & profits interest for 1,2,or 3 yrs., then sell at end of period



# MEDICAL OFFICE BUILDING (MOB)

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- Additional Value on Exit
  - Leave physician with profits interest only with immediate sale of ownership interest
  - Guarantee minimum years of ownership & profit interest to account for up front risk for senior physician (i.e., 10 years)
  - Use of a “sale-tail”



# USE OF “SALE TAILS”

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Concept that allows retired physician to participate in sale proceeds some defined period of time after retirement



# CONCLUSION

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Real Estate, if  
Properly Structured,  
Can Be One Real Asset  
for a Practice.



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