

## Chapter 9

### **HIRING AND BECOMING THE ASSOCIATE**

Why would an associate be hired? Because the practice owner needs someone to ease the burden of an extremely busy life, provide coverage for time-off, someone to practice with, another doctor to meet patient and/or referral demand for professional services and another doctor to buy him or her out upon retirement or other departure from practice. Will an administrative profit be made from the associate? Hopefully, although the market trend is to overpay associates. The practice productivity, as well as its profitability, may not be where it should to both pay the associate and earn an appropriate and administrative profit of five to fifteen percent. On top of this, the facility may not be the right square footage to accommodate the practice owner, the hygienist(s), and the associate. Additionally, the practice owner has to take time from your patients in a "one and one-half doctor" practice to mentor and train the associate/apprentice doctor.

Why would a new doctor want to become an associate? Because the new doctor may not have the ability to establish his or her own practice and have a schedule filled for a significant period of time. The new doctor will also probably lack confidence and need the mentorship of a seasoned dentist or specialist.

Do associate arrangements work? Yes. They can and should. The practice owner needs relief from stress with an associate who can truly help ease the burden of a busy practice with potential for growth. The practice owner would typically be pleased to train his or her successor knowing who will treat patients of the practice upon retirement. The practice owner also would like to know that he or she will be welcome to treat patients after "official" retirement on a limited basis, unless retirement will be complete and not partial.

#### **Personality Profiling**

From each doctor's perspective, compatibility will be a key to a successful long term relationship. In this regard, personality testing and profiling is available to assess personality types and compatibility. These testing procedures and tools are effective, inexpensive and easy to use. They are a starting point for accessing compatibility over the long term. It is tried and tested that certain personality types work well with one another and others do not. Staff personalities, and those of the doctors' spouses, are also significant to determine whether the working relationship will be successful in the practice. At a minimum, personality profiling can be a tool whereby the practice owner and associate can discuss their working relationship, philosophical values, personality types and philosophies about work.

#### **Spouse in the Practice**

The non-doctor spouse can greatly influence practice operations; the activities of the doctor(s), the operations of the practice and non-doctor staff members. The relationship between

the incoming doctor, the incoming doctor's spouse, the practice owner and the practice owner's spouse is crucial, especially if the doctor's spouse is the office manager or works in the practice. The doctor's spouse working in the practice is very common, yet the dialog between the doctors often excludes the role of the non-doctor spouse in the practice.

### **Length of Association**

How long should the association last? Some associates will work on a part or full-time basis indefinitely and do not desire to own a practice. Others do desire to make their presence in the practice permanent as owners. For a specialist, the association typically lasts between one and three years. For general dentists, two to four years, with exceptions. First, the associate and practice owner must desire to practice together on a permanent basis. Further, the associate's productivity must be consistently sufficient to both earn an appropriate living for the period when the practice or practice interest is being paid for and meet the financial obligations of paying for the practice or practice interest. Therefore, the date of admitting the associate to ownership status should be based upon performance and not time.

### **Associate Compensation**

Associate compensation can and should be determined in advance of the hiring process through an analysis of what the practice can afford to pay with the owner(s) making a 5% to 15% administrative profit, in light of market conditions whereby quality candidates are difficult to locate. Market conditions currently provide for relatively high compensation to both general dentists and specialists. Why? There is a shortage of incoming doctors, particularly specialty practitioners.

As an example, let's say that the incoming doctor is overpaid. Assume that the practice owner earns 40% of gross revenues as owner compensation in all forms and agrees to pay the associate 35% of production, less 35% of the corresponding laboratory costs. The associate further receives credit for hygiene examinations but not hygiene services performed by the hygienist(s) of the practice. Assume further that the practice pays the associate's malpractice insurance, one-half of individual health insurance premiums and \$1,000.00 toward the cost of continuing education for each consecutive twelve months of the associateship. This seems like a fairly good compensation package for the associate. But how does the associate become an owner? The associate will not want to incur a reduction in pay to become an owner and there is not a sufficient spread between owner compensation in all forms and the associate's compensation to allow for future ownership. Further, the practice owner earns little, if any, administrative profit during the term of the associateship. What if the associate earns 25% of production? Then the practice owner earns an administrative profit on the associate and sufficient profit is available to allow the associate to be elevated to ownership, pay for the ownership interest and not incur a reduction in pay. This assumes that the ownership interest is paid for within an agreed upon and measured period of time, e.g. 5 or 7 years. One way to resolve this compensation problem is to pay the associate the greater of a specified base salary, not a draw, per month or the agreed percentage of "adjusted" production or collections. Adjusted

production is the associate's production, less write-offs, refunds, uncollectible accounts and/or laboratory remakes. Once predetermined production levels are consistently reached, the base salary becomes irrelevant.

There is also a shortage of new doctors who choose to work full-time and own practices, which means a pool of associate doctors who will acquire your practice, in part or in whole, is shrinking. This may result in declining practice values and relatively high associate compensation in both and general and specialty practices, not to mention tremendous difficulty recruiting new doctors in rural and undesirable geographic areas.

