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PHYSICIAN-OWNED REAL ESTATE

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New Blood – It's Your Real Estate's Lifeblood

The Two Keys to Keep It Flowing

The All-Too-Familiar Scenario

In 2021, a group of 10 physician partners invested in the MOB that housed their practice. They financed 85% of the $20MM project cost and contributed the remaining 15% in cash. The rents produced cash-on-cash returns to the doctors of over 10% in the first year.

In 2025, two new partners were scheduled to buy in and would have been attributed an ownership share proportionate to their investment against the equity. The new practice partners, however, declined the offer to invest in the real estate and, by doing so, devalued and destabilized the original real estate investment. Without continued buy-in from new partners, there's no assured source of funding buyouts and, perhaps more importantly, the group is less likely to renew its lease once the original partners become the minority.

	Original Partners	New Partners
Property Value	$20,000,000	$24,000,000
Outstanding Debt	$17,000,000	$12,000,000
Group's Equity	**$3,000,000**	**$12,000,000**
Number of Partners	10	12
Equal Ownership %	10.00%	8.33%
Buy-In Amount	**$300,000**	**$1,000,000**
1st Year Distribution	$30,744	$50,620
Return on Equity / Cash on Cash	**10.25%**	**5.06%**

Table 1

"Just Not Interested in Real Estate"

That's the conclusion drawn by many existing partners when they witness an unwillingness of those younger doctors to buy in. After all, "They are getting the same deal we got." But are they? In fact, the investment opportunity has failed the "A&A Assessment" – Affordability and Attractiveness. The real reason new docs might pass on buying into the real estate may not, in fact, be a lack of interest.

What's The Problem?

Let's take a look at what is being offered to the new docs. As the valuation of the group's real estate portfolio grows and the entity repays its debt obligations, the buy-in for a new partner often increases and can become burdensome. Assume that within those years, the property has appreciated by 20% and the loan has been paid down by 20%. The property now has a value of $24MM with just over $12MM of debt (*see Table 1*). What was previously a $300K investment for a 10% share and 10% initial return is now a $1MM investment for an 8.33% share and a 5% return. Not the same deal at all.

At the national CPOMP conference in 2022, James Winchester, the moderator of a session on operating agreements, posed a simple and singular question to a group of senior doctors who owned their property which in turn gave rise to the A&A Assessment. "If you were looking to buy this property today, would you do so if you had to come up with 50% of the purchase price in cash for a return of less than 6% or would you pass? If the answer is 'pass,' why would you expect a different answer from the new docs?"

Not interested or not interesting?

The Link Between Attractiveness & Affordability

There aren't many new partners who have $300K in liquid assets lying around, let alone $1MM. Subsequently, these new partners often require personal loans from lenders to finance their buy-ins. In some instances, the group may even internally finance these buy-ins, which often detracts from the returns received by the existing partners. In either instance, it results in a note being due to the bank or to the existing partners. The ability of the new partner to cover this debt obligation becomes paramount.

Covering this personal loan payment can be much less demanding on the new partner if the real estate entity is generating greater returns and distributing more cash annually, relative to the buy-in amount. In other words, if the real estate entity has a better cash-on-cash return, the partner can cover more of their personal debt with the distributions being received from the real estate (*see Table 2*).

So, the last question becomes how do we improve the cash-on-cash returns that the real estate entity is generating? There are three items that primarily impact the cash-on-cash returns that a partner receives without negatively impacting the returns of their partners:

1. The Rental Income
2. The Loan-to-Value
3. The Loan Terms (Interest Rate & Amortization)

	Original Partners	New Partners
Return on Equity / Cash on Cash	**10.25%**	**5.06%**
Personal Debt Amount (90% of Buy-In)	$270,000	$900,000
Cash Required for Equity	**$30,000**	**$100,000**
Portion of 1st Year Distributions	$30,744	$50,620
Personal Debt Payment	$45,794	$152,646
Remaining Shortfall	($15,050)	($102,027)
% of Personal Debt Covered by Distributions	**67.13%**	**33.16%**

Table 2

Assuming the rental income is in line with fair market rent, this item isn't something that you're likely going to adjust a great deal because it cuts into the practice's profitability. Thus, the property financing becomes the primary tool to positively impact the partners' returns without adversely affecting existing partners.

If you're curious to learn your cash-on-cash returns, and whether they could potentially be enhanced to make the investment interesting, please reach out to solutions@cmacpartners.com to find out more and receive your own complementary analysis.

On the Inside...

Tailoring Your Operating Agreement

One Size Does Not Fit All

Mariela Araujo
Principal

A couple years ago, I had an eye-opening conversation with a physician at a prestigious orthopedic conference.

We were discussing the way the group handles its buy-ins and buyouts, as one of their legacy partners was getting close to retirement. This physician was somewhat concerned about the amount of distributions they would have to let go to buy this partner out, given that the current structure was a note to the retired partner to be paid over three years, and the equity per partner was sitting at over $1MM, with just six partners in total.

With the very limited time we had at the conference, we couldn't get into the details of the capacity of the entity to fund this upcoming buyout, so we decided it was best to schedule a video conference when we were both back in our respective offices.

Once I returned, I ran our 30-year economic model to factor in their existing rental income and corresponding debt obligations so I might ascertain the forecasted distributions. This process revealed that executing a three-year buyout plan would severely strain the financial viability of the entity. Given that the forecasted distributions were insufficient to cover the buyout note, the partners would find themselves obliged to cover the buyout costs personally - a burdensome prospect, particularly for those still grappling with student debt.

Upon recognizing this deficiency, the group wanted to amend the buyout provisions, proposing an extension of the buyout period. However, objections from senior physicians nearing retirement impeded this course of action. Subsequently, when the time arrived, the retired physician was bought out and the remaining partners had no other choice but to issue personal checks to fulfill the buyout obligations.

How could this have been avoided?

This situation stemmed from a lack of thorough financial evaluation at the time the Operating Agreement was drafted. The legal counsel engaged then, who had considerable experience in Commercial Real Estate, replicated provisions akin to those employed by the firm over the past several years.

But physician-owned medical real estate ventures are unique entities that demand meticulous attention to detail in their operational framework. Unlike conventional real estate ventures, these properties intertwine the ingress and egress of physicians and the ability to create affordable and attractive investment propositions, thereby necessitating a tailored approach in their governance.

CMAC has developed a guide to address the intricacies of these investments. Drawing from a repository of hundreds of operating agreements from independent practices nationwide, this guide incorporates over 75 pertinent questions, ensuring comprehensive coverage of various scenarios. It is organized into distinct categories covering valuation methodologies, buy-ins and buyouts, voting rights, and events of sale. Serving as the cornerstone of the investment, this document delineates not only the legal framework but also the economic considerations critical to the success and sustainability of physician-owned real estate.

