WHY THE SALE OF A MEDICAL PRACTICE WILL OFTEN TRANSFORM PHYSICIAN "ENGAGEMENT" INTO PHYSICIAN "INVOLVEMENT."

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Private equity has entered the medical practice marketplace once again. While deal structures vary, there are many commonalities to the basic models regarding acquisition and operating model designs. With each transaction, there are gains and losses for both buyers and sellers, where the buyer gains risk, and the seller sells risk and loses commensurate control. This case study will focus on another foundational loss for both buyer and seller that is too frequently dismissed as unimportant to both, that loss is physician engagement.

After examining more than one type of buy-side transaction proposal, we have recognized that sellers are often motivated to sell because they are promised two things from buyers: (1) the buyer will take on a significant amount of the seller's financial risk, and (2) the buyer will lend business expertise to better run the seller's practice. In the proposed transaction, an important, and arguably essential dynamic is traded-away; that dynamic is "physician engagement." Physicians will trade "engagement" for "involvement." Although the difference may not at first seem important, it is very likely the most significant factor leading to both seller's and buyer's remorse down the line.

Let's return to the motivations for sale to understand this dynamic and its importance better. In almost all these transactions, the fundamental motivator for the seller is this promise from the buyer:

"You won't need to worry about a thing after the sale. You practice medicine, and we will take care of the rest."

Sellers are relieved of the very dynamics that kept them engaged as owners and providers in the first place if this promise from buyers is fulfilled. This arrangement reduces the importance of running their practice as well as possible to minimize risk and optimize reward (reward including and beyond the financial.)[1] We asked an executive operating a private equity-backed medical practice how he expected to keep physicians engaged now that they operate as contracted employees instead of owners. His answer was:

"The doctors have a compensation plan based upon their production of collected, professional revenues. If they don't produce, they don't get paid. In addition, they have stock in the larger company that acquired their practice."

We would argue this strategy will not keep the former-owner providers "engaged." The flaw in this buyer's logic is they believe that physicians motivated by self-interest will behave in a manner required to achieve organizational success. When the group was owned and operated by physicians, they each understood their success was dependent upon the success of the group as a whole. They had to be engaged interdependently for the group to be successful. Now that the risk has been shifted to the buyer, and the physicians are each paid according to their individual productivity (as defined above), their priority becomes the success of "their practice," rather than that of the group overall. They are now merely involved in the workings of the clinic, looking out for their self-interests, and are not engaged with keeping the overall practice successful.

For physician sellers who enter into the buy/sell transaction with eyes open wide, the observations and related opinions and perspectives presented here may not be useful. For potential physician sellers who recognize the risks, as described, and remain intrigued by the prospects of a sale of their practice, three questions should be asked and answered by individuals in the group as it proceeds to sale:

1. "How much control is required after the sale, especially if the terms of the sale require a longer-term, legally enforceable, commitment to stay with the group to reap the full value of the financial rewards offered?"
2. "To what extent is the promise of financial rewards "down the line" meaningful; i.e., if they evaporated, would the loss be "too much"?
3. "Are there terms and conditions in transaction documentation that would cause one or all sellers to experience significant loss beyond the financial; loss of high-value intrinsic rewards enjoyed as an owner?"

Partial answers to the questions presented can be gleaned from the proposed closing documentation. Especially, the purchase agreement, the management services agreement, the employment agreement, any related non-compete covenants, and the compensation plan.

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[1] Zismer, D, K.; "Discussion; Framework to Gauge Physician Burnout"; Physician Leadership Journal, (PLJ) vol. 6, issue 3, May/June 2019, PP 50-54