It is important to complete an analysis of what the particular practice can afford to pay, given anticipated associate revenues, the 5% to 15% administrative profit, overhead costs with the associate in place including the variable expenses of additional laboratory and supply costs, and perhaps some additional equipment and/or a chair side assistant. In short, what the practice can afford to pay an associate needs to be within its operational budget. If the practice cannot afford the market rate for an associate, the practice owner needs to reorganize the management systems in order to maximize profitability. Further, the practice owner should review the fees which may be too low. After the practice becomes economically healthy, then hire the associate, at a compensation package which the practice can afford to pay. The practice owner should not be fooled into thinking that a high paid associate who takes time to train and mentor will pay a fair value for all or a portion of the practice in the future. Therefore, it is not enough just to hire the associate; the practice owner should authorize his or her advisors to complete the succession planning process, including the practice valuation and the terms, business and tax structure of the future relationship with the associate. The potential associate should expect no less of the practice owner.

What is an appropriate rate of compensation? For a general dentist, 25% to 35% of adjusted production or collections. Another way to pay the associate is 25% of adjusted production, inclusive of all hygiene services. An example of an associate compensation provision is included in Figure 9-2. For a specialist, 30% to 45% of adjusted production or collections may be an appropriate percentage and a base compensation level for certain specialties.

If the practice owner and associate agree to a "draw" against future collections, the parties, particularly the associate, should agree to a provision contained in the employment agreement that the associate does not have to repay the draw should the associate leave the practice. Similarly, if the associate is paid on collections, the employment agreement should contain a provision that collections would continue to be paid for some period of time after the employment term ends and should also provide for an "accounting" of those collections.

For specialty practices, the recruitment process is clearly regional if not national. Associate compensation packages for specialists in all cases, except prosthodontics, are high, but

high associate productivity is also anticipated. The compensation is often increased each year incrementally during the associate period. There may also be a discretionary or productivity based bonus provision.

Compensation, bonuses, benefits and payment of business expenses should be specifically defined in the associate employment agreement. For example, in a general practice, the methodology for payment of laboratory expenses can be handled as indicated in Figures 9-1 A through D. Each method generates a different result. Further, it may be helpful to include any laboratory expense calculation, as well as any bonus provision calculation as an example in a schedule to the employment agreement.

In certain circumstances it may be appropriate to reduce the associate compensation by any expenses and benefits paid on behalf of the associate. This ensures that the percentage of productivity or collections remains at a quantified rate.

Bonuses are designed to economically reward work over and above the standards expected by the employer. In dental practices, bonuses usually take the form of a reward for exceeding a predetermined level of collection or productivity.

Designing a bonus formula only based upon collections or productivity is one dimensional. Consider designing associate bonuses to encourage quality of work, effort, attitude, overall performance, yet consider the cash and financial position of the practice. In short, bonuses should be discretionary for associates. The associate should benefit from such a formula in that other important criteria in addition to productivity, e.g., quality of services, are evaluated. An example of a discretionary bonus provision is included in Figure 9-3.

Because the associate period is a time of mutual evaluation for both parties, the associate can assess the fairness of the practice owner, who is often more generous than necessary, although not always. If you are the associate and you don't like the bonuses or think that the practice owner is being fair, you should leave. You don't want to be an owner with this doctor. Practice owners should evaluate much more than productivity and inadequate performance can take many forms. Therefore, if more than production or collections will be evaluated, design an evaluation form to work from in light of the cash flow and financial position of the practice.

### **Proposal For Employment**

Prior to the preparation of the associate employment agreement, the key terms of the employment relationship can and should be set forth in a "Proposal for Employment" letter. An example of such a letter is contained in Figure 9-4.

## **Associate Needs Analysis**

Does the practice need and can it support an associate? If so, what is the percentage of yearly practice collections available for the associate as compensation? Can the facility support the associate to allow multiple doctors to work comfortably and effectively?

An "Associate Needs Analysis" should be completed by the practice owner and advisor(s), most notably the CPA for the practice prior to the interview. While this text does not include the Associate Needs Analysis, the steps for the CPA to work through with the practice owner are<sup>1</sup>: (a) determine owner profit in all forms; (b) determine the actual overhead rate (in light of the owner profit); (c) determine past growth (on a yearly basis) to assess future growth for the associate and practice; (d) determine a realistic return on investment, e.g., investment in new equipment for the incoming doctor; (e) determine the percentage available for the associate compensation in light of what the market pays in compensation and benefits; and (f) determine the impact on the practice owner's net income for current and future years.

Assuming that the incoming doctor has completed the Qualitative and Quantitative Considerations and the practice owner has directed his or her CPA to complete the Associate Needs Analysis to determine and/or confirm that an associate should be hired, each party is ready for the interview.

## **Associate Interview Questions**

The Associate Interview Questions, Figure 9-5, are applicable to both the incoming doctor and practice owner. While the Qualitative Considerations provide insight for the parties relative to what the incoming doctor wants in his or her career, the Associate Interview Questions provide guidance for a productive interview. Too often, interviews are based on whether "we like each other". While compatibility and "comfort level" are important, the 20 categories of interview questions show that there are important considerations that need to be discussed by the practice owner and incoming doctor. In short, the incoming doctor needs to answer what he or she wants in a practice. The practice owner, on the other hand, needs to know whether the practice can support an associate. The 20 categories of interview questions are designed to assist the doctors in developing a positive long-term working relationship. Quality long-term working relationships are not often attained by accident. They are designed. By asking the appropriate questions of each other after you have completed your initial homework, you will minimize the risk of a failed relationship.