We invite you and your partners to answer the following questions:

- Is our operating agreement aligned with our group's specific objectives and philosophies?
- Have we evaluated the economic implications of the provisions within the operating agreement?
- Will the existing provisions contribute to the long-term sustainability of our investments?

These questions, among others, can be addressed through CMAC's interactive guide and economic models, facilitating informed decision-making and fostering sustainable owner-occupied real estate investments. Email solutions@cmacpartners.com for a link to the guide.

Seller Beware *Are You Sure You Want a Second Bite of the Apple?*

Contrary to Snow White's poison-induced slumber, the sale-leaseback second bite of the apple might keep you wide awake. This article will outline the typical structure, risks, and considerations of the "red delicious" of physician-owned real estate.

What do real estate buyers mean by "second bite of the apple?"

When real estate owners sell their buildings in a sale-leaseback transaction, the "second bite of the apple" is a commonly used term referring to owners rolling their proceeds into the purchasing entity's portfolio, thereby capitalizing on a future portfolio sale. The concept has gained steam in recent years as sellers look to defer capital gains tax to a later date and reinvest their acquisition proceeds. Unfortunately, this second bite of the apple can quickly transform an event buyers would describe as "taking your chips off the table" into one more akin to "rolling the dice."

Considerations of Taking the Second Bite

A common misconception owners make is conflating the owner-occupied investment they have enjoyed with the investment they would make with a private equity buyer. Just because the buyer focuses on medical properties does not make these investments comparable. An important question to ask yourself is: would you make the same investment if you weren't rolling your proceeds (and deferring taxes)? If not, then you probably shouldn't be considering rolling your gain at sale. There are numerous variables to consider when investing in a real estate fund, including:

- What assets are included?
- What is the fund structure – debt vs. equity?
- What timeframe is the fund aiming to hold its assets?

Thoroughly understanding the investment is paramount to making a sound investment decision. Below is an example of a group that may be hoping they had read this article a little sooner.

Case Study: Ophthalmology Practice Takes Second Bite

In 2021, a northeastern ophthalmology practice sold its building at a 6.25% capitalization rate. Enticed by promises of 10% cash-on-cash returns and historical fund performance, the partners opted to roll their proceeds into a new fund offered by the buyer. This all sounded enticing, and many of the partners decided to partake in the continued investment. Good returns and deferred taxes

equated to a great deal ... until they looked under the hood.

The private equity firm's strategy involved rapid aggregation and packaging of medical properties for institutional buyers, funded largely through short-term, interest-only debt. Rising long-term interest rates (increased by approximately 300 basis points since acquisition), however, elevated cap rates, diminishing property values. Consequently, the partners found themselves with depreciated assets and limited refinancing options as debt maturity approached.

As of this writing, we are a couple of months away from the maturity of that interest-only debt. The ownership has limited ability to refinance because the loan-to-value is significantly higher now than at acquisition. An increase in interest rates means that even if financing were possible, it would cause negative cash flow. The only solutions are to sell the building at a loss or inject significant equity in the hope that interest rates decline.

Beware of Speculative Investments

This cautionary tale underscores the inherent risks of speculative real estate investments. CMAC provides clients with comprehensive advice on the complexities and implications of sale-leaseback opportunities. If you're considering such a transaction without expert guidance, reach out to CMAC for assistance.

Pay a $275,000 Penalty or Pay Back the Loan

How a Major National Bank Used a Technical Default to Extract its Pound of Flesh

It was a great relationship going in. All handshakes and smiles. "We are happy to make this real estate loan and we don't need the practice's business banking. I mean, it would be nice, but that's fine…" until it isn't!

This is a story of just how incredibly important each and every covenant can be in a borrower's loan documents. Understanding and monitoring your obligations will help you be prepared if:

- The relationship turns sour,
- Personnel or policies change in a way unfavorable to the borrower, or
- Regulators require the bank to trim its portfolio.

"LET THE BORROWER BEWARE"

In this particular case, a large specialty group in the northeast failed to meet a bank ratio covenant, which triggered a technical default. In most scenarios like this, the lending bank will work with the borrower to cure the breach or make sure it is not repeated. This bank felt that there was an implicit agreement by the borrower to consider shifting its depository business. The borrower felt there was no such obligation and, as it was a not a stipulation of the loan agreement, did not plan to move deposits. That did not sit well with the lender and when the borrower missed on a covenant ratio, the bank did not hesitate to make its point … in spades! The bank gave the borrower three options. It could:

a) move its accounts to this bank,
b) pay back the loan, or
c) pay a penalty of $275,000.

When William Congreve wrote that "Hell hath no fury like a woman scorned," he obviously had never met an unhappy banker.

By sharing this experience, it is the writer's hope that future borrowers may never find themselves in such a position by following CMAC's three "Covenant Canons."

1. Negotiate – Don't agree to something that you don't fully understand or feel may be troublesome. Try to recognize what security the bank is seeking and look for a better way to provide it.

2. Test – Some formulas can be rather complex. Sit down with the bank and have them use your historic performances as examples so that you can fully understand the method of testing and assure yourself that you would meet the standards now and in the past.

3. Monitor – Things change. By constantly testing, you should never be surprised by a breach of a covenant. By going to the bank early, you will either find a way to work around the breach with the bank or have advance notice to seek other options.

The Easiest Technical Defaults

While most borrowers are focused on numbers and ratios, other breaches, generally involving reporting, can be subtle and just as deadly. One of the least noticeable and most pervasive is the reporting requirement on personal guarantees. We consider this reporting requirement a much greater risk than the guarantee itself. Consider a group of 20 partners who are required, by virtue of their personal guarantees, to send their personal financial information to the bank within 30 days from the end of a period and just one of them does not make the deadline. Bingo!

A Better Ending

In the case of the northeast borrower, CMAC negotiated with the bank to find a more palatable outcome for all parties. The bank raised the fixed rate by just a few basis points with an understanding that it would reduce the rate back to its original level should the borrower ever move its deposits. A soft landing, admittedly, but one that we all would have rather avoided.

The bottom line is that every provision in a loan agreement can be important no matter how mundane it may appear. Understand your obligations, make sure you are comfortable meeting those obligations, and monitor your performance to ensure compliance!

Internal Valuations: How a Higher Multiple Can Lead to Lower Returns

Ha Tran
Principal

Internal valuations have evolved. More than 50% of our clients are now using a multiple of their building's net operating income to derive their share value. This article explores how selecting the correct multiple can be a counterintuitive process.

"As an owner, we like our multiples to be high."

"Higher multiples are great. A higher multiple on my EBITDA makes my practice more valuable. A higher multiple on my real estate means my building is worth more." It's not uncommon to hear physician owners follow this logic and apply it to their practice-occupied real estate. A few weeks ago, I participated in a panel discussion with a physician who was making this very point, stating that, "As an owner, we like our multiples to be high, so we set our cap rate low for buy-ins and buyouts." Let's explore an example to help illustrate that logic.

