“Succession Planning for a Small Rural Medical Practice”

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FOCUS

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Introduction

One day during a very informal conversation that took place “about who would retire when someday,” between a two-partner physician owned rural medical clinic physicians and their clinic manager. It was learned that there was no real plan in place for either partner to sell or transfer their ownership in the clinic. The medical clinic manager was tasked with researching and writing a potential succession plan of the elder partner, who was thought to be the first to retire in about five years’ time frame.

In this focus paper, the author will provide very in-depth detail to the process of succession planning. The research methodology used was done by interviewing and surveying other rural physicians, a certified public accountant (CPA) who services medical practices, and an attorney who handles many purchases and sales for these types of entities. This research was conducted to gain insight as to not only the commonality of whether succession planning is done in advance, but if it is done at all, as well as outline a method to prepare one if a physician owner does not currently have one in place. The author also relied on several professional periodicals for additional knowledge and expertise on the research topic of succession planning for medical practices.

Background

The two physician partners opened the medical clinic in October of 2001 and are currently practicing together after almost 16 years. Little to no thought was given to how the succession of each partner would proceed. Both physician partners thought they would “cross that bridge when they got there.”

As you see, each physician relocated to this small, rural community by taking employment back in 1999 and the other in 2000 with a mid-sized clinic that was a hospital based entity. This entity
closed its doors shortly after hiring these two physicians in 2001. These two physicians had to act rather quickly to decide to enter into this partnership or begin the process of relocation again. Occasionally business choices and decisions are placed in front of you at the most unexpected times. Both physician partners believe today that they did make the right decision for many reasons that will be listed further in this manuscript.

Fast forward to 2017, the Clinic Manager of this small, rural medical clinic, having over 25 years’ experience in healthcare administration with two degrees, one in each accounting and business management, and having never facilitated such a transition as succession planning, looked forward to researching and planning for such an event. This Clinic Manager preferred to work in a proactive fashion rather than reactive, and believed by researching and educating herself in succession planning, she may be able to advise the physicians better to avoid any potential costly mistakes. The Clinic Manager began the process of online research. Next she drafted a physician owner survey in order to survey the other local community physician owners to gain insight and historical knowledge. The Clinic Manager also wrote two lists of interview questions, one for the clinic’s certified public accountant (CPA) and the other for the clinic’s attorney in order to gain additional expert insight on the topic of succession planning for small rural practices.

Body

Legal Ownership

Per an article in Medical Economics (John Campbell),

In a 2016 Medical Economics article it is cited that in 2013 nearly 40% of doctors in the U.S. are aged 50 or older, and one in four are 65 or older, according to the American Medical Association. For these baby boomers retirement is a fast-approaching reality. As they ponder their next life phase, doctors who own private practices face several challenges
unique to the profession. Physicians can only pass their business on to another physician, naturally limiting the number of available potential buyers. And this small pool grows smaller still as a large number of younger doctors are turning away from private practice to work for large healthcare providers.

In the State of Oregon, at this current time, medical clinics must be owned by a licensed physician (Legislature). This legal requirement lends itself to either hospital owned practices or primarily, physician owned practices, especially in rural areas of the state; this being the case for these two board certified family physicians. This adds special requirements that need to be met to sell or transfer a medical practice.

These physician owners were very much proactive back in 2001 when they opened their medical practice. They had the reasoning to hire an attorney to file their business entity registration with the state and to draw up their business operating agreement, as well as other legal documents to own and operate a medical clinic. As partners, they wrote a simple business plan and divided outlined duties. One physician was chosen to be the managing partner for business affairs and the other managing partner for medical affairs. To this day the division of management remains the same, and it has lent well to their very successful medical practice.

**Industry Trends**

The author surveyed nine local independent physicians in her small, rural community that own and operate seven small, independent medical practices. Some of the practices had one owner, but employed two to three practitioners. The author only interviewed the physician owners at each practice. For the medical industry, the author found the independent physician owners to follow industry trends; however, did find variances. (Survey).
The author learned that all of the physicians interviewed actually started their own practice. None of them bought an existing medical practice. All of them had practiced previously as employed physicians, with the exception of two physicians. One had worked only 6-months for a previous clinic that closed its doors within 6-months of her hire. The other had owned two previous clinics, each with different partners, prior to opening his current medical practice. He had never worked as an employee throughout his career.

