ASSOCIATESHIPS, PARTNERSHIPS, ACQUISITIONS, OH MY…. A Review of Relevant Issues for the Early Stages of Your Career

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ASSOCIATE AGREEMENTS

- If possible...DON'T SIGN ANYTHING!
- A Written Contract generally benefits the Owner, not you
ASSOCIATE AGREEMENTS
Cont.

- Employee v. Independent Contractor
ASSOCIATE AGREEMENTS Cont.

- Compensation
  - Production or Collection
  - Per diem
  - Hybrid

- HMO vs Other production-based payment
Term of the Contract
- Typical duration is one year

At-Will Employee v. Contracted Employee
ASSOCIATE AGREEMENTS

Cont.

- RESTRICTIVE COVENANTS
  - Covenant Not to Compete
  - Covenant Not to Solicit
  - Covenant Not to Solicit/Hire Employees

- Are they enforceable?
ASSOCIATE AGREEMENTS

Cont.

- A Covenant Not to Compete is enforceable during the **duration** of the Contract, not after the termination or the expiration.
- No Written Contract, no enforceable covenant.
- Other Restrictive Covenants are enforceable by inserting a provision into your Associate Agreement. Any ideas?
ASSOCIATE AGREEMENTS Cont.

- Trade Secret Information
  - Most important provision in an Associate Agreement
  - Catch-all
  - Alternative to California public policy
  - Courts will vigorously protect trade secrets, provided that the Owner keeps them secret
ASSOCIATE BUY-IN

- Various scenarios
  - Many different “ideas” in the market
  - Unfortunately, many unfairly harm one party
  - Ownership concerns for Owner
  - Property “vesting” concerns for Associate
ASSOCIATE BUY-IN Cont.

- Purchase Price
  - When should this be established?
ASSOCIATE BUY-IN Cont.

- Tax Ramifications
  - You
- Owner
ASSOCIATE BUY-IN Cont.

- Decision Making Authority
  - Day-to-day operation?
  - Large capital expenditures?
  - Personnel decisions?
WHAT IS A DENTAL PRACTICE WORTH?

- Despite what you may hear, there is NO universal valuation method
- Valuations involve many factors and also reflect the availability of capital to finance acquisitions
- Historically, No “Dental” Lenders
- Wall Street Acceptance Early 1990’s
TRADITIONAL APPROACH: PERCENTAGE OF COLLECTIONS

- Sale price established by assigning a percentage to prior year’s collections
- Range was 40-85% of collections
- Fee for service practices in highly populated markets with desirable lifestyle assigned the highest value
- Medi-Cal and capitation-based practices in rural markets assigned the lowest value
- Approach doesn’t take into account the value of equipment, value of goodwill, number of patients and other factors affecting the value
- Although generally accepted 25 years ago, largely ignored today
CURRENT VALUATION APPROACHES

- **ASSET APPROACH**
  - Assigns value to individual assets of Practice (i.e., equipment, instruments, supplies, furniture, records, goodwill).
  - Very subjective approach – not all brokers are alike
  - Outcome often affected by who hired the appraiser
  - Valuation of intangibles extremely subjective
CURRENT VALUATION APPROACHES

- MARKET APPROACH
  - Very similar to residential real estate appraisals
  - Compares price and profit margins of similar practices in the area
  - Doesn’t take into account quality of practice, growth patterns
CURRENT VALUATION APPROACHES

- Doesn’t factor in difference in deal terms when practices sold (i.e., tax benefits, financing, restrictions, etc.)
  - Seller gets all Tax Benefits - impact on Buyer?
  - Seller could be taking lots of patients
  - Seller may be staying on guaranteed contract, impacting Buyer’s take home and what purchase price he offers
CURRENT VALUATION APPROACHES

- INCOME APPROACH
  - Based on tax returns, profit and loss statements to derive true Doctor “net”
  - Purchase Price based on Buyer’s ability to pay overhead, debt service and earn a living
  - Applies capitalization rate to true net income of Doctor.
  - Rate varies by region, practice desirability
  - Generally, sales based on 150% to 300% of Doctor’s true net income – Depends on area, amount to be spent on upgrades
  - This approach is highly favored by CPAs and dental lenders
DSO’S

- What are they?
  - Individuals or companies which provide management support services for dentists
  - Provide all, or most, of the non-clinical operations of a dental practice
  - Ex: Heartland, Aspen, Pacific Dental, Kool Smiles, Dental One Partners
ARE THEY LEGAL?

- In the vast majority of states, they are

- HOWEVER, depending upon the state codes and statutes, as well as developing case law, this is a highly state-specific issue currently
In order for a DSO to be legal, generally the following must be adhered to:

- Management Agreement between the doctor and the DSO
- A management fee is paid to the DSO, cannot be based upon profits and must be reasonable
- The dentist remains in charge of clinical portion of the practice
- DSO is in charge of all non-clinical aspects of the practice
RISE OF DSOs

- In 1992, 157 practices were management services owned/operated
- In 2007, 3,009 practices were management services owned/operated
- Today, Schein and Patterson state their supply/equipment revenue from group practices/DSOs is between 15-20%*
- Over 8,000 dentists now work for DSOS

*statistic given by large MSO executive, not by Schein and/or Patterson
THE INDIVIDUAL DENTIST

- 60% of Dentists under the age of 44 are women
- Female dentists are almost 2x more likely to practice part time then their male counterparts
- Female dentists are much less likely to be practice owners (36% to 53%)
- Female dentists are 50% more likely to be comfortable being long time associates
- 80% of the graduating class from an individual dental school did not want to own their own practices
- In 2011 average debt for dental school graduates was $213,000 for private schools and $161,000 for public schools
THE YOUNG DENTIST

- Saddled with debt, young dentists are making career choices based upon financial security over the ability to own a practice and make more money (41% of dental seniors).

- Dentists who have graduated within the last 10 years are 3x more likely to work for a corporation than their predecessors.
Growing Impact of DSOs

+ Largest growth segment of dental practice—20% in 2012
  + Top 10 LGPs
    + 2700 dental practices
    + 6400 affiliated dentists
    + 2010 patient revenue of almost $4B
  + Several of the large groups are at or approaching $1B per year in revenue
Although there are several national and regional competitors:

- Largest competitor has annual revenues of approx. $700MM
- Top 20 players comprise approx. **7.5% of the total market**
Different Practice Modalities

Private Practice

+ Solo practice—still most prevalent, but shrinking
+ Partnership—possibly most dangerous form
+ Small Group Practice—local group of dentists with 1 or several locations
+ Large Group Practice—generally multi-state, professionally managed, and financially backed
THE UPSIDES TO CORPORATE DENTISTRY

- Generally, higher starting pay
- Great training workshops
- Strong emphasis on teaching case acceptance
- Quicker development of dental skills
DOWNSIDE OF CORPORATE DENTISTRY

- Limits your skill sets by referring heavily to specialists
- Longer patient work days (90% v. 60%)
- Less independence
- Less compensation over the course of career v. solo practice owner
- Pressure to “upsell” patients
QUESTIONS?

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