legal matters

Buying In and Buying Out

If you want to be an owner of a medical practice, the first thing to consider is to consider it first. Set up your path to ownership when you first enter into an employment contract with a group or sole practitioner.

BY JOHN ALLEVATO

It is highly likely that at some point in your career you will be offered the right to purchase an equity interest in your medical practice—to become an owner. This can occur in any number of ways, including circumstances where you become the sole owner if you start your own practice.

More often than not, physicians 'buy in' or become owners of group medical practices with their colleagues. While it was common 10 to 15 years ago to be employed or have your practice purchased by a hospital, times have changed. Most hospitals are still licking their wounds from their foray into the ownership of medical practices (primarily gatekeeper practices), so that possibility is remote these days. The only exceptions may be for hospital-based physician specialties such as radiology, anesthesiology, pathology, and emergency medicine. But large numbers of even these practices are privately owned and operate under exclusive arrangements with hospitals.

So, when you have the opportunity at some point to become an owner of a group medical practice, you need to be armed with information on how to deal with that scenario—one of the most significant business transactions in which you will ever be involved. Here we are going to focus on the issues surrounding the 'buy-in' to a group medical practice. The term buy-in is not completely accurate—it is not entirely uncommon for a physician to acquire equity in the practice without an economic outlay. You'll learn more about that later.

The term buy-in is not completely accurate—it is not entirely uncommon for a physician to acquire equity in the practice without an economic outlay.

Also, we will discuss joining the practice of a sole practitioner, where you become the "retirement plan," so to speak. First, let's look at how to deal with initial negotiations.

It's important to remember that the time for you to get professional assistance for this process is during the negotiations, not after them. Seek advice from a health-care attorney or adviser familiar with the buy-in and contract negotiation process. More than likely, this will be necessary during your first employment

Continued from previous page

contract negotiations with the group.

The setup

The right time to begin the conversation about becoming an owner with the medical group you are planning to join is at the time you are interviewing with the group for your initial contract. Keep in mind that this issue should not necessarily dominate the discussions, but if someone in the group does not bring up your buy-in, then you must bring it up prior to signing a contract or joining the group.

And what should the initial discussions cover? These are the things you should know:

- When you would first be considered to become an owner of the practice;
- The terms under which you would buy into the medical practice, including what percentage you would own and whether you would be a voting member;
- You should find out, as much as possible, the economic terms of the buy-in, such as the cost to you (or the formula for determining the cost of your entry into ownership), how the group expects you to make the buy-in payment (will they finance it or must you approach your banker?) and the duration of the buy-in payments, and;
- How your compensation is determined after you become an owner of the group practice.

First, you cannot expect a "guarantee," or even strong assurance, up front from the group that you will be eligible to become an owner of the group. It is reasonable for the other members of the group to want a period of time to get to know you, your style of practice, your work ethic, your medical competence, your manner with patients, and how you "fit" into the group before deciding to invite you in. Thus, you should expect to find out when you will be first considered for ownership rather than seeking an ironclad guarantee that you will become an owner.

Getting this information out on the table as soon as possible means you understand from the beginning where you stand and when you will know more about your future with the group.

The details

Let's briefly review some important provisions that are the subject of any negotiation of buy-in. Your particular circumstances will dictate the details of your contract. A lot of these details may not occur during your first contract negotiation. That is fine. At the very least, get in writing when you will be considered for equity ownership. When the time comes to negotiate the actual buy-in, however, you will need to consider the other details.

• When should you first be considered for equity ownership? This answer will vary significantly, but generally within the first three years or so of your employ you should know if and when you are going to be asked to join the group as an owner. There are many ways this is accomplished, from having the new partner gradually buy in, to doing it all at once. The time frame for when you are first considered for an ownership interest should be a term in your initial employment contract.

• What are the terms of your buy in? There are no general answers to this, so let's focus on the key issues. How much is it going to cost for you to buy in? Is there a fixed amount or a formula price to determine the amount? If a formula is used, its components may consist of you buying your share of the fixed assets of the practice, plus your receivables, or a percentage of your receivables.

Know what your ownership percentage of the practice will be after you buy in. Don't assume you will be an equal partner with the other members of the group. Many times the founders or the older members retain a larger percentage, perhaps a control percentage or the voting rights. At the very least you should know that up front.