None of the nine owner physicians had a succession plan when they opened their practices. Most just wanted to get their startup off the ground and then plan from there. Except for having legal limited liability corporation/partnership, partnership agreements if applicable, and tax planning, none had a formal business plan when they started their medical practices. They were all very informal with an exception of two practices having formal operating agreements between the physician partners. When surveyed, one was even surprised to hear that they may be able to sell their interest half of the partnership and receive actual return on their investment for it.

Of these nine physician owners, they have achieved an average of 18 years of independent practice and ownership of their medical clinics. Five of the nine physicians’ medical practices are of sole ownership in nature, and the four remaining physicians share in two separate partnerships. The average practitioner count per clinic is 1.6. Of these seven clinics, three have clinic managers that oversee all operations. One has an office manager that oversees the front office business portion of the medical clinic while the physician owner manages the medical back office part of the medical clinic. The remaining three clinics are managed solely by the physician owner.

Only one of the seven medical practices currently had a formal written business plan while none have a formal written succession plan. Five out of the seven medical clinics regularly use a certified public accountant to receive advice from. Three of the seven medical practices utilize an
attorney on an ongoing basis for legal advice. One utilizes an attorney occasionally. One consulted an attorney for startup purposes only, and two did not utilize an attorney at all.

Of the nine physicians interviewed, the average length until retirement is 7.7 years’ time. Over half of which plan to retire within a handful of years.

When asked if there was anything that surprised them about being in private practice, the author received answers such as; they did not anticipate how much change there would be ongoing that he would be responsible for. Another said that he found himself working more than he thought he would. He would often count in his head how much income would be lost had he taken a day off; he said he would then often work rather than take that day off. Another replied that she was surprised at how much better it was than being employed. She could affect change quite quickly, and that provided her a sense of peace to her and her patients alike. Another replied that she really enjoyed having independence of the kind of medicine she wanted to deliver to her patients. One physician stated that there was no surprise as he had already owned partnerships in two previous medical clinics, and he knew what to expect with this being his third medical practice partnership. Some other responses were that they were very burdened with the management of the practice until it evolved large enough to bring on a practice manager to handle the burdensome state and federal regulatory requirements as well as all of the daily management workload. All clinics that have managers relayed the importance of having a professional that understands the requirements and is able to shift quickly with the legal climate of operating a medical practice of today. Most physicians stated they believed having a qualified clinic manager added to their continued ability to remain independent.

The physicians interviewed were asked what they liked most about being independent and they replied that they enjoyed the anonymity of being in private practice, the liberty to take time off, and being able to truly advocate for their patients without the burden of politics of large
administration. They enjoyed the freedom and ability to affect rapid change when needed, being able to make decisions quite freely, having the ability to set their own schedule, and being able to decide when they start to taper-off as they prepare to enter the last years of private practice.

When asked the final question of what they would most like to change about being independent, several often replied that they would simplify legal regulatory burdens. One said she wished her partnership would have purchased their facilities rather than lease. She remarked had she purchased her facility in the beginning, it would have improved her future retirement. One physician stated that he would change nothing. He believes that he structured and staffed his practice appropriately, and by being staffed at the correct level, he has the ability to treat patients’ timely and effectively; thus avoiding stress and burnout.

**Startup**

It is advised, but most often not followed, demonstrated by the author’s physician survey, that you should begin purchasing a medical practice knowing what your succession plan will be. This will assist the physician upon retirement or relocation. For this reason, the Clinic Manager sought out the assistance of her clinic’s certified public accountant and attorney for expert guidance.

**Legal Advice**

The Clinic Manager interviewed the Clinic’s attorney (Reynolds). The Clinic Manager had prepared a list of researched questions prior to the interview. The first question was to obtain the attorney’s opinion based on her experience of advising many medical practices during her career. This question asked if in her professional opinion was it better to own or be employed as a physician. The answer was

> It depended on many factors such as how important a sense of security was to the physician. That there seemed to be a lot of risk built in to starting or buying a medical practice. If you
are someone straight from medical school, you may not have had time to build enough security and may want to avoid the risk.

The other point the attorney raised was that it really all fell down to personal choice. How much control the physician wanted to have over their work environment and schedule.

