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Buy-Sell Agreements for Healthcare Practices

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For many healthcare practice shareholders, buy-sell agreements hold about as much near-term importance as estate planning. They know that it is important but the issue seems so far away that they would prefer to put it off until later. However, putting off a buy-sell agreement can cause major problems if the event (e.g., death of a shareholder) comes sooner than expected. It is certainly much easier to address these issues while all parties get along rather than deal with disgruntled shareholders or the heirs of a deceased shareholder.

A buy-sell agreement is intended to provide for the continuity of ownership and, hopefully, the future continuation of the practice. These agreements usually address several key issues:

Who can buy a departing shareholder's share? It is important to consider if the purchase is limited to shareholders or if outsiders can be owners. The buy-sell agreement can be designed to fulfill the wishes of the shareholder, which is very important for an asset that may have taken a lifetime to build.

What can trigger a buyout? The review of "trigger events" may take some time to consider. In addition to death, disability, or retirement, other reasons to purchase the business may develop, such as shareholder disputes and personal reasons (e.g., divorce or bankruptcy). These events should also be considered in terms of how the practice is valued under each scenario.

How will the buy-sell be funded? Business succession specialists often recommend that a buy-sell agreement should be funded, at least partially, with life insurance, since most purchasers do not have enough cash on-hand. If a life insurance policy is desired, a valuation will likely be necessary. Once a value is set by an appraiser and agreed on by all shareholders, the amount becomes the value used for the buy-sell agreement. Of course, certain trigger events, such as divorce, will not be paid for via a death benefit at all, so other funding vehicles should be considered.

How will the practice be valued? The actual valuation of the practice is, of course, a critical element. Purchasers often have a very different idea of what a practice is worth versus an owner. A valuation can be used to determine the purchase price for a shareholder's interest in the partnership, which can be a fixed price, a formula or a valuation process completed by a valuation professional. Valuation firms consider several methods in valuing a practice, including market (i.e., similar practice sales), income, and asset-based valuations. To avoid litigation, a fair and clear valuation process is important, as well as other stop-gap measures to resolve disagreements. Your business valuation professional can explain all of these issues and how to best deal with them in your situation.

What process will be used to purchase the practice? The actual process used to purchase the practice can be specified in the buy-sell agreement, such as a cross-purchase plan or a repurchase plan. If funding is from a life insurance policy, certain structures are established to facilitate this process.

Since the ownership interest in a practice is often the largest financial asset of the shareholder(s), it is crucial to seek the advice of qualified advisors in structuring your buy-sell agreement. Contact HMWC CPAs & Business Advisors with your questions.

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