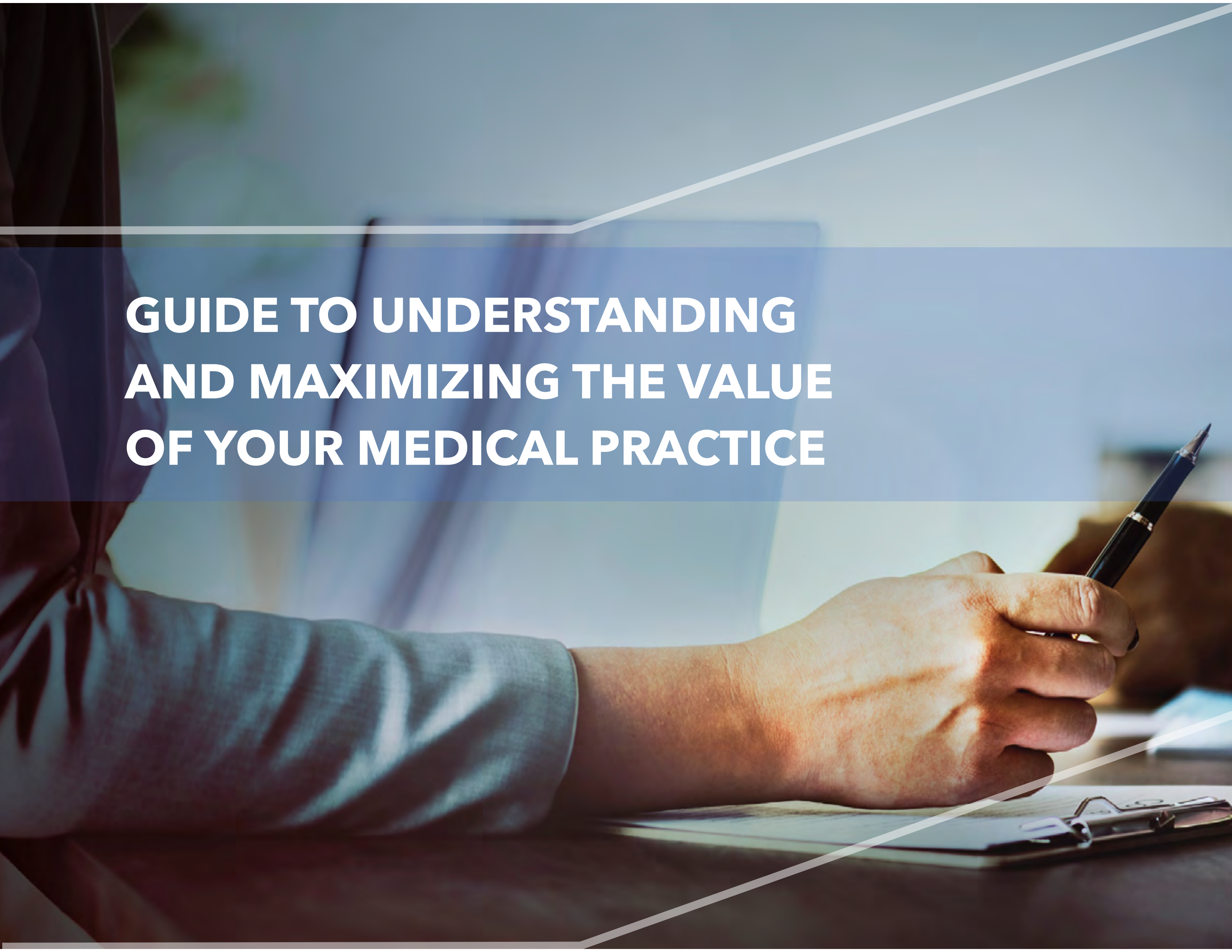

GUIDE TO UNDERSTANDING AND MAXIMIZING THE VALUE OF YOUR MEDICAL PRACTICE

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WHAT'S YOUR NEXT STEP?

Whether you are considering selling your practice, or you want to explore the potential of selling or taking on an investor, the first step is to get your practice in the best operational and financial shape possible.