When asked her opinion whether it was best to start up or purchase a medical practice her reply was to start up. She then clarified that if a person could purchase a medical practice, that truly would be ideal in that the physician would not have to wait to build the patient census in order to have enough revenue coming in to cover the overhead and still pay themselves. However, if the same physician was straight from residency they may not have enough capital to purchase a practice, unless it were sold under contract. If the physician chose to start up then they may have to start very small by purchasing minor office equipment and supplies, and may not pull a very good income for some time. For these reasons, the attorney thought this was the reason most physicians choose to become employed rather than own their medical practice.

When asked the best way to form ownership or partnership legally; the attorney responded with either a limited liability company (LLC) or limited liability partnership (LLP). The number one reason for choosing one of these ownerships is to shelter the physician owner personally from potential litigation arising, such as a slip or trip wherein a patient is injured.

When asked what her advice would be between owning as a sole ownership versus a partnership, she replied they each have pros and cons. One pro was that you would have a partner to share the risk and reward with. Also, you would have built in coverage so as to not be spread thin and would have another to share call with. The cons were possibly having different expectations and goals. The attorney did say that if a physician decided to enter into a partnership, they should seek expert legal counsel first. Explained below.
Reynolds stated

There would be a need to draw up an ironclad partnership and operating agreements. Wherein the partners would set the terms upfront as to who would manage what parts of the medical practice, how the ownership would transfer if there were a sudden life event such as a major health condition, divorce, bankruptcy, and even death. Reynolds often drafts a document called a Deadlock Agreement wherein the partners have agreed in advance of certain terms that would allow one to buy out the other after one of the curtain outline life events had occurred. In this Deadlock agreement, the price would be set in advance (reviewed annually), and the other partner would receive all interest if the agreement was enacted and purchased as previously outline. She also advised that each partner should cross-purchase life insurance. This would help alleviate the need for sudden cash in the event that one partner passes, and the remaining partner needs to purchase the deceased partner’s interest from the surviving heir.

Reynolds recommends that existing partnerships bring on any new potential partner as an employee or a contract employee for a preset period of time prior to purchase into the partnership. She said this gives both parties time to see if it will be a good fit prior to entering into what would be a lengthy legal relationship.

When asked if there was any other advice, she stated, “one should plan very early, have everything in writing, know all of the cards you are playing, and don’t be the one who doesn’t do their homework!”

**Tax Advice**

The Clinic Manager then interviewed their certified public accountant to inquire about succession planning for small rural medical practices (Mike Wallace). She asked what the best way to set up
a small medical practice. He replied either a sole proprietorship, a limited liability company (LLC), or a limited liability partnership (LLP).

When asked if it were better to start up or purchase an existing medical practice the certified public accountant stated he would want to purchase one already operating. He further stated

If the purchase terms allowed, a physician could possibly pay for his interest out of operating income since there would already be an existing revenue stream. Some physicians selling are quite open to accepting terms for payment to alleviate them from a heavy tax burden in the year of sale. Most sales are financed by the seller anywhere from 3 to 5 year terms. The selling physician would often only be selling the equipment/furnishings and goodwill in the practice as most physicians own the clinic property in a separate holding for tax and liability purposes. So, the purchaser may be entering into several agreements upon purchase. One, equipment/furnishings, two, goodwill, three, building from a different holding entity, and possibly four, taking over an existing lease if the property was leased rather than owned.

When asked if it were hard to finance the purchase of a medical clinic Wallace replied

Often these were young doctors that are still repaying student debt, and did not usually have a lot of capital reserved yet. If the purchaser had a home with sufficient equity, one might tap into that as an asset to loan against. The other would be to have the selling physician carry the contract. This however may be difficult at times when the new physician is just starting out. He or she may be just entering into contract with most of the insurance companies which may pay lower and slower at first. The new owner can only repay the seller as fast and as much as he or she produces income. The purchaser cannot repay the seller any faster than he or she produces income in order to avoid repaying with phantom income which would then lose much of their tax advantage by actually repaying from personal income rather than from the gross revenue from the medical practice itself.
When asked how one would plan their retirement investing the accountant stated, “If it were a sole corporation they would invest through a 401k. If it were a LLC or a LLP, the physician owner/s would invest through a Simplified Employee Pension Plan (SEP).”