## **The Release Provision**

As part of the interview process, the practice owner should request that the incoming doctor sign a written release as part of the written employment application, similar to Figure 9-6. The release authorizes the practice owner to check the references of the incoming doctor; both

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<sup>1</sup> Building up to Economic Freedom, PennWell Books, 1986, James B. Jackson, D.D.S.

personal and professional. If the incoming doctor has not yet practiced dentistry or his or her specialty, the professional reference check would include discussions with professors. Further, the incoming doctor should be requested to provide at least five written letters of recommendation to the practice owner. Such letters of recommendation may be from professional or personal references. The incoming doctor should also ask the practice owner for references prior to making the decision to join a particular practice.

### **Succession Plan**

Unless a practice owner is planning to hire a permanent associate, the practice owner's succession plan should also be specifically defined prior to interviewing and hiring the associate. This means that the practice valuation and legal documents should be prepared in advance of the associate joining the practice. Why? Because determining practice value and preparing legal documents in advance generally reduces risk of misunderstandings. While there are significant efforts and costs involved in defining the succession plan, preparing the practice valuation and drafting legal documents, the succession plan will be in place, irrespective of the identity of the candidate/doctor who is intended to succeed the owner(s).

The succession exit options available to the practice owner are: (a) sell the entire practice; (b) hire the associate with the obligation to sell and purchase the practice in one to three years; (c) enter into a solo group arrangement, whereby the associate acquires the goodwill attributable to the associate's developing patient base after two to three years, plus an undivided interest in the dental equipment, and where the practices thereafter operate separately under an office sharing arrangement; (d) enter into a co-ownership relationship, assuming that the practice owner intends to work for at least five more years on a full-time basis; or (e) close the door and walk away after working for one or two more years.

If the practice owner chooses to sell the complete practice or closes the door and walks away, the associate won't be hired. Similarly, if the associate will be a permanent full or part-time doctor, the incoming doctor has no need to complete any "due diligence" or purchaser homework investigation.

If the incoming doctor will play any part in the practice owner's predetermined succession plan, the associate should sign a confidentiality letter, similar to Figure 9-7. When the interview process has progressed to an advanced stage, the new doctor should commence and complete the due diligence investigation. Unfortunately, the failure to undertake and complete the due diligence investigation is a significant cause of many failed associate relationships. Think about how difficult it would be to elevate an associate to owner without the associate and practice owner having a thorough understanding of the succession plan, purchase price (or date and formula for its determination) and legal documents that define the business and tax structure.

As an alternative, the practice owner may substitute a letter that outlines the proposal for ownership for the actual legal documents. An example of a proposal for ownership is included as Figure 9-4. However, the alternatives are not as thorough as preparation of the actual

documents. It should be noted that the proposal letter (as well as the documents) are contingent upon the associate's continued employment through the date that ownership is offered. Another alternative to preparation of the succession plan documents would be to include detailed equity purchase provisions in the associate employment agreement.

### **Key Employment Agreement Provisions**

Associate employment agreements alter any at-will employment relationship with the practice, whereby an employee can be fired for any reason, with or without cause. Many states have modified the employment at-will doctrine, giving employees remedies for inappropriate employer conduct.

Associate doctor relationships modify any at-will employment relationship to the extent of an associate employment agreement. So why have an associate employment agreement? Primarily, to protect the practice from dilution of value due to competition by a former associate doctor and to ensure that all parties understand their contractual obligations.

Below are the significant associate employment agreement provisions. These provisions are identical for both general dentists and specialists, except that specialists generally earn more in compensation and benefits than do general dentists and specialists are usually prohibited from soliciting both patients and referral sources. Additionally, specialists tend to become owners earlier than do general dentists.

### **Employment**

The employment agreement should provide for the practice to offer employment and for the associate to accept the employment under the terms and conditions of the employment agreement.

The employment agreement should provide that the entire employment relationship is covered by the employment agreement itself and that in the event of a dispute, no other verbal or written evidence may be admitted to trial other than the terms of the employment agreement. This provision was a key factor in a case which was successfully litigated by my partner, Richard D. Panza, Esq., in *Wall v. Firelands Radiology, Inc.* [1995], 106 Ohio App.3d 313. This case involved a restrictive covenant provision, among other issues, whereby an associate physician was precluded from admitting evidence regarding the employment relationship which was not covered in the employment agreement itself.

The agreement needs to survive its term so that the restrictive covenants/nondisclosure provisions are in effect should the associate leave the practice.

The associate should promise that the associate is not currently a party to any prior employment agreements. In the event that the associate would be violating a restrictive covenant

provision by joining the practice, the practice and/or the practice owner could be arguably liable to the other practice which the associate left for intentional interference with contract.

## **Employment Term**

The employment agreement would commence on a certain date, provided that the associate is licensed to practice in the particular state. The employment term would continue until the earlier of a specified date or as provided in the employment termination provisions.

## **Employee's Compensation**

The compensation section provides for and defines the payment of compensation and any bonuses. The obligation of the practice to pay the associate the compensation and any bonuses should be conditioned upon the associate adhering to the associate's duties and responsibilities, particularly the non-competition/non-disclosure provisions contained in the employment agreement.

