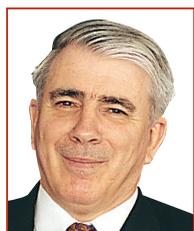


Conflict resolution: Associateship disputes, partner disputes, marriage property settlement disputes

By Graham Middleton, BA, MBA



“Legal duration is proportional to value of assets and value of assets proportional to legal fees... If a couple has minimal net assets, the lawyers generally advise a quick settlement!”

Whether it's two or three dental specialists in a joint practice who decide they're incompatible or a couple of orthodontists locked in differences with a third partner about to retire, or three or four dental associates with a practice structure and income distribution model which destroys individual initiative and practice profitability, the reality is that dentists and dental specialists are far from immune to situations resulting in frustration, conflict and stalemate. If not resolved, these situations fester, creating heightened mistrust, undermining of staff relationships, reduced profitability and loss of professional enjoyment of practice.

Lawyers tend to inflame matters

In 27 years of dealing with dentists and dental specialists, it is my overwhelming experience that involving lawyers, particularly early in a dispute, leads to heightened mistrust.

I've yet to meet a lawyer with sufficient knowledge of the dental profession, let alone its specialist areas, to comprehend the differences between good and bad business structures, or to fully understand what should and should not be written into an associateship agreement or indeed the process

of getting to a sensible associateship agreement. Involving lawyers in a dispute, particularly early in the matter, is more likely to extend and inflame than to resolve.

Dental divorce - property settlement

Unfortunately, dentists are as prone to personal relationship breakdowns as the rest of society and some family law specialists, aka divorce lawyers, are adept at throwing petrol onto the mistrust which already exists between two people whose personal relationship has broken down. Indeed, some lawyers prolong disputes and this fattens the fee file. Lawyers tend to come in quads, meaning that each party quickly ends up with both a solicitor and a barrister, the barrister asking questions of the solicitors and the solicitors firing demands at the other solicitor to pass to the other barrister for comment, creating a nice round of legal correspondence with referral out to various valuers and experts. Inevitably, when another 30 June passes, this generates demand for new accounts post 30 June which may take several months to obtain, which then generates demand for revaluation of the practice... and so the matter drags on. It's not unusual for such matters to drag on for three years and cost the parties several hundred thousand dollars.

The economic law governing legal fees in divorce

Long observation has taught me that the duration of a marital property dispute is directly proportional to the interests of the lawyers involved in finding new issues to challenge the opposing party about. In turn, this is directly proportional to the value of the joint assets, which in turn is directly related to the total legal fees involved in reaching settlement. Therefore, we could come up with a formula which says: “Legal duration is proportional to value of assets and value of assets proportional to legal fees.”

If a couple has minimal net assets, the lawyers generally advise a quick settlement!

Orthodontists in dispute

A group of orthodontists is in dispute. The continuing orthodontists who have potentially quite a few years left in practice are contemplating buying out the practice equity of a group member who is wishing to retire. There are disputes concerning the effect of the existing partnership agreements as to fee sharing and the value of the older specialist’s declining practice element. The dispute reaches an impasse. A searching and expert valuation is completed. Both buyers and sellers and sellers’ lawyers/accountants subject it to critical analysis and determine that it is unlikely to be successfully challenged. The continuing orthodontists buy out the retiring one’s equity at that valuation and the practice moves on. In retrospect, each of the parties recognises that prolonging the dispute had been unpleasant for all of them.

Incompetent valuer inflames and prolongs marital property settlement

A marital separation occurs and the two parties appoint solicitors. The solicitors agree on a valuer, but the accountant they appoint, while having had experience in the valuation of other types of businesses, completely lacks any knowledge of dental practice performance. His valuation is clearly wrong and favours one party heavily. The other party calls for expert analysis and the flaws and gaps in the valuation are exposed. This prolongs the whole process, but eventually the two valuers are directed to consult each other. The first

valuer cannot sustain his position. The parties finally agree to settle on a second valuation. They too can subsequently get on with their lives. The lesson here is that dentists or spouses of dentists in this situation need to have a valuation done by acknowledged experts in order to resolve the matter more quickly. A trap for the unwary is that many solicitors have relationships with particular accountants and even though they have never valued practices, their names tend to get put forward. It’s vital to ask what expertise the valuer or valuing organisation has before agreeing to a joint valuation. Unless they have valued hundreds of dental practices and have a wealth of data on dental practice performance, it’s best to pass them over.