When asked how one would value a medical practice in order to price to sell, Wallace replied

You would handle the building as outlined above; either purchase or lease. Then you would value the medical equipment, furnishings, and supplies in a separate purchase and sale agreement. Then you would examine the Profit and Loss Statement for the previous 3-5 years. You would research what other employed physicians were paid in same locale, size, region and specialty. Then you would tax up your annual owner withdrawals to get the same tax liability as an employed physician, and subtract one from the other. If the practice still showed a positive owner income you would have your net profit for that given year. You would need to perform this evaluation for at least 3-5 years to see a trend and verify the valuation. One would also verify this information by requesting to review the selling physicians 3-5 previous year’s tax returns.

The valuation process might be quite risky to the purchaser whereas the proven income may not be realized after the selling physician retires due to patients not remaining with the purchasing physician for a multitude of reasons. For this and other reasons the verified profit method of valuation is often heavily discounted. It would be rather difficult to value the insurance contracts as they belong directly to the selling physician and cannot be transferred. There would be no value in the direct insurance contracts.

The Clinic Manager agreed and added that some insurance companies have closed networks that may not be accepting new physicians at the time of sale. For this reason, the purchasing physician would want to verify contract availability with all insurance companies prior to entering in to any binding legal agreement.
The accountant agreed with the attorney that it would be beneficial to both the selling and purchasing physician to sell on terms. This would spread out the tax liability for the selling physician, as well as provide a great income stream short term while assisting the purchasing physician by being able to split the purchase amount over time.

One side note on the goodwill purchased (mainly patient inventory/census), the selling physician would claim it as a capital asset and have deferred taxation. The equipment, furnishings, and supplies would be sold on a separate note that would be taxed on the interest gained annually.

Per Wallace, it is good idea to have the purchasing physician come on board for a year or two prior to the sale to evaluate whether it will be a good arrangement moving forward for all parties involved as selling physicians often want to avoid having to step back in after a default situation.

**Evaluating the Medical Clinic**

A recent article in Medical Economics (Walker) outlined how to valuate a medical practice.

Practice Valuation: They are the two most important business terms a practice owner needs to know. For a young physician venturing into private practice, they could determine his or her largest financial transaction. And to a retiring physician, practice valuation may decide the amount of sweat equity built over a career.

After a physician has worked a long time, they want to receive value for what they have built up. They have a great ready-made income stream to sell, and the buyer is looking for a ready-made income stream to purchase. That is what value is all about says Mark E. Kropiewnicki, JD, LLM, President of Health Care Law Associates, P.C.

Determining the value of a physician practice requires addressing a variety of issues: referral patterns; the age of the seller and whether he or she is staying with the practice for an
extended period of time; the practice’s insurance mix; the reimbursement and economic climate at the time, and the practice specialty, says David H. Glusman, CPA, CFS, partner-in-charge, Philadelphia region for the accounting and consulting firm Marcum LLP, in Bala Cynwyd, Pennsylvania. “The single largest driving factor in the value of a practice is the cash flow available for the buyer after taking into account a fair market value compensation for the seller or replacement physician,” he says.

“Two physicians in the same geography in the same specialty may not have the same fair market value compensation,” he explains. “The relative efficiency in the practice is certainly one criterion. The other issues that relate to the practice, how it is operating and its profitability also are carefully evaluated. At the end of the day, selling a medical practice has become a lot more like selling any other business; the buyer is looking for a return on their investment in the form of cash flow and potential growth.

“The combination of art and science in preparing a business valuation for a medical practice is understanding the relative risks which go into the capitalization rate to be used in the economic environment that allows for the determination of the likely cash flow stream. The seller is looking for the sale price to reflect the past efforts to build the practice, its reputation, and the revenue it will continue to provide to the new owner,” Glusman adds.

Tangible and financial assets, patient accounts receivable, office building, goodwill, and intangible assets are all factors that determine a practice’s value. Tangible and financial assets include the practice’s equipment and furniture, cash, prepaid insurance [unexpired insurance premiums], and other assets less liabilities, including payroll taxes, loans, and retirement plan contributions, DeMuth says.
Because most medical practices are cash basis taxpayers, patient accounts receivable do not normally show up on their financial statements, according to DeMuth. “The amount of the receivables should be based upon the amount charged, which is expected to be collected,” he says. “There are several ways this could be calculated depending upon the information available.” Practice goodwill is generally the most subjective and variable asset in valuing a medical practice. Valuing the intangible assets and goodwill of a medical practice can be a contentious issue.