There may be a signing or annual non-competition bonus, particularly if the employment term commenced prior to the associate signing the employment agreement. The signing or non-competition bonus provides for the associate's later promise not to compete as contracts need consideration on both sides. If the employment agreement is signed before the new doctor starts working, compensation and bonuses are the consideration for the non-competition/non-disclosure promises made.

## **Employee's Duties And Responsibilities**

The duties and responsibilities section defines the associate's work schedule, full or part-time, on-call time and the authority and responsibility of the practice owner for the activities of the associate/doctor.

## **Employee's Non-Disclosure and Non-Competition Promises**

The non-disclosure promises specifically define "confidential information" such as patient lists/referral source lists, as well as practice forms, business and development plans and computer information. The associate may not retain or disclose this information which is owned by the practice to any outside party during the term of the employment or for an agreed period of time thereafter. The associate should be required to return any confidential information to the practice in the event that the employment terminates for any reason.

The non-competition promises provide that the associate may not compete with the practice during the term of employment or for a specified period of time thereafter within a specific geographic radius. However, often a map is attached as an exhibit to the employment agreement that specifies the restricted area. Further, the associate may not, directly or indirectly, solicit patients and/or referral sources of the practice and may not hire employees of the practice for a specified period of time after the employment terminates for any reason. In those states

where permitted, this section also grants a court authority to redefine the restrictive covenant provisions in the event that the court considers the restrictions too broad.

The incoming doctor may negotiate with the practice owner that the restrictive covenant not commence for some period of time, e.g., four months. Additionally, if the associate is from the geographical area where the practice is located, the associate may negotiate a buy-out of the restrictive covenant based upon the revenues generated by the associate, e.g., 37% of one year's gross revenues.

### **Vacation and Other Time-Off**

The vacation and other time-off provisions provide for vacation time-off, with or without compensation, for each consecutive calendar year or twelve months of the employment term. The time-off may also be non-cumulative and forfeited if not taken within the applicable twelve monthly period. Further, the time-off may not interfere with the time-off anticipated by the practice owner.

Educational time-off may be granted by the employer, with or without compensation, for the associate's attendance at meetings, conventions, seminars, and/or post-graduate courses reasonably related to the associate's duties and obligations under the employment agreement, provided that the time-off is approved, in advance, by the practice.

Other time-off may be granted and paid or unpaid. Other time-off would include military reserve duty, pregnancy leave, time to study for board certifications, moving or relocation time-off, specified holidays, illness or sick days, jury duty or sabbatical time-off.

### **Fringe Benefits, Expenses and Insurance**

The fringe benefits, expenses and insurance provisions provide for any fringe benefits, expenses and/or insurances, health and professional liability, either paid by the practice or the associate during each consecutive twelve month period or calendar year of the employment term. In certain circumstances, the associate's compensation may be reduced by some portion or all of the cost of the benefit, provided that federal tax laws are complied with.

### **Prohibition Against Transfer**

Prohibition against transfer provides that the associate cannot assign the associate's duties and responsibilities under the employment agreement to another. Without these provisions, the associate could arguably assign the associate's non-disclosure/non-competition promises to another.

### **Termination of Employment**

Termination by notice allows either the practice or associate to terminate the employment relationship with advance notice, e.g. 30, 60 or 90 days. However, if the practice terminates the

employment term and does not desire for the associate to continue to render professional services, the employment agreement may provide that the associate will not be permitted to continue work, subject to patient abandonment concerns, and will be paid at a predetermined rate with benefits during any notice period. If the associate is compensated as a percentage of production or collections, the notice period compensation may equal the average monthly compensation for the three succeeding months prior to the month of termination of employment. This compensation, and any benefits, for the notice period should be specifically defined in the employment agreement.

In the event of the associate's death or disability, the practice should retain the option to terminate the employment term. Disability would mean any physical or mental condition resulting from accident or illness which prevents, as determined by the practice in its sole discretion, the associate from performing the associate's then-existing duties and obligations under the employment agreement.

Breach by the associate-employee is a "for cause" termination and should grant the practice with the option to immediately terminate the employment term without notice. Such a provision may read as follows: "notwithstanding any other provision of this Agreement, Employer may immediately terminate the Employment Term at any time and without prior demand or notice if: (a) Employee fails to perform, for any reason, any of Employee's obligations, duties, promises or representations in Section 5, Section 6 or Section 9 [the non-disclosure/non-competition provisions and prohibition against transfer provisions]; or (b) Employee commits a crime against Employer, or any of the Officers, Directors, employees, patients or agents of Employer; or (c) Employee commits any other crime, except a minor traffic violation, or any act involving fraud, dishonesty or moral turpitude; or (d) Employee fails to follow any employment directive or policy issued by Corporation." The point here is, for cause termination should be defined and negotiated by the parties to the employment agreement being signed. Item (d), for example, may include a "cure" period.

In the event that the practice breaches its promises to the associate, the associate should also have the ability to terminate the employment term without notice.

The practice would also retain the ability to terminate the employment term without notice in the event of the associate being suspended from practicing dentistry or the associate's specialty or otherwise becomes disqualified to practice dentistry or the associate's specialty in a particular state. This provision may provide that the suspension or disqualification last longer than a certain period of time period, e.g., 30 days.