We created this Guide to Maximizing the Value & Sale of Your Practice to help you understand your options and take the right steps for the future of your practice —and your life goals.

The content is organized to take you step-by-step from strategic planning through maximizing revenue and financial housekeeping.

THINKING ABOUT SELLING YOUR PRACTICE?

The thought of selling your healthcare practice can spark many questions:

- Should I sell my practice?
- Why would I sell? Do I want to retire or stay in practice and increase cash flow?
- When is the best time to sell?
- How do I get ready to sell my practice?
- What can I do now to maximize profit?

Your first step is to answer these questions before you embark on the process of selling or securing an investor.

Some of the questions will reflect your personal goals and desires.

This guide is intended to help you answer the other questions and take the first steps to reaching your goals.

> *"The best time to sell is when your practice is successful; not when it's underperforming and you're tired of trying to keep it afloat."*

What do investors look for when buying a healthcare practice?

Buyers and investors look for high-functioning, low-cost, efficient practices that maximize revenues with:

- A good location
- An experienced staff
- Operational efficiencies
- A well-established patient base

The better financial and physical shape your practice is in, the more attractive it will be to investors.

Even if you simply want to explore the options and benefits of selling in the future, it makes sense to get your practice in the best operational and financial shape possible (see page 4).

Whatever your goals for your practice, the best way to maximize your value or your sale price is to optimize your operations. That's what this guide will help you do!

FIVE STEPS TO MAXIMIZE YOUR VALUE AND PRACTICE SALE PRICE

1 Develop a Strategic Plan

You'll want to start by setting benchmarks for the next 2+ years to strengthen your position in your marketplace. Be sure you recognize the difference between your actual value and your potential value.

Just because your practice may have the potential to tap into new markets and increase revenue, doesn't mean your buyer is going to pay you the associated value. You'll need to create actual value to ensure you receive the full value of your practice during the sale. Implement efforts to:

- Increase your marketing activities
- Increase your patient base
- Investigate new vertical and horizontal service line opportunities

2 Achieve Operational Excellence

A key to receiving obtaining the maximum price from the sale of your practice is offering a top-performing healthcare practice to the market. You'll want to implement initiatives to address any issues related to your practice's operational throughput, staffing alignment, staff education, coding and billing education. (See **How to Optimize Your Practice Operations** on pg. 6.)

3 Track Results

When you develop your strategic plan, you'll need to identify Key Performance Indicators (KPIs) that will be used to measure your progress on increasing your practice's value. On a monthly basis, you should monitor your KPIs. These indicators could be overhead costs, financial transparency, patient retention or new referrals, etc.

If you need assistance in creating and tracking the right KPIs for your business, H&N Consulting can help. Contact us at info@hnhealthconsult.com

4 Create Financial Balance

When it comes to attracting the best buyer or investor, financial balance is critical. Of course, getting your practice in the best financial shape possible is important even before you think of selling. Balance is created by controlling costs and maximizing revenue.

H&N Consulting finds that **controlling costs** and **increasing revenue** helps clients achieve healthier financial balance - whether you are preparing to sell or simply looking to improve operational efficiency and business value.

5 Understand Practice Value

As you get ready to sell, make sure you understand your value. A practice valuation expert can advise you on what to ask for and why, as well as guide you through the various buying models that exist today.

Don't wait until you have an offer on the table! The sooner you understand the true worth of your practice, the sooner you can improve your value to maximize your sale price.

How Is Value Determined?

Just like in any other business, valuations are based on a multiple of Earnings Before Interests, Taxes, Depreciation, and Amortization (EBITDA). Every time you spend a dollar, ask yourself if your return on that dollar will produce enough of a benefit by the time you're ready to sell. If not, then don't spend the money if at all possible.

HOW TO OPTIMIZE YOUR OPERATIONS BEFORE SELLING

Whether you are considering selling now or in the future, or you want to improve profitability for yourself, start by get your practice in the best operational and financial shape possible. Here are five actions you can take now to help ensure the financial health of your practice.

1. Reduce payroll expenses

Here are three primary ways you can reduce your practice's overall payroll expenses.