An ophthalmology clinic owned by 10 partners is producing $1MM of net operating income. The group has been using a 10x multiple (10% cap rate) resulting in a $10MM value. Currently, the property has $6MM of debt, therefore creating an equity position of $4MM.

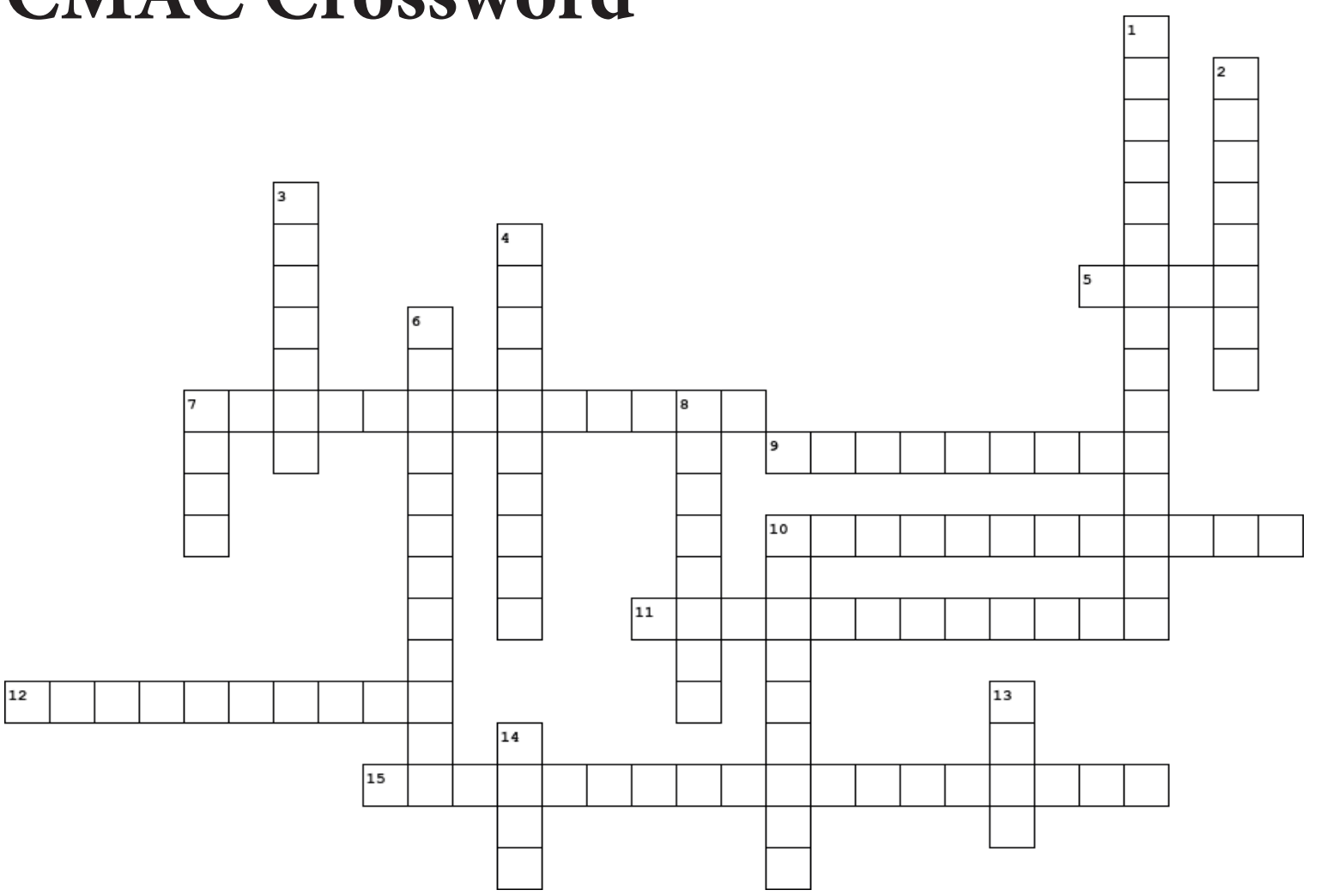
The group is considering adjusting the multiple to align more closely to a market value, which would take the multiple up from 10x to 14x (7.14% cap). Suddenly, the building's value increases to $14MM. With $6MM of debt, there is now double the amount of equity ($8MM). All 10 partners have $800,000 of equity instead of $400,000. Everyone is a winner! We can stop following the math and assume all these partners lived happily ever after with more income, right? Not so fast.

With MENTES360, a forecasting, management, and reporting tool that generates a customized 30-year model, we can now understand in granular detail the impact of such changes – and the results might come as a surprise. This change is NOT necessarily good for the majority of the existing ownership and here's why. As a private practice real estate owner, you are consistently selling AND buying ownership in the real estate entity as new partners join and existing partners retire. While higher multiples are great if you are selling, they are not great if you are buying more ownership. Your purchase price just got more expensive. Every time shareholders leave the real estate entity with an increased buyout price, the remaining shareholders will be making a higher payment. This creates an inflexion point. The shorter the timeframe to retirement, the more motivated you are to increase the multiple. The longer the timeframe, the less motivated you are.

Jumping back to the example above, despite the eventual doubling of equity for the existing partners, the partners with 20 – 30 years remaining to practice received returns that were roughly 30% less than they would have received with a lower multiple. The longer the partners stayed, the worse their individual outcomes became. For groups that are trying to promote retention, increasing the multiple will likely have an undesirable effect, as partners become economically incentivized to retire earlier. For groups that are trying to bring in new partners, the outcome is a little more obvious, as the buy-in becomes more expensive and the returns are diminished.

Above all, when considering changes to valuation methodology, we recommend being able to quantify the effects on an individual level, for both existing partners and prospective new partners. This is why more and more of our clients are turning to MENTES360 for impartial analysis. If you would like to schedule a free demo based on your practice's situation, please reach out at support@mentes360.com.

CMAC Crossword



Across

5. Abbreviation for the organization governing interest rate derivative products, which developed the "Master Agreement" between parties.
7. Allows the owner-occupant of a property to sell it to an investor-landlord while continuing to occupy the property as tenants.
9. When the terms of an existing loan, such as interest rates or payment schedules, are revised.
10. A bank product that gives you access to amoney (up to a set limit) that you can borrow and repay as needed. You only pay interest on the amount you borrow.
11. Financial summary showing assets and liabilities at a certain point in time.
12. Something pledged as security for repayment of a loan to be forfeited in the event of a default.
15. Amount of lease revenue that flows through to the owner after payment of all expenses, excluding payment of any debt service (i.e.principal and interest).