Finally, the practice may retain a discretionary termination option which would terminate the employment term without prior demand or notice in the sole discretion of the practice. Such a provision is typically in effect for the first 90 to 180 days of the employment term.

## **Indemnification and Contribution**

In the associate's employment agreement, the indemnification provision may read as follows: "Employee hereby indemnifies and saves Employer harmless from and against all claims, liabilities, judgments, decrees, fines, penalties, fees, amounts paid in settlement or any other costs, losses, expenses (including, but not limited to, attorneys' fees and court costs) directly or indirectly arising or resulting from or in connection or association with any threatened or pending action, suit or proceedings by third-party (whether civil, criminal, administrative, investigatory or otherwise and whether valid or not) and any appeals related thereto, under which the employee is a party or participant because of Employee's negligence or any other actions or admissions by Employee (other than willful misconduct) resulting from Employee's duties and obligations under this Agreement."

## **Miscellaneous**

This section provides for the application of the laws of a particular state in the event of a dispute and provides the place where the dispute will be decided.

## **Equity Purchase Provision**

This section may be included to provide that upon a specified date or earlier if invited by the practice, the associate would have the option to acquire an interest in the practice, assuming that the associate remains employed at such time. This section may provide for defined performance and quality goals to be attained by the associate prior to ownership being offered. The purchase price or appraisal prices, terms of payment and structure of transaction may be specifically set forth. Finally, the equity provisions where co-ownership is offered should be contingent upon the associate entering into a mutually agreeable: (a) owner employment agreement; (b) close corporation, shareholder or operating agreement defining decision making control or "founder's rights" in the event of a voting deadlock or dispute; and (c) buy-sell agreement, providing for the obligation or option of the other owner(s) or practice to acquire the interest of the departing owner in the event of death, permanent disability, retirement, dispute or other termination of employment. The equity provision may also take the form of a freestanding option agreement with the corresponding practice agreements as schedules. Finally, the equity provision may be in the form of a letter of understanding, which outlines the key provisions of the contemplated ownership.

## **Additional Benefits**

This optional section usually provides for the continued payment, if any, of compensation and coverage of benefits for some period of time in the event of death or permanent disability, typically until the disability income replacement insurance is in effect. At times, there may be continued payment of compensation in the event of temporary disability. These payments are typically offset by any disability insurance benefit. In certain circumstances, there may be a period of severance pay which is often conditioned upon certain events, e.g., the departing specialist practicing in California not competing with the practice.

## **Anticipating Ownership**

When is ownership discussed? The earlier the better. To the extent that the parties discuss and determine the fair market value of the practice and the date it is recalculated, the interest being acquired — a complete or partial interest in the practice, the payment terms, the structure of the transaction, the future obligation or option to buy-out any existing owner(s), the less chance there is for future misunderstanding on these complex matters. This process should be weighed against the economic cost of preceding earlier, rather than at a later predetermined date, after the associate relationship has commenced.

## **Independent Contractor Status**

Most associates do not qualify under either applicable state or federal laws as independent contractors. The criteria to determine independent contractor status was set forth in Revenue Ruling 87-41 and is contained in Figure 9-8. In reading through the twenty criteria to determine independent contractor status, you may find that any associate which you have classified as an independent contractor is in reality an employee. This means that the associate should be classified and paid as an employee with applicable taxes taken out of compensation. Some practices have attempted to pay associate doctors as independent contractors to avoid the employer's portion of payroll taxes. This conduct can pose a significant risk to the practice. If the practice owner is going to err on worker classification status, err on the side of classifying the doctor as an employee.

An example of an independent contractor may be an orthodontist rendering professional services in a pediatric dentists practice two days or a week or an endodontist providing professional services in a general practice on certain days and times.

The doctor who sells his or her practice and then provides services on behalf of the purchasing doctor may or may not qualify as an independent contractor. The specific relationship and circumstances should be reviewed on a case-by-case basis to determine proper worker classification.

Associate doctors should be concerned of indemnifying or holding harmless the senior doctor's practice in the event that the associate is classified as an independent contractor. Many independent contractor agreements, similar to associate employment agreements, provide that the associate would hold harmless or indemnify the practice for any costs or penalties relative to the practice's misclassification of the associate as a worker. The bottom line is that most associate doctors are employees, not independent contractors. One method of justifying an independent contractor relationship is whereby the associate doctor charges the patients for treatment and pays the practice an agreed amount for use of the premises.

Practice owners should note that the enforcement of non-competition provisions may be difficult where the associate is classified as an independent contractor rather than as an

employee. If you, as practice owner, are concerned with the associate competing in the event that the associate leaves your practice, classify the associate as an employee and not an independent contractor.

### **Buy-Sell Agreements**

The practice owner may consider a buy-sell agreement for the associate in the event of death or permanent disability. In short, if the practice owner dies or becomes permanently disabled, the associate buys the practice. Insurance should be considered as a funding mechanism, subject to health, costs and availability. In the event of a catastrophe, the practice owner and his or her family members won't have to negotiate the sale of the practice under adverse circumstances. From the associate's prospective, he or she should understand that the deceased or permanently disabled doctor's practice won't be sold to another.

In the event that the association is unsuccessful, the associate leaves and he starts over. From the associate's perspective, confidence and time are lost. Both the practice owner and the associate have much to lose by the associateship not working. Therefore, it is in everyone's interest to do all possible to ensure the long term success of the working relationship.

