

Hiring an associate with a future sale in mind

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Dentists who are planning to retire in seven years or less often think that hiring an associate to admit them as a partner later is a good idea. It might not be. Unless the existing owner plans to practice approximately seven years or more, admitting an associate as a partner may not be a good idea because it usually takes more than seven years for an associate to pay for a 49% or 50% partnership interest.

Assume that the newly admitted partner buys 49% or 50% of the practice through internal financing, with the obligation to buy out the senior partner upon retirement if the senior partner retires in fewer than seven years. The new partner will have paid very little for their partnership interest and then be obligated to complete the buy-out, possibly with insufficient production to pay for it.

Most partner buy-ins are internally financed because lenders generally will not finance a fractional interest without the practice and/or existing partner providing a guaranty, which is not advisable should the new partner leave for any reason. The senior partner may think that a third party can be located to buy their remaining interest rather than have the new partner be obligated for the remaining buy-out. But it can be very difficult to locate a third party who would be compatible with the new partner.

At a minimum, there is a significant risk that the senior partner will not be able to retire when anticipated. In the worst case, the

senior partner's interest may become worthless without a viable candidate.

However, hiring an associate with a future sale in mind provides for one owner and avoids the complexities of partnership. It is a good alternative for a selling owner with a large and growing practice who plans to work seven years or less. An existing owner who sells the practice in seven or fewer years is usually fully paid in cash. After the sale, the former owner may work on an agreed-upon full-time or limited basis and in the same capacity as part-time employment in a complete sale and purchase, which is subject to the discretion of the new owner based upon the need for an additional dentist.

How letter of intent provisions differ in a future sale from a complete sale and purchase

Hiring an associate in anticipation of a future sale is more complex than an immediate sale and purchase because there are additional variables due to the timing of the transactions. Just like in a complete sale and purchase, a letter of intent for a future sale is a written agreement that precedes the preparation of the sale and purchase agreements. The failure to prepare a thorough letter of intent can result in unnecessary and expensive negotiations for both the selling and purchasing dentists, which could have been avoided had the letter of intent been prepared.

The categories of the letter of intent provisions in a complete sale and purchase should include the parties



involved, financial matters, assets purchased or excluded, patient concerns, and obligations and conditions of purchase. All categories are included in the future sale but also include provisions relating to associate employment, calculation or valuation formula of the selling and purchase price, and postsale employment of the selling dentist.

Associate employment

The future purchaser becomes an associate dentist in accordance with the terms of an associate employment agreement. The letter of intent includes the term of employment, compensation including benefits, direct business expenses and insurances, professional duties and standards, work schedule inclusive of emergency coverage, a restrictive covenant, and termination of employment provisions.

Sale and purchase price

A formula for the calculation of the sale and purchase price may be based upon a valuation before the associate begins employment, and a second valuation one year before the sale, which will be the valuation used. The first valuation merely illustrates to the potential associate that an additional dentist is needed. As an alternative, a valuation can be

prepared when the associate begins employment and a second immediately prior to the sale, and the two valuations are averaged. The problem with averaging the two appraisals is that the associate is reluctant to agree to the second appraisal immediately before the sale because they believe their input contributed to the increased goodwill value. Additionally, an appraisal just before the sale often results in difficult negotiations, which take time and involve additional advisory fees.

The purchase of equipment and technology is by mutual agreement of the selling and purchasing dentists, except for equipment or technology breakdowns with the replacement items purchased at the discretion of the selling dentist. The price of any new equipment or technology is typically valued on a 10-year, straight-line basis.

Postsale employment of the selling dentist

The postsale employment of the selling dentist in a future sale is distinguished from a complete sale and purchase because there must be a sufficient patient load to hire the associate. This means that the new owner will usually want the selling

dentist to continue to work to transfer the goodwill purchased, and until a worthy associate can be recruited by the new owner. To the extent that the selling and purchasing dentists can do so, it is beneficial to include all the terms of the anticipated future employment, subject to the purchasing dentist's need for an additional dentist, the desire of the selling dentist to continue to work on a predetermined schedule, and the selling dentist's health at the time of the sale.

Any contingencies affecting the postsale employment should be included to the extent possible, including unexpected family emergencies or issues, work autonomy, and operational disputes. The selling dentist should not want hold-backs of the purchase price based on the selling dentist's postsale continued employment and especially based upon future collection goals that the selling dentist may not be able to control.

The Federal Trade Commission's ban on noncompetes

However, a caveat to hiring an associate with a future sale in mind is that on April 23, 2024, the Federal Trade Commission (FTC) issued its final rule that effectively prohibits

all noncompete provisions, except for the sale of a business and for senior executives earning more than \$151,164 annually that are currently in existence. Several lawsuits have already been filed and more are expected challenging the noncompete ban, which will hopefully be successful, but at least is anticipated to delay implementation of the ban. Until such time, however, noncompetes can remain in effect subject to state law.

Summary and thoughts

A future sale is a good alternative to a short-term partnership where the practice owner does not plan to work more than seven years. With a future sale, a letter of intent is crucial due to the additional variables not present in a complete sale and purchase. **DE**

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