Cut overtime. Overtime can be a huge drain on practices and having a zero tolerance policy can reduce your payroll costs substantially. One H&N client reduced annual payroll costs by 14% by implementing a zero-overtime policy. If you routinely pay overtime, read this resource: "Don't Let Overtime Take Over."

Adjust staffing levels. Are your schedules templates designed to maximize productivity or do you find your resources stretched at certain times of the day? Altering your staffing schedules can help control costs.

For example, rather than having your entire staff begin work at the same time every day, consider staggering start times to ensure you are appropriately staffed for your busy periods. You should also look to see if you can convert one or more staff positions from full-time to part-time.

Maximize your providers' time. Think about what you can do to maximize your physician and AAP's schedules. Where can you decrease payroll costs on your most expensive resources, or fill that time more wisely? For example, an H&N client hired a nurse practitioner while the physicians still had room in their schedules to grow.

2. Trim material costs

Look at your supply and waste management costs. If you haven't looked closely at these expenses in the last 6-12 months, chances are you are leaving money on the table that can be put back into your pocket.

How?

Ask your suppliers how you can take advantage of better pricing. Are there discounts for volume or prompt payment? Let them know that you are shopping around for the best deals. Frequently suppliers will reduce prices to retain your business.

If you are not already participating in a buying group, investigate your available options and sign up right away to take advantage of group volume discounts.

Explore extending your service contracts and leases on equipment or real estate. This can reduce monthly costs and your practice's overhead costs.

Be sure all of your service contracts, equipment and real estate leases are acquired as part of the sale of your practice.

3. Maximize revenues by coding for everything you do

Many practices leave money on the table because they only code what they know, rather than everything they do. Additionally, they don't code for services that usually do not get paid. Coding for everything that you do allows you to:

- Take advantage of payers' changing policies – What was not covered yesterday might be paid tomorrow.
- Have patients share in the cost of their care by billing them for non-covered services, ABN's and waivers.
- Demonstrate the value of the services that you provide to a buyer.

4. Collect every dollar possible

Do not waive copays and coinsurance! Apart from breaching your payer contracts when you do this, you are also further discounting your services.

Remember when you join a payer network, you agree to a reduced payment. They pay you a portion of that discounted fee and the patient is supposed to pay the remainder of your fee.

For example: Let's say your charges are $150 for a 99213, and the payer fee schedule is $120. If a patient has a $20 copay, the payer will give you $100. You may think that's giving a $30 discount to the payer, but if you don't collect the patient's $20 copay, you are providing an overall discount on that service of $50 – one third of your charge!

Make it easy for patients to pay you. Accept credit and debit cards, checks, and cash. If possible, set up payment plans and tie them to credit cards.

Keep credit cards on file (using secure processes which meet legal requirements, of course) and automatically balance-bill patient responsibility fees.

Have patients sign waivers for non-covered services that they request. Most payers allow you collect payment on services that are not covered by benefits, provided that the patient has been fully informed and signed a waiver stating that they understand their liability for payment for those services.

5. Financial Housekeeping

Review your unpaid accounts receivable and collect those in arrears. This will not only help your cash flow in the short term, but it also will give you a better picture of exactly where your practice stands in the event of a sale. You don't want those old, un-collectable A/R bloating your books.

Don't wait until you are starting the sales process to take steps to maximize the value of your practice and organize for a smooth and profitable sale.

Even a few improvements can result in a big payoff when it comes time to sell!

QUICK REFERENCE CHECKLIST FOR SELLING YOUR PRACTICE

Our Checklist to Help You Maximize the Value of Your Practice and Prepare to Sell Your Practice

Contain & Control Payroll Expenses

- Keep overtime to a minimum (or eliminate it entirely).
- Flex your staffing hours.
- Implement scheduling to maximize every physician's productivity.

Trim Operational & Supply Cost

- Review and negotiate your leases on equipment and maintenance, as well as vendor and service contracts annually.
- Join a buying group.