**Figure 9-1**

**EFFECT OF DENTAL LABORATORY COSTS  
 ON ASSOCIATE COMPENSATION**

**Figure 9-1A**

**Production, Less Percentage Lab, Times Percentage**

1.	Monthly Associate Production:.....	\$30,000
2.	Less, 1/3 Dental Laboratory Costs Attributable To Associate (10% x .33 = \$3,000 x .33 = \$1,000): .....	<\$ 990>
3.	Subtotal: .....	<u>\$29,010</u>
4.	Compensation Percentage: .....	x 33%
5.	Monthly Associate Compensation: .....	<u>\$ 9,573</u>

**Figure 9-1B**

**Production, Times Percentage, Less Percentage Lab**

1.	Monthly Associate Production:.....	\$30,000
2.	Compensation Percentage	x 33%
3.	Subtotal: .....	<u>\$ 9,900</u>
4.	Less, 1/3 Dental Laboratory Costs:.....	<\$ 990>
5.	Monthly Associate Compensation: .....	<u>\$ 8,910</u>

**Figure 9-1C**

**Production, Times Percentage**

1.	Monthly Associate Production:.....	\$30,000
2.	Compensation Percentage	x 30%
3.	Subtotal: .....	<u>\$ 9,900</u>

**Figure 9-1D**

**Production, Less 1/2 Lab, Times Higher Percentage**

1.	Monthly Associate Production:.....	\$30,000
2.	Less, 1/2 Dental Laboratory Costs:.....	<\$ 1,500>
3.	Subtotal: .....	<u>\$28,500</u>
4.	Compensation Percentage: .....	x 35%
5.	Monthly Associate Compensation: .....	<u>\$ 9,975</u>

## Figure 9-2

### ASSOCIATE COMPENSATION

For each consecutive month of the Employment Term, Corporation shall pay Employee a basic salary (the "Basic Salary") equal to the greater of: (a) \_\_\_\_\_ Dollars (\$\_\_\_\_\_); or (b) thirty percent (30%) of Adjusted Production (as herein defined) attributable to professional dental services rendered to Corporation's Patients (as herein defined) inclusive of hygiene examination fees and excluding hygiene services performed by Corporation's hygienist(s). The Basic Salary shall be paid in at least monthly installments during Corporation's usual and customary pay periods and shall be prorated (on a daily basis) if the Employment Term terminates prior to the completion of any monthly period. For purposes of this Agreement, Adjusted Production means Employee's rendering of professional dental services hereunder, less dental laboratory remakes, refunds, uncollectible accounts, write-offs, discounts and reduced fee plans of any nature. Notwithstanding the foregoing, Employee's Basic Salary and any Bonuses (as herein defined) shall be reduced and off-set by the full cost of any benefits and business expenses under Section \_\_\_\_ and any retirement plan contributions made by Corporation on Employee's behalf under Section \_\_\_\_.

**Figure 9-3**  
**BONUS(ES)**  
**(OPTIONAL)**

In its sole discretion, Corporation may, but should not be obligated to, pay Employee a bonus(es) (collectively the "Bonus"). Any Bonus hereunder shall be based upon Employee's overall contribution to Corporation's dental practice, including, but not limited to, Employee's attitude, effort, quality of clinical care, relationships with Patients and staff, productivity and punctuality, and shall further be based upon Corporation's general cash and financial position.

## Figure 9-4

### PROPOSAL FOR EMPLOYMENT

**DRS. SMITH & JONES, INC.**  
[Insert Address]

August 1, \_\_\_\_\_

Dr. Thomas R. Roberts  
[Insert Address]

RE: Proposal for Employment

Dear Tom:

Dr. Smith and I would be very pleased to have you join Drs. Smith & Jones, Inc. (the "Corporation") as a full-time periodontist on or approximately January 1, \_\_\_\_\_, pursuant to the proposal described herein.

I. Term of Employment. Your employment as an associate periodontist with the Corporation would be for a term, not to exceed three (3) years and based upon your production that must exceed \$575,000.00 over a twelve (12) consecutive month period, the "Agreement Term". During such time, the Corporation, its shareholders and you would have the opportunity to mutually evaluate our working relationship and the prospect of working together as shareholders of the Corporation over the long term.

II. Ownership Interest. After completion of the Agreement Term, you would be provided the opportunity to purchase a number of shares of the Corporation's issued and outstanding common stock equal to that of any other shareholder, presumably one-third (1/3) of the issued and outstanding shares. The purchase of your shares in the Corporation would be subject to the preparation of documents mutually acceptable to you and the Corporation.

III. Compensation as an Employee/Periodontist. You would be paid compensation as follows:

- (a) For the first year of the Agreement Term, you would be paid a salary of \$150,000.00; and
- (b) For the second year of the Agreement Term, you would be paid a salary of \$175,000.00.

Additionally, you would be eligible for a discretionary bonus payable prior to the end of each calendar year of the Agreement Term, which would be based upon your total contribution to the Corporation's periodontal practice and further based upon the Corporation's cash and financial position.