If the practice or related entity owns the office building, a commercial real-estate appraiser normally appraises the structure. If the office is leased, the leasehold may have a value depending upon the number of years remaining, amount paid for rent compared to going market rent, and the ability to renew the lease, DeMuth explains.

Office location and profitability are also important, according to Kropiewnicki. “If a practice is in the middle of nowhere, rural versus suburban Pennsylvania or New Jersey, then the rural practice will almost certainly be worth less than the suburban practice, all else being equal,” he says. “Also, profitability is a major factor, so if you have two practices in the same geographic area each grossing $1 million, and one physician is making $300,000 and the other physician is netting out $500,000, a buyer should be willing to pay more for the more profitable practice.”

“While there are numerous factors which could affect it, the value of goodwill is generally dependent upon the ability of the purchaser to be able to earn a superior return from the practice compared with what could normally be expected to be earned by physicians in the specialties represented in the practice,” DeMuth says.
“In my opinion, debt-capacity is the most appropriate method to use to value a medical practice” Vincent M. Brinly, director of valuation services at Practice Valuation Group, Washington, D.C. Brinly adds, “The capitalization-of-earnings method and the debt-capacity method are similar; both capitalize adjusted net cash flow to determine fair market value. In a professional practice, the emphasis is on the value of professional goodwill. Since the focus of the debt-capacity method is on the transfer risk or value of the patient records that can be transferred from one doctor to another, it is the most fitting method of appraisal to value a professional practice,” he explains.

“In addition to legal issues, tax issues need to be taken into consideration such as the tax impact of earnings in S corporations, partnerships and other flow through entities that commonly exist for physician practices,” says Glusman.

Taxation is affected by the legal form in which the practice seller conducts business, be it a proprietorship, general partnership, Limited Liability Company or partnership, or a C or an S corporation, DeMuth explains.

“The deal has to take into consideration the legal structure and the tax implications that carries,” Glusman agrees. “Nonetheless, the net price paid for the assets, including any goodwill, must be fully justified as fair market value to avoid governmental allegations at a later date.”

The purchase or sale of a medical practice or of an ownership interest can be one of the biggest financial transactions in a doctor’s life. “The physician’s financial interest in his medical practice may be more than his home,” DeMuth says. “To assure that the doctor is paid or pays appropriately for what has been or will be his life’s work, its incumbent upon him or her to see that the practice’s value is appropriately determined and legally sound.”
Sales and Purchase Agreement

As the clinic’s attorney stated earlier in this manuscript, after evaluation the next step is to draw up a sales and purchase agreement. A sales and purchase agreement is a legal contract that obligates a buyer to buy and a seller to sell a product or service. Sales and purchase agreements are found in all types of businesses but are most often associated with real estate deals as a way of finalizing the interests of both parties before closing the deal. She also advised to always seek legal counsel prior to entering into any legal agreements. As you can see earlier in my physician survey, this counsel is not always followed.

Operating Agreements

Per Small Business Administration (Administration)

If you are seeking a business structure with more personal protection but less formality, then forming an LLC, or limited liability company, is a good consideration. Regardless of your business structure, some paperwork like an operating agreement is expected. Here are the basics every LLC owner should know about operating agreements:

What is an operating agreement?

An operating agreement is a key document used by LLCs because it outlines the business’ financial and functional decisions including rules, regulations and provisions. The purpose of the document is to govern the internal operations of the business in a way that suits the specific needs of the business owners. Once the document is signed by the members of the limited liability company, it acts as an official contract binding them to its terms.

Why do you need an operating agreement?
1. To protect the business' limited liability status: Operating agreements give members protection from personal liability to the LLC. Without this specific formality, your LLC can closely resemble a sole proprietorship or partnership, jeopardizing your personal liability.

2. To clarify verbal agreements: Even if members have orally agreed to certain terms, misunderstanding or miscommunication can take place. It is always best to have the operational conditions and other business arrangements handled in writing so they can be referred to in the event of any conflict.

3. To protect your agreement in the eyes of your state: State default rules govern LLCs without an official operating agreement. This means that each state outlines default rules that apply to businesses that do not sign operating agreements. Because the state default rules are so general, it is not advisable to rely on a governing body state to manage your agreement.

*Tip: Consult with an attorney and accountant to assist with the financial and legal matters of your agreement.*

What does an operating agreement entail?