Maximize Revenue

- Work smarter, not harder! Document and code for every service you perform.
- Bill in a timely manner.
- **Know your numbers**
  - days to bill
  - days in Accounts Receivable
  - dollars in Accounts Receivable buckets
  - number of patients you need to see to cover overhead on a daily basis
  - average revenue per patient
  - payer mix percentages
- Negotiate your payer contracts
- Investigate limiting your payer mix.
- Report quality metrics.
- **Make it easy for the patient to pay**
  - accept all forms of payment
  - provide payment plans
- Collect all co-pays up front.
- Ensure necessary pre-authorizations.
- Obtain ABNs when appropriate for non-covered services.
- Balance bill patients.
- Limit or decline professional and family discounts.
- Keep no-shows to a minimum: hold patients accountable.
- Work all denials and underpayments.
- Develop a collection policy.
- Decide what to do and how to deal with unpaid Accounts Receivable.

Gather Your Business Operations Information

As you begin the conversation about selling your practice, your buyer or investor will ask for the following confidential items that are part of your routine business operations. **Don't wait until you start the sales process to gather these details:**

- ✓ Your Primary business and any affiliates corporate name(s)
- ✓ Type of Business/Practice: Specialties and customer
- ✓ Addresses of primary location (and any satellite locations)
- ✓ Year your company was founded
- ✓ Corporate structure (C, S, LLC, etc.)
- ✓ Owner name(s) and ownership percentage
- ✓ Copy of current YTD and past 2 years' Financial Statements and Balance Sheets
- ✓ Copy of YTD monthly deposit report
- ✓ List of procedures/services offered and YTD Revenue percentage for each
- ✓ Name of billing software
- ✓ List of Physicians and AAPs
- ✓ Real Estate lease information
- ✓ List of all you payer (CMS, insurance and ACO) contracts
- ✓ Owner's compensation and benefits for prior year and current YTD

GLOSSARY OF TERMS

Related to Venture Capital and Private Equity

A-C

-A-

Adjusted EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) is a measure computed for a company that looks at its "top line" earnings before deducting interest expense, taxes and depreciation charges. It is used to compare related companies and for purposes of valuation.

Advisory Board: A group of external advisors to a private equity group or portfolio company. Advice provided varies from overall strategy to portfolio valuation. Less formal than a Board of Directors.

Amortization: An accounting procedure that gradually reduces the book value of an intangible asset through periodic charges to income.

Angel Financing: Capital raised for a private company from independently wealthy investors. This capital is generally used as seed financing.

Angel Fund: A formal or informal assemblage of active angel investors who cooperate in some part of the investment process. Key characteristics of an angel group are: control by member angels (who manage the entity or have control over the entity's managers), and collaboration by member angels in the investment process.

Angel Investing: An angel investor is an individual who makes direct investments of personal funds into a venture, typically early-stage businesses. Because the capital is being invested at a risky time in a business venture, the angel must be capable of taking a loss of the entire investment, and, as such, most angel investors are high-net-worth individuals. These individuals are nearly always "accredited investors" as defined under the Securities Act of 1933.

-B-

Balance Sheet: A condensed financial statement showing the nature and amount of a company's assets, liabilities, and capital on a given date.

Book Value: Book value of a stock is determined from a company's balance sheet by adding all current and fixed assets and then deducting all debts, other liabilities, and the liquidation price of any preferred issues. The sum arrived at is divided by the number of common shares outstanding, and the result is book value per common share.

Bridge Financing: A limited amount of equity or short-term debt financing typically raised within 6-18 months of an anticipated public offering or private placement meant to "bridge" a company to the next round of financing.

Burn Rate: The rate at which a company expends net cash over a certain period, usually a month.

Business Plan: A document that describes the entrepreneur's idea, the market problem, proposed solution, business and revenue models, marketing strategy, technology, company profile, competitive landscape, as well as financial data for coming years. The business plan opens with a brief executive summary, most probably the most important element of the document due to the time constraints of venture capital funds and angels.

-C-

CAGR: Compound Annual Growth Rate. The year-over-year growth rate applied to an investment or other aspect of a firm using a base amount.

Capital (or Assets) Under Management: The amount of capital available to a fund-management team for venture investments.

Capital Gains: The difference between an asset's purchase price and selling price, when the selling price is greater. Long-term capital gains (on assets held for a year or longer) are taxed at a lower rate than ordinary income.

Capitalize: To record an outlay as an asset (as opposed to an expense), which is subject to depreciation or amortization.

