Pitfalls to Avoid When Selling a Practice

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MEDICAL PRACTICE

Pitfalls to Avoid When Selling a Practice

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The opportunity to sell a practice reflects the culmination of years of hard work and can be one of the most satisfying moments of a doctor's career. Unfortunately, since doctors typically only do this once in their lifetime, they do not have a chance to learn from previous mistakes. As attorneys working primarily with physicians, podiatrists, dentists, chiropractors and other healthcare professionals and facilities, we have encountered the fallout from "sales gone wrong" in a variety of circumstances. The following are a few illustrations of how proper planning and structuring can help ensure the success of your practice sale:

Avoid Arrangements That Might Violate "Fee-Splitting" and "Kickback" Laws

Obviously, setting the price for your practice is a key consideration, but a willing buyer may not be confident that patients will remain loyal to a new, or younger, face. They may balk at paying a high price due to this uncertainty. You can alleviate these concerns by committing to announcement letters with your personal endorsement of the buyer and by staying on board for some period of time post-transition (with compensation for your work, of course). However, some buyers may suggest "wait-and-see" pricing, pursuant to which they pay a percentage of collections or profits earned post-sale. This approach could constitute illegal "fee splitting" between independent third parties, or be considered a "kickback" in exchange for continuing patient referrals, potentially subjecting both the buyer and seller to disciplinary action for "professional misconduct" that could result in the suspension or revocation of their respective professional licenses – or the risk of an allegation by the buyer's attorney that the deal is illegal and unenforceable.

Be Careful How You Transfer "Goodwill"

The major component of a practice's valuation is its "goodwill", which is that amount which reflects the value of the business as a going concern in reference to historical revenue generation through patient loyalty and referral relationships. Is the goodwill personal to the practice owner, or does it belong to the practice entity itself? Most would agree that the owner has nurtured the relationships. Accordingly, in structuring a sale agreement, a selling entity must be wary if it is classified as a "C" corporation or its equivalent in the applicable state for tax purposes. A "C" corporation is taxed at the corporate level and the owner is taxed again when distributions are made to him from the sale proceeds. To avoid this double taxation, the goodwill can be sold through a separate agreement directly between the individual owner and the buyer,

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while the other assets would be transferred pursuant to an agreement with the practice entity.

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The better the buyer does, the more assured you can be that purchase price payments to be paid over time will be there when you expect them to be. This makes it especially important that those administrative and professional staff members who have endeared themselves to patients over the years stick around with the buyer to ensure continuity of the patient experience and the maintenance of goodwill. Familiar faces breed confidence! The purchase agreement should therefore address those individuals who are entitled to remain, and care should be taken to assure their interest in continuing to work with the new owner. On the opposite note, existing professional personnel who decide to leave constitute a major threat to the practice's continuing viability, particularly if they are not subject to a restrictive covenant (i.e., a non-compete) and have access to patient and referral source contact information. Care should therefore be taken before an announcement of the pending sale is made to ensure that adequate protections are in place, including instituting assignable employment contracts containing restrictive covenant clauses where needed.

Minimize Landlord Interference When Transferring Your Office Lease

Ensuring practice continuity after the sale is often dependent upon making sure that the office location remains the same. Many professionals fail to note that their lease often does not allow for assignment to a buyer without the landlord's consent. Effectuating a lease transfer (and absolving yourself from continuing liability under the lease, if possible) may become the biggest hurdle, and delay, in finalizing a sale. Any professional who expects to sell their practice should make an effort to add a clause to their lease indicat-

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ing that no consent from the landlord is required (or that such consent will not be unreasonably withheld) if the lease assignment is to another doctor as part of a practice sale transaction. If it is too late for that, then as soon as a seller feels comfortable, he or she should promptly commence securing the required landlord consent. The lease may specify the types of information that must be provided to properly request landlord consent. Be sure that the timing of the request for consent is carefully considered, though, so the landlord does not have time to shop around the lease.

These are but a few of the considerations involved in selling your medical practice. With proper planning and competent legal and accounting guidance, the experience can be pleasant, seamless and, most importantly, rewarding.

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