#### **Figure 9-4**

IV. Benefits Paid on your Behalf. In addition to your salary, the Corporation would pay the reasonable cost of benefits on your behalf, which would be substantially similar to those of its current periodontist/employees, dependent upon economic and market conditions. Such benefits presently include the payment of:

- (a) Liability insurance premiums;
- (b) Family hospitalization insurance premiums;
- (c) Disability insurance premiums;
- (d) Continuing education costs and associated travel expenses, approved in advance by the Corporation;
- (e) Entertainment expenses;
- (f) Dues and membership fees; and
- (g) Retirement plan contributions (in accordance with the eligibility provisions of the Corporation's profit-sharing plan).

V. Time Off. You would receive three (3) weeks of vacation for each year of the Agreement Term. Additionally, you would receive holidays off and receive certain days off for attendance at continuing education courses.

VI. Expenditure of Time. The position which the Corporation is offering to you requires your full-time efforts. You would be expected to work on a full-time basis in accordance with the Corporation's usual scheduling policies. However, there would be times which you would be expected (during the day, evenings and weekends) to develop referring relationships with general dentists through various non-clinical marketing activities.

VII. Employment Agreement. Provided that you accept the terms of the proposed employment with the Corporation as outlined herein, you would be asked to sign an employment agreement. The employment agreement would be presented to you in the near future for your and your legal counsel's review. The employment agreement would contain provisions relating to your compensation, fringe benefits, non-competition/non-disclosure, termination and responsibilities.

VIII. Termination of Employment. It is the intention of the Corporation's current shareholders that you become a shareholder within three (3) years. However, in the event that the working relationship between you and the Corporation would ever become unacceptable, either to you or the Corporation for any reason, a provision contained in your employment agreement would provide for termination by either party, upon the expiration of thirty (30) days written notice.

IX. Purchase Price. The purchase price for the shares in the Corporation which you would purchase would equal the fair market value of such shares as a percentage of all of the issued and outstanding common shares of the Corporation. Our recent appraisal indicates that the fair

### Figure 9-4

market value of the Corporation is \$900,000.00 and has been reduced to reflect that you are purchasing stock in after-tax dollars. Therefore, the purchase price for one-third (1/3) of the issued and outstanding shares would equal \$300,000.00 as of the date you become an owner of the Corporation (the "Buy-In").

X. Payment of the Purchase Price. The purchase price for the Buy-In would be paid as follows: (a) twenty-five percent (25%) of the purchase price would be paid pursuant to a cash down payment; and (b) the remaining seventy-five percent (75%) of the purchase price would be financed by the Corporation and paid over seven (7) years, at two percent (2%) less than the prime rate of interest then charged by the Corporation's bank.

XI. Operational Control. As an owner of the Corporation, you would share a voice in its operation and control equal to that of any other shareholder.

XII. Non-Binding Proposal. This proposal is not intended to create or impose any legally binding obligations on the part of you, the Corporation or its shareholders. The consummation of the proposal contained herein is expressly conditioned upon and subject to the execution of definitive legal documents, which legal documents must be in form and substance satisfactory to you, the Corporation and our respective legal counsel.

Please carefully review the foregoing with your legal counsel and call me with any questions which you may have relative to this matter. Thereafter, if the terms and conditions described herein meet with your and your legal counsel's approvals, please sign and date below where indicated and return a signed copy of this letter to me in the pre-addressed, stamped envelope on or before August 15, \_\_\_\_\_. Upon my receipt of the signed copy of this letter, I will request that the Corporation's legal counsel commence preparation of your employment agreement in "draft" version.

Dr. Smith and I look forward to your joining the Corporation as an periodontist in the near future.

Sincerely yours,

DRS. SMITH & JONES, INC.

By: Dr. Joseph G. Jones, President

I have read this letter carefully and accept the terms and conditions stated herein.

\_\_\_\_\_  
Date

\_\_\_\_\_  
Dr. Thomas R. Roberts

## Figure 9-5

### ASSOCIATE INTERVIEW QUESTIONS

#### 1. **Mission and Philosophy**

What is the mission, philosophy and clinical quality standards of the practice?

#### 2. **Goals**

Do we share similar goals for clinical excellence, leadership, practice growth and learning the business of dentistry?

#### 3. **Facility Design**

How is the practice facility designed and what are the spacial limitations, if any? —Is the facility clean? —How many treatment rooms are there and how many hygienist(s) work in the practice? Who will work where as compared to current scheduling practices?

#### 4. **Compatibility**

What type of person do I want to associate with and will patients and/or referral sources, as well as staff accept me? How do I give my patients away? Will we be compatible on both the professional and personal levels?

#### 5. **Personality Profiling**

Will we use personality profiling testing to assess our compatibility? —If not, how will we evaluate each other? —At what point in the interview process will the non-doctor spouses meet?

#### 6. **Practice Systems**

How are the systems of the practice managed? A partial list of the systems that should be managed are described in Attachment 8.

#### 7. **Professional Services Performed/Collections**

What procedures and services does the practice owner perform and what procedures are referred? What procedures and services will the incoming doctor perform? —How are the services performed paid for and what is the collection policy and rate of the practice?

## Figure 9-5

### 8. **Work Schedule/Patient Assignment**

What is the work schedule for the practice owner (days and hours)? What is the anticipated work schedule for the associate (days and hours) and how will patient assignments be made? —What kind of patients will be treated by the associate? —Inspect and discuss the appointment book! —Is the practice overbooked and do patients wait?