Down

1. Also called a profit & loss, the detailed financial results of a business over a period of time. Quantifies amount of revenue generated and expenses incurred.
2. A legal agreement by which a bank lendsmoney at interest in exchange for taking title ofthe debtor's property, with the condition that the conveyance of title becomes void upon the payment of the debt.
3. The failure to promptly pay interest or principal when due is a common trigger of this condition.
4. One one-hundredth of a percentage point.
6. The value of an expected income stream determined as of the date of valuation using an expected rate of return.
7. This Abbreviation for a one day, collateralized, floating rate that is a widely used index by banks as a replacement for LIBOR.
8. A promise or agreement between a borrower and a lender that outlines one of the terms of a business loan or bond issue.
10. General name for any obligation that is owed by company; examples include loans, debts, bills.
13. Abbreviation for the proportionate amount by which net income must exceed the loan payments over a given period in order to assure that there will always be sufficient income to pay the debt.
14. A debt investment in which an investor loans money to an entity (corporate or governmental) that borrows the funds for a defined period of time at a fixed interest rate.

Crossword solution on page 9

Understanding Cap Rates

The Poster Child for Counterintuitive Thinking

Peter Kokins
Principal

As a young man just starting to learn the game of golf, I remember my confusion when I visited the sporting goods store to purchase my first glove. "Are you right-handed or left-handed" I was asked. "I'm a righty." "Great, then here's a glove for your left." The conversation that ensued was reminiscent of Abbot and Costello's "Who's on First."

So it is with cap rates. It just seems right to think that if someone throws a higher capitalization rate at you for the property you are selling, you should get a higher selling price. Not the case. Just the opposite in fact.

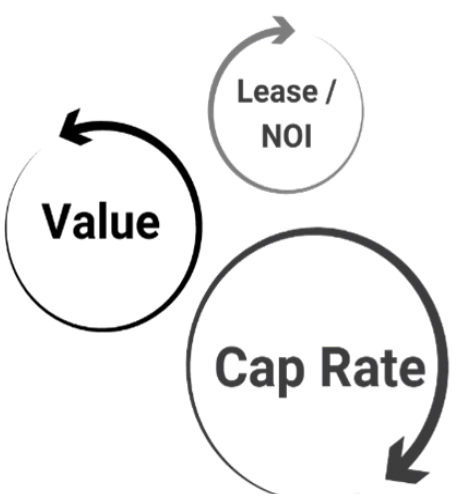
The purpose of this article is to unconfuse the reader once and for all by doing two things:

1. Explaining what a cap rate is, and
2. Giving you an easy way to remind yourself if you ever get "re-confused."

What the Heck is a Cap Rate?

A cap rate is simply the measure of return that any investment is expected to produce. If a buyer speaks of paying an "8.5 cap rate" for a property, that means the buyer is expecting an 8.5% return. Let's apply this in an example. If a property was throwing off a net operating income (NOI) of $1,000,000, the buyer seeking an 8.5 cap would divide the $1,000,000 by 8.5% to determine the purchase price of $11,764,706. Going backwards, if we multiply the purchase price of $11,764,706 by 8.5%, then the NOI would be $1,000,000.

Now, let's say that we find a buyer willing to pay 7.75% for that same property that's producing $1,000,000 NOI. We divide the $1,000,000 NOI by 7.75% and arrive at a purchase price of $12,903,226. Again, if we multiply the higher purchase price of $12,903,226 by 7.75%, we're back at the same NOI of $1,000,000 but with a purchase price that is $1,138,520 higher because of a LOWER Cap Rate.



An Easy Way to Remember

With something as counter intuitive as cap rates, it is helpful to have a fallback. I suggest an easy mnemonic; in fact, something easier than remembering how to spell mnemonic. It can actually be fun to come up with something on your own and that is probably way better than the one I use ...

"If the cap is high, it's time to buy"
"If the cap is LOW, we're in the dough"

Whatever works for you. Just keep it simple and meaningful.