Operating agreements are contract documents that are generally between five and twenty pages long.

What is included in an operating agreement?

The functionality of internal affairs is outlined in the operating agreement including but not limited to:

- Percentage of members' ownership
- Voting rights and responsibilities
- Powers and duties of members and managers
- Distribution of profits and loses
Non-compete agreement

Per Law Office of Aaron Larson (Larson)

What is a Non-Compete Agreement

A non-compete agreement is a contract pursuant to which one party agrees not to engage in business activities that compete with the business of the other party. The agreement may be incorporated as a clause in a larger contract, such as an employment contract or the contract for the sale of a business. This type of agreement is also known as a covenant not to compete.

Non-compete agreements are often included within contracts for:

Employment – Non-compete agreements are common in an employment context, with an employee agreeing not to compete with a former employer for an agreed period of time after the end of the employment relationship.

Sale of a Business – Non-compete clauses are routinely included in contracts for the sale of a business, with the seller agreeing not to compete with the buyer.

Business-to-Business Transactions – Non-compete agreements may be incorporated into contracts with business partners, vendors or independent contractors, who may otherwise be able to take advantage of information that they learn while working with a business in order to later compete with the business that employs their services.

What Terms are Included in a Non-Compete Agreement
A non-compete agreement describes restrictions on what competition is permitted, where it is permitted, and the length of time that any restrictions on competition remain in effect. The terms of a non-compete agreement will thus normally focus on three issues:

Scope – What sort of business venture is restricted or forbidden during the term of the agreement?

Time – For how long after the end of a business or employment relationship will the non-compete agreement remain in effect?

Distance – Over what distance or geographic range is the non-compete agreement in effect?

Are Non-Compete Agreements Legal

Most U.S. jurisdictions allow non-compete agreements in an employment context, or in a business-to-business contract, and all allow non-competes in contracts for the sale of a business. Thus, in most jurisdictions an employee can be required to sign a non-compete agreement by an employer or prospective employer.

Some jurisdictions disfavor non-competes in the context of employment. For example, California, Montana, North Dakota, and Oklahoma prohibit non-compete agreements for employees, and Illinois prohibits them for low-level employees. In California, outside of the context of the sale of a business, non-compete agreements are not normally enforceable.

Even in states that will not enforce non-compete agreements, it may be possible for a past, out-of-state employer or party to a contract to enforce a non-compete agreement in that other state's courts. If a non-compete is valid under the laws of the state in which it was executed, and in which the business transaction or employment occurred, then litigation to enforce the contract remains possible in that state.
Similar Contractual Covenants

In addition to a non-compete provision, a contract for employment, services or the sale of a business may include additional covenants to protect the business from competition. Two common examples are:

Non-disclosure agreements – An agreement that certain information is considered to be the property of the business, and that the restrained person will not utilize or share that information in any other context.

Non-solicitation agreements – An agreement that during the term of the contract, and possibly for a period of time after its conclusion, that the restricted party will not solicit customers or employees of the business.

Non-disclosure and non-solicitation agreements are more broadly enforceable than non-competition agreements, and are evaluated under different legal standards.

When Are Non-Compete Agreements Enforceable

To be enforceable, a non-compete agreement must be adequately supported by consideration at the time it is signed, it must protect a legitimate business interest, and must be reasonable in its scope, duration, and geographic limits.

Consideration

In order for the clause to be enforceable, something of value must be received by the person agreeing to a non-compete clause. In the sale of a business, the terms of the sale and payment for the business are sufficient. In an employment context, if the agreement is entered as a condition of being hired, the creating of the employment relationship is normally sufficient.
If an employer asks an existing employee to sign a non-compete agreement, it will generally be necessary to offer more than continued employment to render the agreement enforceable, such as a raise or promotion.

Legitimate business interests

The states that allow non-compete agreements do so out of recognition that businesses may be at a disadvantage if a business seller or certain former employees are able to compete with them without restriction. Nonetheless, any restriction must be related to the business's legitimate business interests.

For example, a non-compete clause cannot be used as a mechanism to hamper an employee's ability to get work with non-competing businesses.

Reasonableness

In most jurisdictions that allow non-compete agreements, courts will examine the reasonableness of the agreement's terms, to determine if its scope, duration, and geographic limitations are reasonable.