Carried Interest or "Carry": The portion of any gains realized by the fund to which the fund managers are entitled, generally without having to contribute capital to the fund. Carried interest payments are customary in the venture capital industry, in order to create a significant economic incentive for venture capital fund managers to achieve capital gains.

-C-

Cash Position: The amount of cash available to a company at a given point in time.

Clawback: A clawback obligation represents the general partner's promise that, over the life of the fund, the managers will not receive a greater share of the fund's distributions than they bargained for. Generally, this means that the general partner may not keep distributions representing more than a specified percentage (e.g., 20%) of the fund's cumulative profits, if any. When triggered, the clawback will require that the general partner return to the fund's limited partners an amount equal to what is determined to be "excess" distributions.

Closing: An investment event occurring after the required legal documents are implemented between the investor and a company and after the capital is transferred in exchange for company ownership or debt obligation.

Co-investment: The syndication of a private equity financing round or an investment by an individual (usually general partners) alongside a private equity fund in a financing round.

Collar Agreement: Agreed-upon adjustments in the number of shares offered in a stock-for-stock exchange to account for price fluctuations before the completion of the deal.

Committed Capital: The total dollar amount of capital pledged to a private equity fund.

Common Stock: A unit of ownership of a corporation. In the case of a public company, the stock is traded between investors on various exchanges. Owners of common stock are typically entitled to vote on the selection of directors and other important events and in some cases receive dividends on their holdings. Investors who purchase common stock hope that the stock price will increase so the value of their investment will appreciate. Common stock offers no performance guarantees. Additionally, in the event that a corporation is liquidated, the claims of secured and unsecured creditors and owners of bonds and preferred stock take precedence over the claims of those who own common stock.

Corporate Charter: The document prepared when a corporation is formed. The Charter sets forth the objectives and goals of the corporation, as well as a complete statement of what the corporation can and cannot do while pursuing these goals.

Corporate Resolution: A document stating that the corporation's board of directors has authorized a particular individual to act on behalf of the corporation.

Corporate Venturing: Venture capital provided by [in-house investment funds of] large corporations to further their own strategic interests.

Corporation: A legal, taxable entity chartered by a state or the federal government. Ownership of a corporation is held by the stockholders.

Covenant: A protective clause in an agreement.

-D-

Debenture: A debt instrument; basically, the same as a Promissory Note.

Debt: Any obligation by one person to pay another. May be a primary (direct) obligation as in a Note, or a secondary (contingent) obligation as in a guaranty.

Depreciation: An expense recorded to reduce the value of a long-term tangible asset. Since it is a non-cash expense, it increases free cash flow while decreasing the amount of a company's reported earnings.

Dilution: A reduction in the percentage ownership of a given shareholder in a company caused by the issuance of new shares.

Director: Person elected by shareholders to serve on the board of directors. The directors appoint the president, vice president and all other operating officers, and decide when dividends should be paid (among other matters).

-D-

Disclosure Document: A booklet outlining the risk factors associated with an investment.
Divestiture: Disposition or sale of an asset by a company. A company will often divest an asset which is not performing well, which is not vital to the company's core business, or which is worth more to a potential buyer or as a separate entity than as part of the company.
Due Diligence: A process undertaken by potential investors "individuals or institutions" to analyze and assess the desirability, value, and potential of an investment opportunity.