Heaton Eye Associates

Tyler, TX

Ophthalmology

$35,400,000

Wisconsin Institute of Urology

Neenah, WI

Urology

$12,000,000

Shoreline Orthopaedics

Holland, MI

Orthopedics

$17,700,000

EYE-Q Vision Care

Fresno, CA

Ophthalmology

$14,400,000

Wake Internal Medicine Consultants

Raleigh, NC

Internal Medicine

$19,500,000

Ogden Clinic

Ogden, UT

Multi-Specialty

$12,400,000

Orthopedic & Sports Medicine Center

Elkhart, IN

Orthopedics

$16,900,000

Kansas City Bone & Joint Clinic

Overland Park, KS

Neurology & Pain

$3,500,000

CMAC Partners

WE KNOW MEDICAL

Urology

Arkansas Urology*
Little Rock, AR

Central Ohio Urology Group
Gahanna, OH

Idaho Urologic Institute*
Meridian, ID

Southeastern Urological Center
Tallahassee, FL

Urology Associates, P.C.
Nashville, TN

Urology San Antonio
San Antonio, TX

UroPartners
Westchester, IL

Wisconsin Institute of Urology*
Neenah, WI

Ophthalmology

Bay Eyes Cataract and Laser Center
Fairhope, AL

BoozmanHof
Rogers, AR

California Eye Institute*
Fresno, CA

Emerald Coast Eye Institute*
Fort Walton Beach, FL

Eye Associates of Boca Raton
Boca Raton, FL

Eye Associates of Colorado Springs
Colorado Springs, CO

Eye Surgeons Associates*
Bettendorf, IA

Eye Center of North Florida
Panama City, FL

Eye Institute of West Florida*
Largo, FL

Eye Specialists of Mid-Florida*
Winter Haven, FL

EYE-Q Vision Care
Fresno, CA

Heaton Eye Associates
Tyler, TX

Huntsville Laser Center
Huntsville, AL

Laser & Surgery Center of the Palm Beaches
Palm Beach Gardens, FL

Magruder Laser Vision*
Orlando, FL

Medical Eye Specialists
Bozeman, MT

Ocala Eye
Ocala, FL

Ophthalmology Consultants
St. Louis, MO

Pacific Cataract & Laser Institute
Chehalis, WA

Retina Consultants of Southern Colorado
Colorado Springs, CO

Retina-Vitreous Surgeons of Central New York
St. Louis, MO

St. Louis Eye Surgery & Laser Center
St. Louis, MO

The Eye Clinic of Florida
Zephyrhills, FL

Tower Clock Eye Center
Green Bay, WI

Virginia Eye Institute*
Richmond, VA

Hospitals

Arkansas Surgical Hospital
Little Rock, AR

Ascension St. Vincent Orthopedic Hospital
Evansville, IN

Catholic Health/St. Francis Hospital*
Colorado Springs, CO

Heritage Park Surgical Hospital
Sherman, TX

Lafayette Surgical Specialty Hospital
Lafayette, LA

North Carolina Specialty Hospital
Durham, NC

Springhill Medical Center
Mobile, AL

The Breast Cancer Center at Physicians Medical Center
Houma, LA

The Spine Hospital of Louisiana at the NeuroMedical Center
Baton Rouge, LA

Western Reserve Hospital*
Cuyahoga Falls, OH

Cardiology

Abilene Cardiology
Abilene, TX

Alabama Heart & Vascular Medicine
Tuscaloosa, AL

Alaska Heart & Vascular Institute
Anchorage, AK

Cardiovascular Associates*
Birmingham, AL

Cardiovascular Institute of Orlando
Orlando, FL

Cardiovascular Institute of the South
Houma, LA

Clearwater Cardiovascular
Clearwater, FL

Florida Heart Group*
Orlando, FL

Fort Worth Heart*
Fort Worth, TX

Northeast Georgia Heart
Gainesville, GA

Orlando Heart
Orlando, FL

Pima Heart
Tucson, AZ

Savannah Cardiology
Savannah, GA

South Denver Cardiology
Littleton, CO

Southern Cardiovascular
Gadsden, AL

Sutherland Cardiology Clinic
Memphis, TN

Surgery Centers

Bend Surgery Center
Bend, OR

Blue Water Surgery Center*
Port St. Lucie, FL

Carolinas Center for Surgery*
Morehead City, NC

Hilton Head Surgical
Hilton Head, SC

Palmetto Surgery Center*
Columbia, SC

Plastic Surgery Specialists of South Florida*
Hollywood, FL

Southpoint Surgery Center
Jacksonville, FL

Surgery Center of Southern Oregon
Medford, OR

Multi-Speciality

Audubon Medical Building*
Colorado Springs, CO

Austin Regional Clinic
Austin, TX

Canyon View Medical Group
Springville, UT

Catalyst Medical Group
Lewiston, ID

Granger Medical Clinic
West Valley City, UT

Kansas Medical Center
Andover, KS

Signature Medical Group
St. Louis, MO

Tanner Clinic
Layton, UT

The Doctors' Clinic
Salem, OR

The Lexington Clinic
Lexington, KY

The Oregon Clinic
Portland, OR

Other Specialties

Alyeska Vascular Surgery
Anchorage, AK

Austin Diagnostic Clinic
Austin, TX

Balboa Nephrology
La Jolla, CA

Cancer Specialists of North Florida*
Jacksonville, FL

Cascade Brain & Spine
Bellingham, WA

Center for Neurosciences
Tucson, AZ

Central Park Ear, Nose & Throat
Arlington, TX

Charleston ENT
Charleston, SC

Dallas Nephrology Associates
Dallas, TX

Endoscopy Center of Ocala*
Ocala, FL

ENT Center of Utah
Salt Lake City, UT

Mayfield Brain & Spine
Cinciannati, OH

Metrolina Nephrology Associates
Charlotte, NC

Nephrology Associates
Nashville, TN

North Atlanta Vascular Clinic & Vein Center
Suwanee, GA

North Carolina Eye, Ear, Nose & Throat*
Durham, NC

Northeast Georgia Diagnostic Clinic
Gainesville, GA

Ogden Clinic
Ogden, UT

Ohio ENT & Allergy Physicians
Columbus, OH

Orlando Aesthetic Institute
Orlando, FL

Premier Family Medical
Pleasant Grove, UT

Southern Oregon Neurosurgical & Spine Associates
Medford, OR

Utah Cancer Specialists
Salt Lake City, UT

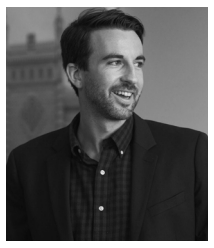
Wake Internal Medicine Consultants
Raleigh, NC

Willamette ENT
Salem, OR

Women's Healthcare Associates
Portland, OR

*** Returning Clients**

The Top 4 Benefits of Independent Physician Groups Owning Their Real Estate



James Winchester
Principal

In the rapidly evolving healthcare landscape, independent physician groups face numerous challenges, from regulatory changes to shifting patient demographics. One strategic move that can significantly benefit these groups is owning the real estate from which they practice. Here are four compelling reasons why physician groups should consider this investment:

1. Control of Practice Destiny

Owning the real estate allows physicians to have full control over their practice environment. This control translates to stability and the ability to make long-term strategic decisions without the uncertainty of landlord demands or lease renewals. When a physician group owns their property, they can tailor the space to their specific needs, whether that involves expanding the facility, incorporating state-of-the-art medical technology, or redesigning the patient flow for better service delivery. This control can become particularly important in markets where space is in low supply and competitors, particularly hospitals and health systems, seek to enhance their strategic position, sometimes at the expense of private practices.

Moreover, ownership ensures that the practice can remain in an established location that is convenient for their patient base, avoiding disruptions caused by potential relocations. This permanence can enhance patient loyalty and trust, as patients appreciate continuity in their healthcare providers.

2. Providing an Attractive Risk-Adjusted Return

Real estate ownership is not only about operational control; it's also a sound financial strategy. Owner-occupied medical real estate can provide an attractive risk-adjusted return, typically boasting annualized returns of between 15% - 20% and therefore outperforming other types of investments over the long term. Debt financing is particularly attractive for private practices as banks can provide better-than-market rates due to the low risk and desire to form depository relationships with the underlying practice. Physician groups can also benefit from property appreciation, creating a valuable asset on their balance sheet.

There's a reason that banks perceive these investments as low risk, and that's primarily because they are driven by the underlying leases that are signed by the practice. As long as the practice is able to afford the leases, the likelihood of default or property depreciation is significantly lowered.

Additionally, real estate investments offer tax advantages, such as depreciation and mortgage interest deductions, which can improve the overall financial health of the individual. By owning their property, physician groups can build equity and wealth, rather than simply paying rent to a landlord.

3. Ancillary Revenue to Attract New Physicians

Ownership of medical office real estate can generate ancillary revenue streams, which can be a powerful tool in attracting new physicians to the practice. This ancillary revenue is typically not offered by competitors and over the lifespan of their practice can result in a meaningful increase in the physician's net worth.

These revenue streams not only bolster the financial position of the group but also enhance the overall service offering, making the practice more attractive to prospective physicians. New doctors often seek out practices that offer stability, growth potential, and opportunities for ancillary income, all of which are facilitated by real estate ownership.