• How much should you pay? Seek the advice of colleagues and professionals in the field for this answer, since it will depend on your geographical location and practice specialty. Sometimes the answer to this is almost nothing. It is not uncommon for some groups to not charge a physician to buy into the practice. The circumstances where that might occur would be a group practice with very little or no capital assets, such as a hospital-based practice where the equipment and overhead are furnished. Again, this varies all over the board, but you should know how much the buy-in should cost you or the formula to determine how much it will cost.

• How will you make the payments? Find out if you are expected to go to your local banker and make a lump-sum payment, or if the group will assist you in making the buy-in payments by "reducing" your income for a number of years until you have "earned" your way into full ownership. While no one likes to have her income artificially lowered, this might be a beneficial way for you to buy in, unless you happen to have lots of assets at your disposal to pay for it all at once.

If the group is flexible and will allow you to gradually make the payments by reductions in your income for a few years, it may be better for you than having to finance the buy-in at a bank.

Continued from previous page

• **How is your compensation then determined?** You should have a firm handle on how your income is determined once you are one of the owners of the practice. You can assume it will be productivity based, as that is usually the case, although there are other methods of compensating physicians in a group practice setting. Be sure you understand the formula for compensation. If you don't, have it explained to you in detail. If productivity is a key determinant of your compensation, learn about how that productivity is measured.

It used to be that you got paid for what you did and how much came in for it. While that is still the norm, it might be more complicated than that. For example, if your group has some capitation contracts with an employer or an HMO, you need to understand how those payments to your group are allocated among the physicians. Also, subject to fraud and abuse and Stark rules, you need to understand how income from ancillary services is shared, as well as physician extender service income.

• **Should you agree to a non-compete provision?** The simple answer is there is no simple answer. You certainly shouldn't agree to such a provision unless everyone in the group is subject to similar non-compete provisions. Even then, there may be particular circumstances where the group practice would be inordinately penalized should you leave. In that case, a special non-compete provision may be in order.

This subject causes great consternation among physicians, as well it should. Remember that courts in most states will uphold reasonable non-compete provisions, so pay close attention to the one in your contract. Make sure it is reasonable in duration and geographical scope. For example, a typical non-compete may restrict you from practicing medicine within 10 miles of your group's practice for a period of one year after your contract is terminated—either by you without cause or by the group for cause. Those terms may be reasonable, but it might not be reasonable for your group to restrict your practice of medicine within 100 miles of the group's practice for three years.

Also, try to negotiate the non-compete provisions so they are applicable only if you are terminated with cause. The group may want them to be applicable if you leave for any reason, and they should apply if you decide to leave without cause. However, if you leave for cause, then it doesn't seem fair for your practice to be restricted. The same goes if you are terminated without cause. In other words, if the group decides one day to terminate you "just because," which they will probably have a right to do, it would not be fair for you to be subject to non-compete provisions. If you do something in violation of your contract (in other words, if you are terminated for cause), then it is understandable for the non-compete provisions to apply to you.

Joining a sole practitioner

One of the most common "retirement" plans of sole practitioners is to hire a young doctor who, if everything works out, will eventually take over the practice. That way, the retiring doctor can be assured that his patients are taken care of and that he can maximize his return on the successful solo practice he has built.

Without a young doctor joining the practice, the retiring physician would recover very little for his business. Bringing in a younger doctor to take over might be the best way for him to make the transition out of his practice.

If you are going to enter into such an arrangement with a sole practitioner, you should have a contract detailing the arrangement up front. Too many times promises are made ("One of these days this practice will be yours") and not kept, for whatever reason. Sometimes it is difficult for the sole practitioner to have a partner. After all, he started a practice and answered to no one for years. What you want to make sure is that you don't get strung along for years without some resolution of your status or understanding of your future with the practice.

While it may initially seem romantic to work your way into an established practice, maybe in a small town, too often the deals don't get done. Don't get caught short—get it in writing.

Thinking about becoming an owner early in your career will prepare you for the time when it occurs, or when you must negotiate your first buy-in contract. Knowing some of the key provisions of the contract you will probably eventually negotiate will serve you well when that time comes. ■

John Allevato is a member in the Charleston, WV, law firm of Spilman Thomas & Battle, PLLC, where he practices business and tax law. He counsels health-care entities and physicians. He is a member of American Health Lawyers Association and an adjunct lecturer at the West Virginia University College of Law. Reach him via e-mail at jallevato@spilmanlaw.com