Resume

- Amherst College, 1979
- U. of Pittsburgh Dental, 1983
- Fairleigh Dickenson U., Ortho., 1985
- Pace Law, 1990
- Associate Professor, NYU Dept. of Orthodontics, 1989 – present
- Private practice of orthodontics, Brooklyn
- Private practice of law, Manhattan

Why am I Speaking to You Today?

- To explore legal issues in a transition from both the buyer’s and seller’s perspective
- To answer some of your questions about the legal issues of a practice transition
- To join my distinguished colleagues in a forum on practice transitions

Objective

This presentation is designed to give both buyers and sellers a brief overview of some of the legal issues to consider when transitioning into or out of an orthodontic practice.

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We will review the legal documents your transition might require.
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We will review what your attorney should do for you and what you should expect from your attorney.

Life Cycle of a Transition

1. Putting together your transition team
2. Hire an associate
3. Associate buys in
4. Associate buys out senior doctor
5. Senior doctor becomes the associate

Why would you be offered a job by a senior doctor?

- Excessive patient load
- Desire to reduce workload
- Transition imminent

What should you be careful of when evaluating an offer?

- Professional companionship
- Expectation of growth
- Desire to keep all procedures "in house"
- Locked-in buyer
- Better utilization of overhead

Associates, you have two functions in the office:

- Make your employer’s life easier
- Make money for your employer

Seller’s Transition Team
- Accountant
- Attorney
- Financial Planner
- Practice Broker
- Transition Consultant
- Spouse

Buyer’s Transition Team
- Accountant
- Attorney
- Finance Source
- Practice Broker
- Transition Consultant
- Insurance Broker
- Spouse
**Attorney’s Role**
- Evaluates: legal issues, employment issues, legal structure of practice, documents
- advisor
- negotiator
- document drafter
- document reviewer

**Legal Considerations**
Things to consider and have in place when contemplating a transition . . .

**Seller’s Entity Status**
- "C" or "S" corporation?
- If a "C" corp, consider switching to "S" status 10 years prior to transition.
- "C" corp makes a transition more difficult due to tax consequences for both parties

**Seller’s Employment by Corporation**
- If you are a C corp and have an employment contract with your corporation, "resign" from corporation at least a year prior to sale.
- This will help ensure the goodwill value is personal to you and not a corporate asset.

**Buyer’s Entity Status**
In conjunction with your accountant, choose the appropriate entity:
- Sole Proprietor
- Professional Corporation (s-corp election)
- Professional Limited Liability Company

**Lease Issues: Buyer and Seller**
- Pay careful attention to your lease years in advance. Negotiate hard.
- Put your lease where you can find it.
- READ THE LEASE
- You must have at least five to seven years left on your lease when you are ready to sell. Buyer cannot get financing without a lease of this duration.
Lease Issues

- Never assume the landlord will cooperate even if he is your patient, friend or brother
- Make absolutely sure you can assign and sublet to your buyer. Key words in lease are “such consent shall not be unreasonably withheld, conditioned or delayed.”
- Practice purchase agreement must have a lease contingency

Lease Issues

- Seller: do not assign your lease unless you close
- Buyer: do not close unless the lease is assigned to you.
- Buyer: if office is owned by seller, get an exclusive even if you vacate the space

Lease Zingers

- right of landlord to recapture space
- large assignment commission to landlord
- unobtainable standards for assignment
- “time is of the essence” clauses
- costly holdover rates
- failure to get an exclusive for ortho office
- failure of landlord to release seller

Lease to Own

- fair market value rent
- fair market value purchase price
- right of first refusal vs. option to purchase

Seller: Restrictive Covenants

- Make sure all associates have employment contracts with restrictive covenants
- Never hire an associate with the idea you will prepare a contract later
- Lack of restrictive covenant will hurt practice marketability

Buyer: Restrictive Covenants

- Restrictive covenants are enforceable: don't sign one if you don't intend to adhere to it.
- Be careful about a “bait and switch” restrictive covenant.
- You will be asked to sign a restrictive covenant: look for creative solutions to difficult issues.
Financial Policy, Accounts Receivable

- Tighten up your financial policies at least a year in advance.
- Make an effort to collect your accounts receivable at least six months in advance. This may be money left on the table after the transition.
- Buyer does not want to collect your a/r. Once you sell, you will not be in a strong position to collect them yourself.

Practice Liens and Loans

- Review and begin to pay off any outstanding debt on practice.
- Do not enter into any long-term leases or contracts. The buyer may not want to assume these and you may have to absorb them.
  - Examples include: yellow page ad, digital x-ray/cbct, postage meter, water cooler, laundry service, sharps pick-up, alarm system, software maintenance.

Practice Statistics: Charts and Computer Entries

- Be diligent about entering computer stats.
- Inaccurate stats present an incomplete picture of the practice.
- Improve your charting. Take progress records.
- Buyer will do a chart audit. Do not be offended or defensive. Neat charts improve value and buyer confidence.