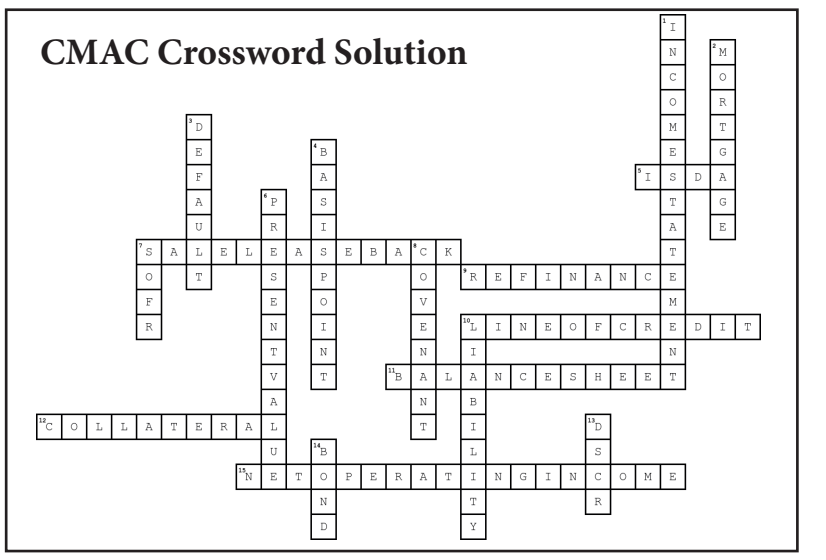
4. Creation of a Retention Tool to Provide Practice Glue

Physician turnover can be costly and disruptive. Real estate ownership can act as a powerful retention tool, creating "practice glue" that binds physicians to the group. When physicians have a stake in the ownership of their practice's real estate investments, they are more inclined to commit to the practice for the long term.

This sense of ownership fosters a collaborative environment where physicians are invested not only in their own success but in the success of the entire group. Shared ownership can lead to a more cohesive team, reducing turnover and ensuring continuity of care for patients. Additionally, the financial benefits of ownership, such as property appreciation and rental income, can serve as a significant incentive for physicians to stay with the practice.

Owning the real estate from which they practice provides private physician groups with substantial advantages. From controlling their practice destiny and ensuring financial stability to attracting new talent and retaining existing physicians, the benefits are clear. As the healthcare environment continues to change, physician groups that strategically invest in real estate will be better positioned to thrive and deliver exceptional patient care.

CMAC Crossword Solution



Physician-Owners Gather at The Broadmoor to Optimize Their Real Estate

CPOMP
CONGRESS OF PHYSICIAN-OWNED MEDICAL PROPERTIES

CPOMP (Congress of Physician-Owned Medical Properties) is a membership organization for independent medical groups that own or plan to own/develop their practice facilities. Physician-owners and C-level executives from these groups have access to a collaborative network of connections and resources to optimize real estate investment outcomes for physician partners.

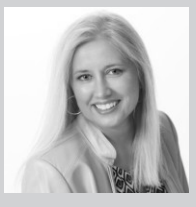
The CPOMP 2024 Annual meeting saw a 60% increase in attendees from the previous year with nearly 100 groups of varying specialties represented. Physician and executive attendees met at The Broadmoor in Colorado Springs, CO to focus on topics such as:

- Physician-Owned Real Estate 101,
- Optimizing Consensus for the Ultimate Operating Agreement, and
- Anatomy of Joint Venture Proposals.

In addition to the interactive and impactful discussions, attendees and their plus-ones enjoyed picturesque mountain views during the evening receptions and a scenic hike at the Garden of the Gods.

Join your peers as they return to The Broadmoor in Colorado Springs for the 2025 Annual Meeting from **September 11th to 13th, 2025**. Register at www.CPOMP.org.

What CMAC Clients Have to Say...



I am very appreciative of the guidance we received and the many conversations guiding us and answering questions. Looking forward to the continued relationship.

Tricia Schildhouse, Practice Administrator
Shoreline Orthopaedics

Thank you so much for your support and assistance with the WIU refinancing. There is no doubt we would not have been nearly as successful without your support – I will absolutely keep CMAC in mind for future endeavors and potential alignments.

Ali Coenen, Executive Director
Wisconsin Institute of Urology

It has been an absolute joy to work with you both along with the CMAC team. You guys made this deal possible and helped so much in the cat wrangling that always accompanies major change.

Renee Weaver, former Finance Dircetor
Wake Internal Medicine Consultants

Swapping Tides: Turning the Rate Game in Your Favor

Chris Tollinchi
Principal

Economic conditions ebb and flow like the tides, and interest rates are no exception. As the rate environment shifts, it's crucial to consider the various instruments available to lock in your rate or hedge your exposure. For borrowers, the likelihood of prepayment should always be top of mind when choosing among rate-fixing products.

Generally, internally fixed rates come with a step-down prepayment penalty. On the other hand, an interest rate swap, which synthetically fixes the rate, involves a two-way make-whole provision. A more sophisticated option is the interest rate swap collar. Unlike a fixed rate, a swap collar binds the rate within a range of a minimum and maximum rate; for example, having 5% as the maximum rate and 4% as the minimum. This involves buying a cap (the upper limit) and selling a floor (the lower limit). While a swap collar may have a slightly higher upfront expense, it often results in lower costs if the hedge is unwound before maturity (breakage).

When dealing with derivatives or swaps, having an experienced advisor by your side is crucial to navigate these complex waters effectively. Here is how it played out for one of our clients recently:

Case Study:
Tallahassee Orthopedic Clinic

An orthopedic practice was interested in a collar due to the lower breakage costs because prepayment during the term was a real possibility. The bank provided an indicative trading level for a costless collar, setting a strike price of 4.75%. Initially, the floor rate was quoted at 3.25%. When the execution call took place, however, the bank attempted to increase the floor rate to 3.45%, which would have cost the borrower an additional $60,000 for a notional loan amount of $4.8MM.

The markets had been flat and trading conditions were static over the preceding days. Fortunately for the borrower, they had CMAC Partners in their corner, monitoring the trade closely. With some smooth talking, CMAC was able to successfully negotiate a refreshed quote which traded much closer to the initial indicative level.

This scenario underscores a vital point: while derivative products, in this case interest rate swap collars, offer significant opportunities to hedge risk and exposure in volatile economic climates, they also present chances for banks to profit at your expense. Staying vigilant and consulting with a knowledgeable swap advisor can make a substantial difference in securing favorable terms.

The Importance of Conducting a Sell vs. Hold Analysis for Owner-Occupied Medical Real Estate

Shannon Stocker
Physician Liaison

Owner-occupied real estate often represents a significant portion of an individual's or a company's assets. While the common notion is to hold onto real estate for the long term, there are situations where selling might be the wiser decision. Understanding when to sell versus when to hold is crucial for maximizing returns and optimizing investment portfolios. This article delves into the importance of conducting a thorough sell versus hold analysis for owner-occupied real estate.