A non-compete agreement is more likely to be held valid in the context of the sale of a business, or in a business-to-business context, than in an employment context. Business owners and managers are assumed to be sophisticated in their understanding of contract terms. For the sale of a business, concerns about the seller potentially opening up a nearby competing enterprise that will draw away customers are significant.

For employment agreements, the reasonableness of a non-compete agreement will depend upon the nature of the employment. Also, employers are generally not permitted to enforce
non-compete agreements that extend to geographic areas in which they do not conduct business.

For example, a geographic limitation on competing within a ten mile radius may be deemed unreasonable for a hairdresser, but a non-compete agreement for a business executive might be deemed reasonable despite a statewide or even nationwide restriction. Similarly, for a hairdresser, a court might be skeptical of a non-compete that was more than one year in duration, but might find reasonable a two- or three-year restriction on competition by a doctor or lawyer who left a local practice.

It is unlikely that a court would find enforceable a provision that prohibited a hairdresser from working in a beauty supply store, but it might enforce a prohibition on a person who sells a restaurant from operating as a caterer within the same general market.

**Transfer of Patients and Their Records**

As the clinic manager it is a well-known law that when a physician sells their interest in their medical clinic, they must report the sale of this transaction to the Board of Medicine within their state (Oregon). They must also draft a letter of notification to their patients notifying them of this transition and who will become their medical record custodian. The physician owner, and/or the new designated owner, legal records custodian must retain patient records for a period of no less than ten years after date of last service.

**Other Options**

Throughout most of this manuscript the Clinic Manager looked primarily at the option of selling a small rural medical practice because this was her task at hand. However, at this time the clinic manager would like to cover a few other options that may be available to the selling physician partner.
1. If after seeking qualified purchasers for over several years, the physician seller’s retirement date is quickly approaching, the seller may have to look at other avenues to be able to retire as planned.

2. The physician seller may approach the hospital to inquire if the local hospital has need of a private medical clinic. The selling physician should notify the hospital shortly after the decision to sell. Most often the hospitals are the first to know of physicians seeking to relocate or make changes in their locale. Notifying the hospital could be a great asset to the sale of the medical practice.

3. If the selling physician does not find a qualified buyer by the time he or she would like to retire, then the selling physician is faced with some tough decisions including closing the practice. There again are some legal requirements to do this such as writing a letter of notification to each of the physician’s patients, and also notifying them whether the selling physician or some other entity will be the medical records guardian as required by law.

4. Should the selling physician close the practice, then there becomes a whole host of new requirements as far as human resources is concerned. Each employee will need to find new employment and all the final payroll requirements will need to be handled.

5. Lastly, the physician who may close the practice without sale, may move directly into retirement. Some requirements are new health insurance, possible social security filings and pension activation.

Conclusion

With this experience, the Clinic Manager was able to effectively research ways to advise the physician partners on how to plan for their succession. Even though the succession may not take place for another five years’ time, the Clinic Manager believes this research was very valuable
and time well spent. She now knows of the importance of preparing and having a succession plan, and then reviewing it annually for relevance and accuracy.

From this experience, the Clinic Manager will advise her two physician partners to begin the process of succession planning. The process will begin with an appointment with the clinic’s attorney. She will also inquire with a medical practice appraiser to gain some preliminary valuation, hopefully at minimal expense. The reason for this caution is that many things can change over the next five years’ time, and performing a full-blown appraisal now would be rather costly and premature. She will begin a lookback over the clinic’s profit and loss statement for the past five years to evaluate the clinic’s net profit per partner. A running report will be maintained hereafter for easy accessibility and review.

Next the clinic manager will need to sit with the physician partners and help them decide how they would like to move forward in the succession planning. The Clinic Manager believes it is best that the two physician partners come to an agreement prior to planning too much as to how they would like to proceed. Some choices that will be offered for consideration are:

1. When does the retiring partner want to retire? Having a firm date helps let all parties know what timeframe they are dealing with.
2. How soon does the physician partners want to have the medical practice appraised? The appraisal will let the partners know the valuation of the practice in order to plan more effectively.
3. Does the retiring partner want to offer up the sale to the remaining partner prior to seeking an outside buyer? This would allow the remaining partner the option to possibly hire on an employed physician allowing the remaining partner to change the partnership to a sole ownership. If the medical practice continues high achievement and great revenue production, this may catapult the remaining physician partner to be able to retire earlier.
due to an increased return on investment. Depending on the purchase price and her return on investment. The remaining partner may want to seek this option. As stated earlier in this manuscript, both partners made all of the correct educated and often calculated decisions that have placed them owning a very thriving medical practice.

