PARTNERSHIPS:

THREE STEPS TO SUCCESS

Written by: Roger K. Hill, A.S.A.

A recent study conducted by GE Capital indicated that partnerships are the fastest growing type of transition plan. The reasons for this phenomenon are many, but the core reason is this: A partnership brings on-line the normally unrealized potential of your practice. In doing this, the practice itself becomes the vehicle that carries you through your career and lives on, surviving changes of doctors and ownership.

Following is an easy-to-understand outline of the essential areas of partnership planning. For each area, the outline also poses (and answers) a question that you have no doubt asked yourself. The outline consists of three sections: **Financial considerations, Legal arrangements, and Operational parameters.**

FINANCIAL

Fair Market Value

- Builds in senior doctor's (solo) anticipated growth
- Excludes associate's contribution to value
- Should include due diligence visit

After-Tax Cash Flow Projections

- Establish production goals for each doctor as well as hygiene (if applicable)
- Establish trigger point for buy-in; that is, the necessary amount of growth in the practice as well as the new doctor's production
- Determine easily affordable (for the new doctor) and tax-efficient (for the senior doctor) buy-in structure to avoid mistakes measured in tens of thousands of dollars
- Illustrate bottom-line (after-tax) outcomes of different profit allocation formulae.
- Determine when the practice is ready for a partnership
- Set timeframe for buy-in
- Establish bottom-line (after income tax) outcome for each doctor before, during and after buy-in
- Test integrity of strategic plan

Question:
"Should I do this before adding an associate, or after they have worked for a year or so?"
Answer: Before.
A well-defined plan will help you secure the right doctor because they will see your organized approach and, most importantly, your plan will set realistic expectations about financial benefits, legal arrangements and process. Failure to define expectations in these areas will almost always result in failure; count on it.

LEGAL: BEFORE THE BUY-IN

Employment Agreement – Sets out compensation, benefits, covenant not to compete, operational details and related items.

Letter of Intent (LOI) – Defines legal arrangements in two critical areas. First, all of the transaction details related to the anticipated buy-in. Second, all of the detail attendant to partnership operations, from the daily items (such as who will be the managing partner) to strategic considerations (such as buy-out / retirement arrangements).

LEGAL:
AT THE BUY-IN

Buy-In Documents

- Earnest money Promissory Note
- Agreement for Purchase and Sale of Stock
- Employment Agreements for each Shareholder Doctor
- Shareholders' Agreement
- Stock Pledge Agreement
- Stock Power
- Corporate Minutes
- Other legal documents, as needed

Question:
"How far into the future are the legal documents effective? Will they address both the buy-in and my buy-out?"

Answer:
It is especially important for each doctor to know all legal arrangements in advance – throughout each phase. Both the Letter of Intent and, later, the buy-in documents, will define the specifics of the buy-in, the entire period of the partnership, and how the buy-out will be conducted when the time is right. The (definitive) buy-in documents will amplify everything in the Letter of Intent and put the buy-in into effect.

Operational:

- Sufficiency of practice facility to accommodate the new doctor
- Appropriate level of new patient flow
- Effective marketing plan
- Commitment / support of staff

Question:
"Of these four items, which is the most important?"

Answer:
Surprisingly, the last one. Facilities can be expanded, new patient flow increased and a market plan designed. However, every plan needs the commitment and support of the staff. Positive attitude must be a given.

The key to successful partnerships is this: Know in advance how every part will work; then put it into motion. The old adage was never more true: Plan your work, then work your plan.

We wish you every success.

Roger K. Hill, A.S.A. is an accredited senior appraiser (ASA) of the American Society of Appraisers, a member of the Institute of Business Appraisers, and a founder/charter member of the Practice Valuation Study Group. With over 29 years of experience in working with general dentists and specialists, Mr. Hill serves clients across the United States providing transition planning for practice sales, partnerships (buy-in/buy-out), practice mergers, associateships/compensation analysis, and financial forecasting (proforma). His work places particular emphasis on achieving comfortable, successful outcomes by using tax efficient structures that provide a financial structure that is both affordable for purchasers yet fair and equitable to sellers. His work also thoroughly examines income distribution formulae (allocation of profit) so that each doctor involved can comfortably achieve his or her goals.

Mr. Hill is an active speaker, frequently addressing national, state, study clubs, and other professional groups. He has been published extensively in many publications on these subjects and, at the request of the American Dental Association, has recently completed work on a book about practice transitions. It is available through the ADA website.

Prior to his work in these areas, Mr. Hill held an administrative position at Baylor College of Medicine, and before that, St. Luke's Episcopal Hospital. He received his M.S.A. from the University of Houston in 1976 and has participated in professional graduate training in the specialties of Valuation Theory and Application as well as real estate law. He joined The McGill & Hill Group in February of 1997.

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