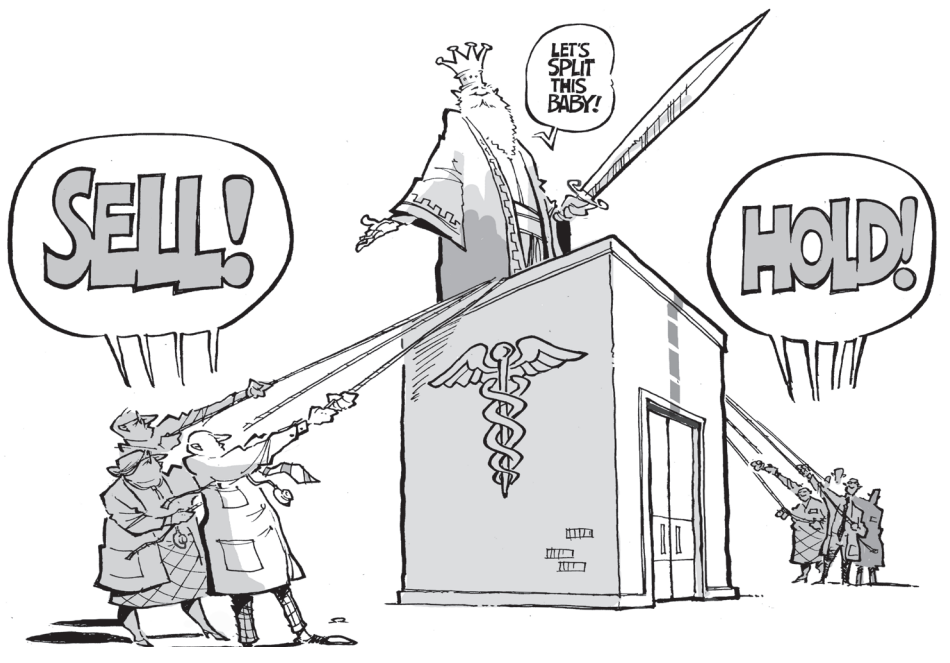
1. Financial Evaluation:

The first step in determining whether to sell or hold a property is conducting a comprehensive financial evaluation. This evaluation involves assessing factors such as the current market value, the potential equity gain that may be anticipated from debt repayment and property appreciation, the projected cash flows and distributions, among other items. Comparing these aspects against the owner's financial goals and objectives can provide insights into whether selling or holding would be more economically advantageous.

2. Market Conditions:

Market conditions play a significant role in the decision-making process. A booming real estate market might present an opportune time to sell, especially if the property has appreciated substantially. Conversely, during a downturn, holding onto the property until market conditions improve might be the prudent choice. Monitoring trends in the local real estate market, including supply and demand dynamics, interest rates, and economic indicators, can help inform the decision.

3. Demographic Changes:



For owner-occupied real estate, demographic changes can influence the decision to sell or hold onto a property. Factors such as customer base relocation, surgery center vicinity, physician commutes or changing business needs may necessitate a reassessment of the property's suitability. In such cases, selling the property and reinvesting in a more suitable alternative or downsizing could be the optimal strategy. In instances such as these, it may be worth evaluating whether selling with a long-term lease obligation is in the practice's best interest.

4. Opportunity Cost:

Understanding the concept of opportunity cost is essential when weighing the decision to sell versus hold real estate. Holding onto a property ties up capital that could be deployed elsewhere for potentially higher returns. Conversely, selling a property prematurely could mean missing out on future appreciation or rental income. Conducting a comparative analysis of the potential returns from alternative investment opportunities can shed light on the opportunity cost of holding or selling the property.

5. Tax Implications:

Tax considerations can heavily influence the decision-making process. Selling a property may trigger capital gains taxes, depreciation recapture, and other tax liabilities. It's also essential to not only factor the tax implications on the real estate owners, but the practice as well. For example, a sale often triggers an increase in property taxes, which often flow through to the tenants in a NNN lease. On the other hand, holding onto the property may offer tax advantages such as depreciation, deductions for mortgage interest and opportunities to receive tax deferred debt financed distributions. Consulting with tax professionals to assess the tax consequences of selling versus holding is crucial in making an informed decision.

6. Risk Management:

Risk management is another critical aspect to consider. Real estate assets are subject to various risks, including market volatility, property damage, tenant turnover, and regulatory changes. Assessing the risk profile of the property and evaluating risk mitigation strategies can help owners determine whether selling or holding aligns with their risk tolerance and investment objectives.

In conclusion, conducting a sell versus hold analysis is imperative for maximizing returns and optimizing the performance of medical owner-occupied real estate. By evaluating financial metrics, market conditions, demographic changes, opportunity costs, tax implications, and risk factors, owners can make well-informed decisions that align with their objectives. Whether it's capitalizing on market opportunities, adapting to changing circumstances, or managing risk, the importance of a thorough sell versus hold analysis cannot be overstated in the realm of real estate investment.

A Sportsbook's Guide to Locking in Interest Rates

Comparing a Mahomes Injury to Rate Cuts

Greg Warren
Managing Partner

Noah, my grandson at Indiana University, is a sports betting whiz but knows nothing about the strategy of locking in interest rates early. So, when I tried to explain how the market sets forward rates and why those rates are unaffected by anticipated changes, he repeated it back to me using terms that he was familiar with. It made a great deal of sense, and I might start having him do the explanations to our clients.

"Let me help you out, Grandpa. Say that Patrick Mahomes gets injured in a game and the doctors say he will be out for two weeks. It so happens that the Chiefs are supposed to play the Jets in four weeks and, following the injury and prognosis, the bookmakers have installed the Chiefs as a 7-point favorite. Suppose that you really like the Jets and think getting seven points would be a great bet. The question is whether you should place your bet now and take the seven or wait until Mahomes is activated again figuring his return will increase the spread for the Chiefs and give you more points. Hey Grandpa, if you like the points now, take them. If everything goes as planned, the spread at gametime will still be seven points because the bookies are already figuring that Mahomes will be playing. If you don't take the points now, it could go against you."

Let's repeat Noah's scenario but substitute Mahomes with Jerome Powell and a rate cut in place of a return from injury. We end up at the same place. Through his remarks, Powell has indicated rate cuts over the next two years. Based on those expectations, the market has already priced forward starting rates and if the projections hold true, those rates will be the same when you go to set in two years as they would be if you set those rates today (to start in two years).

Now, assume you are building a project and wish to fix a rate for seven years at the end of construction in two years. You are also expecting short-term rates to drop during that period. If the

Fed cuts as projected and its forecast is unchanged, those rates you could have fixed today will not fall because those cuts have already been factored in, just as Mahomes return from injury had been factored in. If you like the rate today, lock it in.

To Do Nothing is to Speculate

That may seem a bit counterintuitive but consider this; if you act now, you remove all the variables that could occur over the next two years. You are grabbing the proverbial bird in the hand. By waiting, you open yourself up to the unknowns. Maybe the Fed cuts in the two years will be steeper than projected and the 7-year rates will be less at that time. However, the Fed could also stop the cuts or even raise rates in that two years and the 7-year fixed rate would be much higher.

The bottom line is simply to understand that the forward rates have been established with expectations built in. Waiting may work for you or against you and the group really needs to ask itself if it can afford the downside.