Pre-Sale Patient Management and Care

- Start treatment on any patient who is ready to begin.
- Increase your initial fee and make sure patients adhere to your fee schedule.
- Avoid excessive prepayments and excessive use of third-party financing.
- Avoid a last minute “fire sale” on treatment. Buyer’s can spot that and will look unfavorably on it.

Tax Returns/Financial Data

- Clean up your books.
- Slow down on the personal deductions to show more income.
- Report cash in the unlikely event you haven’t been.
- Have tax returns and P&L ready for buyer.
- Work with your accountant to have all the financial data ready for buyer.

Post-Transition Employment

- Does seller want to work for buyer?
- Does buyer want to employ seller?
- If yes, how much and in what capacity? As an independent contractor or an employee?
- Will Seller close P.C. or have P.C. work for buyer?
- Seller: how you treat buyer will be how buyer will treat you.
Personal and Financial Issues/ Seller

- Can I afford to retire?
- Am I burned out?
- Do I have something else I would rather be doing?
- Is my spouse on-board with the sale? (For better or worse, but not for lunch.)

Personal and Financial Issues/ Buyer

Know seller’s answers to the previous questions and ask yourself:

- Can I afford this practice?
- Do I need to work somewhere else?
- Am I ready to run a practice?
- Is my spouse as excited as I am?

Tax Issues in a Transition

There are three parties to every transition:

- Seller
- Buyer
- IRS

Tax Issues in a Transition

- goodwill
- accounts receivable, contracts receivable
- restrictive covenants
- fixed (tangible) assets
- supplies and instruments
- leasehold improvements
- stock transfer

Goodwill

- best for seller
  - buyer: straight-line 15 year amortization
  - seller:
    - capital gain for unincorporated, S-corp, LLC
    - double tax if C corp
    - 35% corp tax plus personal income tax rate

Restrictive Covenants

- allocation unfavorable to both parties
  - buyer: straight-line 15 year amortization
  - seller: ordinary income

(If restrictive covenants are merged into goodwill, capital gains treatment is possible.)
Fixed (Tangible) Assets
- dental and office equipment, furniture, fixtures
- good for buyer
  - buyer: depreciates annually according to schedule, 5 – 7 years
  - (Section 179) $25,000/yr.
  - buyer may pay sales tax on value of assets
- seller: ordinary income

Supplies and Instruments
- great for buyer
- buyer: immediately deductible
  - no sales tax
- seller: ordinary income

Leasehold Improvements
- so-so for buyer
- up to 39 years to depreciate

Allocation of Purchase Price
- Make sure you can support the allocations in your agreements
- Get your accountant involved

Stock Sale
- Great for seller, terrible for buyer.
- Buyer: no deduction, becomes “basis”
- Buyer: inherits all of corporation’s liabilities
- Seller: capital gain above basis

Fractional (Stock) Buy-In
- Limited value assigned to stock in a fractional buy-in to reduce unfavorable tax outcome to purchaser (depreciated value of assets)
- Income shift, buyer to seller
  - offset (increase) in purchase price
- Personal goodwill of seller
- May be the only way to buy into a group practice
Psychological Issues

- Seller’s Concerns
- Buyer’s Concerns

Our topic:

Presenting Value, Perceiving Value: Understanding practice transitions from the perspective of both buyer and seller.

Seller

- Your practice is probably not worth 1x gross despite how great you feel it is
- You probably aren’t worth $1,500/day despite how great you think you are
- Don’t stay too long, sell while your practice still has real value
- Even though you just “hung out a shingle” and did well, it is a different environment today.
- Are you sure you can live on what you have left?

Buyer

- Seller’s practice is worth more than 25% of gross despite how antiquated you feel the physical plant is
- Somehow, seller managed to make a great living with that dowdy old office
- You probably aren’t worth $1,500/day despite how great you think you are
- It will take you a year or two to realize you don’t know everything
- Are you sure you can live on what you have left?

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Inter-family Transitions

- every parent’s dream
- fraught with emotion
- dependent upon having a large practice
- challenging with divorced families
- complex tax issues
You are ready to move ahead.

What documents will you need?

Formal Document Drafting

- asset, stock, or interest purchase agreement
- new lease or lease assignment and assumption
- employment agreement for seller
- consulting agreement for seller
- deferred compensation agreement for seller
- stock purchase agreement
- stock pledge agreement
- goodwill assignment agreement
- restrictive covenants
- partnership agreements/ partnership dissolution agreements
- promissory note
- bill of sale
- security agreement
- escrow agreement
- lien search/title search

Formal Document Drafting

- letter of intent
- parties negotiate issues
- formal documents are drawn up, usually by seller’s attorney
- documents can be drawn up by broker, consultant or buyer’s attorney
- other attorney reviews and comments

Sailing to Iceland

America’s Cup 2014

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Make an Investment

Disclaimer

This information is not intended as a substitute for legal advice. You should familiarize yourself with the laws of your local jurisdiction and seek legal advice from a local attorney who specializes in such matters.
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