-E-

Early Stage: A state of a company that typically has completed its seed stage and has a founding or core senior management team, has proven its concept or completed its beta test, has minimal revenues, and no positive earnings or cash flows.
EBITDA: Earnings Before Interest, Taxes, Depreciation, and Amortization. A measure of cash flow calculated as: = Revenue - Expenses (excluding tax, interest, depreciation, and amortization).
EBITDA looks at the cash flow of a company. By not including interest, taxes, depreciation, and amortization, we can clearly see the amount of money a company brings in.
This is especially useful when one company is considering a takeover of another because the EBITDA would cover any loan payments needed to finance the takeover.
Economies of Scale: Economic principle that, as the volume of production increases, the cost of producing each unit decreases.
Elevator Pitch: An extremely concise presentation of an entrepreneur's idea, business model, company solution, marketing strategy, and competition delivered to potential investors. Should not last more than a few minutes, or the duration of an elevator ride.
Employee Stock Ownership Plan: A trust fund established by a company to purchase stock on behalf of employees.
Enterprise Value (EV) is a measure of a company's total value, often used as a more comprehensive alternative to equity market capitalization.
Equity: Ownership in the capital of a Company. In corporations, it is called "stock"; in limited partnerships or LLCs, it is called "interests" or "units."
Exercise price: The price at which an option or warrant can be exercised.
Exit Strategy: A fund's intended method for liquidating its holdings while achieving the maximum possible return. These strategies depend on the exit climates, including market conditions and industry trends. Exit strategies can include selling or distributing the portfolio company's shares after an initial public offering (IPO), a sale of the portfolio company, or a recapitalization.

-F-

Finder: A person who helps to arrange a transaction.
Founders' Shares: Shares owned by a company's founders upon its establishment.
Free cash flow: The cash flow of a company available to service the capital structure of the firm. Typically measured as operating cash flow less capital expenditures and tax obligations.
Fund Size: The total amount of capital committed by the investors of a venture capital fund.

-G-

GAAP: Generally Accepted Accounting Principles. The common set of accounting principles, standards, and procedures. GAAP is a combination of authoritative standards set by standard-setting bodies as well as accepted ways of doing accounting.

-G-

General Partner (GP): The partner in a limited partnership responsible for all management decisions of the partnership. The GP has a fiduciary responsibility to act for the benefit of the limited partners (LPs) and is fully liable for its actions.

Golden Handcuffs: This occurs when an employee is required to relinquish unvested stock when terminating his employment contract early.

Golden Parachute: Employment contract of upper management that provides a large payout upon the occurrence of certain control transactions, such as a certain percentage share purchase by an outside entity or when there is a tender offer for a certain percentage of a company's shares. This is discussed in more detail at the Executive Employment Agreement.

-H-

Holding Company: A corporation that owns the securities of another, in most cases with voting control.

Holding Period: The amount of time an investor has held an investment. The period begins on the date of purchase and ends on the date of sale and determines whether a gain or loss is considered short term or long term, for capital-gains-tax purposes.

-I-

Independent Practice Association: A U.S. type of physician alliance in which the physicians own the practice, as opposed to physicians employed by an entity such as a health maintenance organization. Physicians in the IPA are legally organized as a corporation, partnership, professional corporation, or foundation to contract as a group to provide services. Economic risk is shared, but overhead is not. The IPA may contract with a health maintenance organization (HMO) to service enrollees, but will usually still see non-HMO clients.

Initial Public Offering (IPO): The sale or distribution of a stock of a portfolio company to the public for the first time. IPOs are often an opportunity for existing investors (often venture capitalists) to receive significant returns on their original investment. During periods of market downturns or corrections, the opposite is true.

Institutional Investors: Organizations that professionally invest, including insurance companies, depository institutions, pension funds, investment companies, mutual funds, and endowment funds.

Investment Letter: A letter signed by an investor purchasing unregistered long securities under Regulation D, in which the investor attests to the long-term investment nature of the purchase. These securities must be held for a minimum of one year before they can be sold.

IRR: Internal Rate of Return. A typical measure of how VC Funds assess performance. IRR is technically a discount rate at which the present value of a series of investments is equal to the present value of the returns on those investments.

-K-

Kentucky Windage: In hunting, the modified aim required to compensate for wind or target movement. Used in investment terms to describe the process by which an investor must increase the percentage he needs today so that he will end up with a desired target percentage ownership in the future, after adjusting for future dilutive financing rounds.

Key Employees: Professional management attracted by the founder to run the company. Key employees are typically retained with warrants and ownership of the company.

-L-

Lead Investor: Also known as a bell cow investor. Member of a syndicate of private equity investors holding the largest stake, in charge of arranging the financing and most actively involved in the overall project.