4. Lastly, the Clinic Manager would need to identify at the direction of the physician partners, which avenue they wish to go and begin the process. Once the process to seek an outside physician buyer begins, other decisions must be made. Such as will the remaining physician partner be the one picking her partners replacement? How much input will each partner give? Will the selling partner set a price, and will both partners choose the purchasing physician? These are all questions that would need to be planned very carefully via a strategic plan written by the Clinic Manager at the direction of the physician partners.

5. The Clinic Manager will also recommend to the partner physicians to start outlining how and when the recruitment process should commence. Specifics of who they may want to recruit, and start looking into it right away as the average time to recruit to a rural area is about 5-years’ time frame. With her clinic being in a rural setting, which is much different that say urban or suburban clinic in that there is much less chance of recruitment. A few of the many reasons recruitment is difficult in a rural setting are that there is often no suitable employment for their professional spouse, smaller schools may seem less attractive, and there is often fewer entertainment opportunities.

6. In closing, the Clinic Manager would like to point out that staff should be considered at each step of this process. The clinic involved happens to have all certified, long term employees which is rare in the medical community. It ought to be noted that there should be value and consideration for this anomaly.
Works Cited


Personal Interview: Reynolds, Heather, JD, Astoria, Oregon, July 25, 2017

Personal Interview: Wallace, Mike, CPA, Astoria, Oregon, July 21, 2017

Physician Survey 2017 of Small, Rural Physician Owners (see attached)
# Medical Clinic 2016 Profit and Loss Statement

## Ordinary Income/Expense

### Income
- Insurance Refund: -110,324.52
- Patient Fees: 12,153,357.23
- Patient Refund: -112,003.71

**Total Income:** 11,931,029.00

### Expense
- Advertising: 12,647.22
- Bank Service Charges
  - Merchant Card Services: 15,082.18
  - Bank Service Charges - Other: 140.00

**Total Bank Service Charges:** 15,222.18
- Billing: 17,047.05
- Computer Fees: 14,664.99
- Contract Labor: 14,026.28
- Depreciation Expense: 114,847.00
- Dues and Subscriptions: 114,206.67
- Employee Health Insurance: 143,148.66
- Employee Payroll: 1,296,324.56
- Employee SEP Retirement Plan: 146,561.07
- Employee Work Comp Insurance: 11,456.69
- Equipment Rental: 110,015.83
- Guaranteed Payments
  - Medical Staff Guaranteed Payments
    - Medical insurance: 111,288.28
    - Medical Staff Guaranteed Payments: 3,781,433.10

**Total Medical Staff Guaranteed Payments:** 3,892,721.38
- Specialty Staff Guaranteed Payment
  - Medical Insurance: 132,599.58
  - Specialty Staff Guaranteed Payment: 3,921,173.26

**Total Specialty Staff Guaranteed Payment:** 4,053,772.84

### Total Guaranteed Payments
**Total Guaranteed Payments:** 7,946,494.22

### Insurance
- Liability Insurance: 12,560.00
- Malpractice Insurance: 130,182.00
- Insurance - Other: 0.00

**Total Insurance:** 142,742.00
- Laundry: 13,235.90
- Licenses and Permits: 11,688.00

**Total Expenses:** 8,226,825.54

**Net Income:** 11,931,029.00 - 8,226,825.54 = **3,704,203.46**
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Small Rural Physician Owned Clinic Survey Questions:

1. Did you start your practice or buy one already in existence?
2. Were you a new physician straight from residency or had you been practicing already when you purchased/opened?
3. Did you have a succession plan when you purchased/opened?
4. How many years have you owned your practice?
5. Are you a partner or a sole owner of your practice?
6. How many partners are in your practice?
7. Do you manage your clinic or do you have a clinic manager?
8. Do you have a current written business plan?
9. Do you have a current written succession plan?
10. Do you utilize an accountant to assist in your business plan?
11. Do you utilize an attorney to assist in your business plan?
12. How many more years do you expect to work?
13. Anything surprise you about owning your own medical practice?
14. What do you like most about being independent?
15. What would you most like to change about being independent?