In our experience, a group of doctors building an office from which to practice are not speculators. They want to know what their rent will be and having to up it by $4 psf because a rate unexpectedly moved from what it was earlier is not a viable alternative. It is an outcome that can be avoided by "not speculating" and acting sooner rather than later.

All that said, I really don't understand parlays and I am hoping Noah will be patient with me.

Ever Heard of Diversifying Your Portfolio?

How Cash Out Refinances Can Help You Build Wealth & Diversify Income Streams

Grant Blackhurst
Principal

If you were to ask any financial advisor for their golden rules when investing, there's a good chance almost all of them would include diversification near the top of their lists. Diversification is the most effective means of managing risk. By spreading out investments over a variety of assets you're less likely to have your investment portfolio wiped out due to one negative event. As the timeless adage goes, don't put all your eggs in one basket. But how can executing cash out refinance transactions help in diversifying your investment portfolio even further, and how can it be utilized to effectively mitigate your risk?

For those frequent readers of our physician-owned real estate journal, you may remember an article from one of our pervious editions, which talked about how the practice drives the real estate investment. This is vital to remember as we talk about the risks associated with these owner-occupied investments. As long as the practice continues to lease the space and can keep up with the rent payments, the real estate risk is minimal. This remains true even for highly leveraged properties, as the rents are set high enough to cover the loan payments and then some in these cases. The moment this changes, and the practice is unable or unwilling to pay the rent on the property, the real estate risk grows substantially. If the world turned upside down, and your practice was unable to pay the rents, the property would substantially decline in value. That is to say, a vacant building is worth a fraction of the value of a fully leased property.

The question therefore becomes, are you better off having a lot of equity locked in that property or are you better off using that equity – through a cash out refinance – and investing it in assets that aren't tied to the practice's wellbeing? When pondering this question, it's important to recognize that if the practice is unable to pay the rents, it's likely the practice is struggling. and it's the practice that was likely your primary source of income. Then, if these events were to unfold, not only would you lose this income, but you would also lose a substantial amount of your net worth stored as equity in the property. In these situations, the bank would either repossess the property or you'd sell the property at a substantially reduced value.

A cash out refinance event would allow the group to distribute cash to the partners from the equity that's accumulated over the years, while still enabling the partners to retain ownership in an investment that's likely yielding a very attractive return. More than that, the cash out refinance would actually enhance the return on investment that's being generated by the property itself. This means the equity you do have stored in the property starts working even harder for you. And, as we highlighted earlier, taking on this additional debt is usually a fairly low risk proposition assuming the practice continues to use this space and is able to pay the rents. Moreover, in instances where there are no personal guarantees on the debt, the risk is mitigated even further.

This debt financed distribution (cash out refi) is also typically a tax deferred transaction, which allows the group to kick the tax can down the road so to speak and build additional wealth on the money that's been stripped out. To use a back of the napkin calculation, if you're able to reinvest that money at a better return than you're receiving on your new real estate loan, there's a strong chance that you're going to be accumulating more wealth than you would have done if the equity had remained stored in the property. Moreover, if you've invested that money in various different assets such as stocks, other real estate properties, savings accounts to name just a few, you've amassed a good number of additional wealth generating assets that aren't tied to the practice's success and protected yourself from one negative event potentially derailing your retirement plans.

The CMAC Team would like to thank its readers. We hope this newspaper serves as a valuable resource to you and your physician-owned practice.

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CMAC Partners

CMAC Hits 20! *Two Decades of Empowering Independent Physicians*

By Greg Warren, Founder

In 2004, I announced to my wife, Diane, that our future together would now include one retired husband. Tears welled in her eyes. Wow, I thought, this has overjoyed her, and she's thinking about all the time we'll now spend together in our home in Winter Park, FL. Well, I was right on that second part. Those forthcoming tears were not of joy but of anxiety. It was something like, "Greg, we have now had 40 glorious years of marriage. Why mess up something that has gone so well?" I'm not kidding. Even today after 60 years of marriage, when people ask Diane the secret to our union's longevity, she replies, "He travels." And so CMAC Partners was born.

Rather than some long-winded article detailing our history, I thought a few highlights and some pictures would be far more entertaining. It sounds better in the third person, so here we go.

2004 – 2006

Greg Warren is introduced to a loan officer at AmSouth Bank who had pulled together 22 clients to create a single borrower under a Variable Rate Demand Bond (VRDB) using letters of credit – a less expensive way to borrow. He attempts to emulate this remarkable scenario but fails miserably and can't even bring two borrowers together. Greg then meets Peter "The Messiah" Allport of Wachovia Bank who advocates the same VRDB structure on a one-off basis. Voila, CMAC's in business.

CMAC stands for Capital Markets Access Company (mystery solved!) because the bonds were auctioned in the capital markets.

Initially, CMAC had no idea it was headed towards a focus in healthcare until Greg visited his cardiologist for an annual checkup. A simple "how'd you finance your building" turned into CMAC's first closing.

Greg is then introduced to Shannon Stocker. A recent medical school graduate unable to move forward in medicine because of her own health challenges, Shannon teams with Greg and the road to physician-owned real estate is set.

Soon after, Liz Allport, a commercial loan officer who previously worked at Bank of New York on Wall Street and is currently on a kid-raising hiatus, joins the team. Liz brings the experience, the knowledge, and the whip! CMAC finally starts to operate like a business.

Steve Pishko, a University of Florida graduate comes on board and the team is complete. Steve eventually leaves to form his own company but the original three are still a part of CMAC's fabric 20 years later.

2007 – 2018

The 2008 economic upheaval renders the bond market illiquid and seems to signal CMAC's demise. Instead, CMAC creates an additional revenue stream assisting borrowers to negotiate and execute interest rate swaps through a division know as Swap Negotiators. This effort was so successful that it not only kept the doors open but brought CMAC an unexpected 15 minutes of fame when the *New York Times* featured Swap Negotiators as the headline in its Sunday Business section.

Steady growth followed as word of mouth brought new clients across the United States.

2017 - 2023

The "newbies" come in and take CMAC to the next level. CMAC's role as physician advocates expands into real estate structuring and optimizing the profitability and sustainability of those entities.

James Winchester and Chris Tollinchi emerge as the next-generation leaders.

2024

The majority of the CMAC Partners ownership is acquired by its employees. Buckle up for what should be one helluva ride to the next level!!

CMAC Partners 2004 - 2024

Greg Warren
Managing Partner
2004

Shannon Stocker, MD
Physician Liaison
2004

Liz Allport
EVP of Finance
2004

Peter Kokins
Director of Business Development
2013

Chris Tollinchi
Director of Finance
2016

Elizabeth Cvercko
Director of Marketing
2018

James Winchester
Lead Financial Strategist
2018

Ha Tran
Finance Project Manager
2019

Mariela Araujo
Senior Analyst
2020

Grant Blackhurst
Senior Analyst
2020

Jasmine Garcia
Marketing Coordinator
2024