Leveraged Buyout (LBO): A takeover of a company, using a combination of equity and borrowed funds. Generally, the target company's assets act as the collateral for the loans taken out by the acquiring group. The acquiring group then repays the loan from the cash flow of the acquired company. For example, a group of investors may borrow funds, using the assets of the company as collateral, in order to take over a company. Or the management of the company may use this vehicle as a means to regain control of the company by converting a company from public to private. In most LBOs, public shareholders receive a premium to the market price of the shares.

Limited Partner (LP): An investor in a limited partnership with no voice in the management. LPs have limited liability and usually have priority over GPs upon liquidation of the partnership.

Limited Partnerships: An organization comprised of a general partner, who manages a fund, and limited partners, who invest money but have limited liability and are not involved with the day-to-day management of the fund. In the typical venture capital fund, the general partner receives a management fee and a percentage of the profits (or carried interest). The limited partners receive income, capital gains, and tax benefits.

Liquidation: 1) The process of converting securities into cash. 2) The sale of the assets of a company to one or more acquirers in order to pay off debts. In the event that a corporation is liquidated, the claims of secured and unsecured creditors and owners of bonds and preferred stock take precedence over the claims of those who own common stock.

Liquidity Event: An event that allows a VC to realize a gain or loss on an investment. The ending of a private equity provider's involvement in a business venture with a view to realizing an internal return on investment. Most common exit routes include IPOs, buy backs, trade sales, and secondary buyouts. (See: Exit Strategy.)

-M-

Management Fee: Compensation for the management of a venture fund's activities, paid from the fund to the general partner or investment advisor. This compensation generally includes an annual management fee.

A Management Services Organization (MSO) is a legal entity created to provide management and administrative services to other organizations. For the purpose of this article, we will describe the physician-owned MSO that provides services to multiple independent anesthesiology groups and is owned and governed by the owners of the anesthesiology groups the MSO serves.

Merger: A merger usually involves combining two companies into a single larger company. The combination of the two companies involves a transfer of ownership, either through a stock swap or a cash payment between the two companies.

Multiples. Valuation multiples derived from similar business sales are often used to estimate the likely selling price of a business. These multiples are calculated as ratios which relate some measure of business financial performance to its potential selling price.

Mutual Fund: A mutual fund, or an open-end fund, sells as many shares as investor demand requires. As money flows in, the fund grows. If money flows out of the fund, the number of the fund's outstanding shares drops. Open-end funds are sometimes closed to new investors, but existing investors can continue to invest money in the fund. To sell shares, an investor usually sells the shares back to the fund. If an investor wishes to buy additional shares in a mutual fund, the investor must buy newly issued shares directly from the fund. (See also: Closed-end Funds.)

-N-

Net Financing Cost: Also called the cost of carry or, simply, carry, the difference between the cost of financing the purchase of an asset and the asset's cash yield. Positive carry means the yield earned is greater than the financing cost; negative carry means the financing cost exceeds the yield earned.
Net income: The net earnings of a corporation after deducting all costs of selling, depreciation, interest expense, and taxes.

Net Present Value: An approach used in capital budgeting where the present value of cash inflow is subtracted from the present value of cash outflows. NPV compares the value of a dollar today versus the value of that same dollar in the future after taking inflation and return into account.

No Shop, No Solicitation Clauses: A no shop, no solicitation, or exclusivity, clause requires the company to negotiate exclusively with the investor, and not solicit an investment proposal from anyone else for a set period of time after the term sheet is signed. The key provision is the length of time set for the exclusivity period.

-O-

Offering Documents: Documents evidencing a private-placement transaction. Include some combination of a purchase agreement and/or subscription agreement, notes or stock certificates, warrants, registration-rights agreement, stock-holder or investment agreement, investor questionnaire, and documents required by the particular deal.

Option: A security granting the holder the right to purchase a specified number of a Company's securities at a designated price at some point in the future. The term is generally used in connection with employee benefit plans as Incentive Stock Options ("ISOs" or "statutory options") and Non-qualified stock options ("NSOs" or "Nonquals"). However "stand-alone options" may be issued outside of any plan. Generally non-transferable, in distinction to warrants.

-P-

Partnership: A nontaxable entity in which each partner shares in the profits, losses, and liabilities of the partnership. Each partner is responsible for the taxes on its share of profits and losses.