### 9. **Internal and External Marketing**

What is the internal and external marketing policy of the practice? What are the internal and external marketing expectations for the incoming doctor?

### 10. **Coverage/On-Call**

What are the office coverage "on-call" expectations for the incoming doctor and practice owner? How many emergencies occur on a monthly basis?

### 11. **Mentoring**

How will the clinical and administrative mentoring process take place?

### 12. **Productivity**

What are the productivity and revenue expectations for the incoming doctor?

### 13. **Compensation**

How will the incoming doctor compensation package be structured?

### 14. **Benefits and Expenses**

What benefits and expenses will be paid through the practice versus the incoming doctor?

### 15. **Staff Interview**

What point in the interview process will the staff be introduced to the incoming doctor?

### 16. **Roll of Non-Doctor Spouse and Other Family Members**

What is the role of the non-doctor spouse and other family members in the practice?

### **Figure 9-5**

#### **17. Restrictive Covenants/Termination of Employment**

What are the restrictive covenants and termination of employment provisions in the event that the working arrangement fails?

#### **18. Associate Employment Agreement**

At what point of the interview process will the incoming doctor be presented with an associate employment agreement and what are the terms? —Note, the incoming doctor is probably not an independent contractor.

#### **19. Associate and Future Relationship**

What is the length of the associate relationship and what are the specific objectives for the future working relationship?

#### **20. Purchaser Due Diligence-Succession Planning Documents or Proposal for Ownership**

After signing a confidentiality letter, how will the incoming doctor evaluate the specific objectives for the future working relationship in light of cash flow and debt of the practice, practice valuation and succession plan documents. See the Due Diligence Checklist is described in Attachment 6. Certain of the items in Attachment 6 should be requested to be reviewed or used as part of the preparation or confirmation of the practice valuation.

## **Figure 9-6**

### **JOB APPLICATION RELEASE PROVISION**

I certify that the information presented in this Application is true and complete. I understand that, if hired, my continued employment is expressly conditioned upon the accuracy and completeness of the information I have provided. If I am offered, and I accept, employment, I agree to abide by all rules, regulations and policies which the company may institute from time to time, in its discretion.

I understand that this Application, copies of rules, regulations and policies, and any other company documents, are not contracts of employment, and that either I or the company may terminate my employment at any time, for any reason, or no reason. No representative of the company has made any oral or written statements to the contrary and I have not relied on any oral or written statements by a company representative regarding any employment hereunder.

I authorize the company to contact any of the schools, colleges, employers, and references which I have listed on this Application, as well as any other persons or institutions, and to inquire about my suitability and qualifications for employment with the company. In consideration for the opportunity to submit this application, I agree to indemnify and save harmless the company, all the aforementioned schools, colleges, employers and references, and any other person or institution contacted by the company with respect to this Application, from and against all liabilities, costs, expenses (including attorney fees), charges, claims, fines, actions, causes of action directly or indirectly related to this Application and the company's acceptance or the rejection of the Application. A copy of this authorization and release shall be considered the same as the original.

**Figure 9-7**

**CONFIDENTIALITY LETTER**

[INSERT DATE]

**PERSONAL AND CONFIDENTIAL**

[Insert Name]  
[Insert Address]

RE: Confidentiality Letter

Dear [Insert Name]:

You have expressed an interest in acquiring my dental practice (herein called the "Practice"). As such, you will request and I will disclose to you and your advisors certain financial, tax and operational information regarding the Practice, as well as certain of my personal financial information (herein collectively called the "Confidential Information").

In consideration of my release of the Confidential Information, you agree that: (i) the Confidential Information shall (at all times) be and remain my exclusive property; and (ii) you shall hold the Confidential Information as a trustee and fiduciary for me; and (iii) you shall use the Confidential Information solely and exclusively for the purpose of evaluating the potential acquisition of the Practice. Notwithstanding the foregoing, you are permitted to share the Confidential Information with your advisors.

If negotiations between you and I terminate (for any reason) without the consummation of your acquisition of the Practice, you shall promptly return all Confidential Information to me.

If the terms and conditions of this letter are acceptable, please so indicate by signing and dating the enclosed copy of this letter where indicated on page 2, and return the signed copy to me in the self-addressed, stamped envelope. Thereafter, my advisors will provide you and your advisors with any and all reasonable requests for information, including recent financial statements and Federal Income Tax Returns for the Practice.

I look forward to working with you.

Sincerely yours,

[Insert Name]

I have read this letter carefully concerning the terms and conditions of the Confidential Information, and accept the same as stated herein above.

Date: \_\_\_\_\_

\_\_\_\_\_  
[Insert Name]

**Figure 9-8**  
**Revenue Ruling 87-41**

1. Instructions;
2. Training;
3. Integration;
4. Services Rendered Personally;
5. Hiring, Supervising and Paying Assistants;
6. Continuing Relationship;
7. Set Hours of Work;
8. Full Time Required;
9. Doing Work on Employer's Premises;
10. Order or Sequence Set;
11. Oral or Written Reports;
12. Payment by Hour, Week or Month;
13. Payment of Business and/or Traveling Expenses;
14. Furnishing Tools and Materials;
15. Significant Investment;
16. Realization of Profit or Loss;
17. Working for More than One Firm at a Time;
18. Making Services Available to General Public;
19. Right to Discharge; and
20. Right to Terminate.