Partnership Agreement: A contract that specifies the compensation and conditions governing the relationship between investors (LPs) and the venture capitalists (GPs) for the duration of a private equity fund's life.

PIV: Pooled Investment Vehicle. A legal entity that pools various investors' capital and deploys it according to a specific investment strategy.

Private Equity: Equity securities of companies that have not "gone public" (not listed on a public exchange). Private equities are generally illiquid and seen as long-term investments. As they are not listed on an exchange, an investor wishing to sell securities in private companies must find a buyer in the absence of a marketplace. There are many transfer restrictions on private securities. Investors generally receive their return by an initial public offering, a sale or merger, or a recapitalization.

Promissory Note: ("Note") A debt instrument in which the maker promises to pay the holder according to its terms.

-R-

Recapitalization: The reorganization of a company's capital structure. A company may seek to save on taxes by replacing preferred stock with bonds in order to gain interest deductibility. Recapitalization can be an alternative exit strategy for venture capitalists and leveraged-buyout sponsors. (See: Exit Strategy and Leveraged Buyout.)

Right of First Refusal: The right of first refusal gives the holder the right to meet any other offer before the proposed contract is accepted.

Risk: The chance of loss on an investment due to many factors, including inflation, interest rates, default, politics, foreign exchange, call provisions, etc. In Private Equity, risks are outlined in the Risk Factors section of the Placement Memorandum.

-S-

Secondary Sale: The sale of private or restricted holdings in a portfolio company to other investors.
Securities: Includes all types of equity and debt instruments and rights in and to them.
Securities and Exchange Commission: The SEC is an independent, nonpartisan, quasi-judicial regulatory agency that is responsible for administering the federal securities laws. These laws protect investors in securities markets and ensure that investors have access to all material information concerning publicly traded securities. Additionally, the SEC regulates firms that trade securities, people who provide investment advice, and investment companies.
Seed Money: The first round of capital for a start-up business. Seed money usually takes the structure of a loan or an investment in preferred stock or convertible bonds, although sometimes it is common stock. Seed money provides the capital required for initial development and growth. Angel investors and early-stage venture capital funds often provide seed money.
Seed Stage Financing: An initial state of a company's growth characterized by a founding management team, business-plan development, prototype development, and beta testing.
Strategic plan: Strategic planning is an organization's process of defining its strategy or direction, and making decisions on allocating its resources to pursue this strategy. It may also extend to control mechanisms for guiding the implementation of the strategy.
Stock Options: 1) The right to purchase or sell a stock at a specified price within a stated period. A popular investment medium, Options offer an opportunity to hedge positions in other securities, to speculate on stocks with relatively little investment, and to capitalize on changes in the market value of options contracts through a variety of options strategies. 2) A widely-used employee incentive and compensation. The employee is given an option to purchase shares at a certain price (at or below the market price at the time the option is granted) for a specified period of years.
Strategic Investors: Corporate or individual investors that add value to investments they make through industry and personal ties that can assist in raising additional capital as well as provide assistance in the marketing and sales process.

-T-

Takedown Schedule: A takedown schedule means the timing and size of the capital contributions from the limited partners of a venture fund.
Tax-free reorganizations: Types of business combinations in which shareholders do not incur tax liabilities. There are four types – A, B, C, and D reorganizations. They differ in various ways in the amount of stock/cash that can be offered.
Term Sheet: A summary of the terms the investor is prepared to accept. A non-binding outline of the principal points which the Stock Purchase Agreement and related agreements cover in detail.
Time Value of Money: The basic principle that money can earn interest; therefore, something worth $1 today will be worth more in the future if invested. This is also referred to as future value.

-V-

Venture Capital Financing: An investment in a startup business that is perceived to have excellent growth prospects but does not have access to capital markets. Type of financing sought by early-stage companies seeking to grow rapidly.

-W-

Write-off: The act of changing the value of an asset to an expense or a loss. A write-off is used to reduce or eliminate the value of an asset and reduce profits.
Write-up/Write-down: An upward or downward adjustment of the value of an asset for accounting and reporting purposes. These adjustments are estimates and tend to be subjective, although they are usually based on events affecting the investee company or its securities beneficially or detrimentally.

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