Objective of a good dental practice valuer

The objective of a good valuer is to produce reports which lead to quick, out of court settlements because the respective parties and their lawyers recognise that they are unlikely to be challenged successfully in front of a judge. Many years of valuation experience and a strong database of dental practice performance are prerequisites to good valuation.

Incompatible dental specialists

Two specialists share a practice. The practice has two major locations and also offers occasional sessions elsewhere in general dental practices. Their personalities are diametrically opposed, which leads to lots of disagreement. One specialist tends to have an excitable personality and creates a fuss over inconsequential matters. The other knows how to press the button to set his associate off. It’s apparent that they cannot continue together. It’s also apparent that the two major locations will have to be allocated one each, but the question is which to each? There are also squabbles over equipment, staffing and the minor locations. They seek advice and patient consulting with periodic joint meetings, followed by individual meetings resulting in issues being clarified and bit by bit, they are crossed off the list. It’s slow, but progressively the separation takes shape. A couple of contentious issues are resolved by a toss of the coin. The excitable specialist’s lawyer tries to buy into the argument but is told “you can do nothing to resolve this

matter; rather all you can do is add to the dispute, so please go away”. The lawyer retreats to the sidelines. Eventually the practice is separated.

Business structural failure within dental practice

An associated dental practice of several principals has a weird way of sharing costs and income, which removes the incentive for each associate to work harder. As a consequence, the entire practice is suffering. Weaknesses are discussed during the valuation of one of the associates’ portion of the practice and leads to a subsequent request for assistance in changing structure. A revised structure creates incentive for each principal dentist to generate greater effort in order to reap greater rewards and the effect is that the entire practice lifts.

False valuation and false representations re price and value

An entrepreneurial dentist with a wide variety of external activities and businesses gets into financial trouble. He has a large, multi-location practice which is superficially impressive but has significant inefficiencies. He knows a partner in an accounting practice which has had some connections with the dental profession and happens to be in a pool of valuers of a particular bank. The accountant concerned values the practice at an enormous value. On subsequent close reading, the numbers don’t connect. However, all the banker looks at is the bottom number. The entrepreneurial dentist approaches the more accomplished employed dentist in the practice and offers to sell him a third of the practice at an astonishingly high sum supported by the valuation. He hands the dentist the valuation and tells him to talk to a particular person at the bank who will lend him the money to buy into the practice. A transaction occurs and enables the entrepreneurial dentist to pay out some of his debt. However, the practice does not produce the promised return; in fact, far below it. Meanwhile, the entrepreneurial dentist tries the same approach on a second dentist, again offering him the valuation and advising him to approach the same banker. However, the second dentist decides to take external advice. Synstrat values the practice and pulls apart the other valuation, which is revealed as being

extraordinarily misleading. The second dentist shows his report to the first dentist and a veritable explosion occurs when that dentist realises how seriously he has been misled. Subsequently, a legal settlement occurs with the first dentist. Meanwhile the second dentist has departed the practice.

Conflict over premises

A frequent problem leading to disputes between practice buyers and sellers is the value of the dental premises. Since most dental premises pass from dentist to dentist, real estate agents are rarely involved in their sale. Real estate valuers rely on real estate agents' data to back up their valuations. Lacking data on the sale of dental premises, their reports constantly refer to sales of medical practice premises, usually relatively small ones. Unlike dentists, medical general practitioners have negligible equipment and refer out almost all procedures to medical specialists, radiologists, physiotherapists, etc. By contrast, dental practitioners spend their days doing procedures and have large amounts of equipment. The large amount of dental equipment creates the need for large amounts of hidden plumbing and wiring, as well as lots of cabinetry. Often many hundreds of thousands of dollars are involved in large, multiple surgery dental practice fit-outs. The comparisons with medical practices are invalid, but try getting a licenced valuer to admit that they are wrong. Conflict is best avoided by determining in advance what actual sales of dental premises the valuer can cite and agreeing with the other party that only valuations which cite market evidence of sale or arm's length rentals of dental premises will be used as a basis of valuation.

Energetic vs lazy dentists

There are frequently situations where dental associates are deeply unhappy with each other and common causes are:

- One complains that they shoulder the complete responsibility for running the overall practice, controlling costs, checking infection control protocols are being observed, overseeing ongoing repair and maintenance and supervising staff, while their associates are content to do dentistry but leave the administration to them; while
- Conversely, some dentists complain that their associate crowds them out of all decisions and is overly controlling.... *OR*

- There are differences as to preferred practice hours, utilisation of staff, incompatible fee schedules, capital expenditure and need for an uplift of practice appearance.

Each associateship is unique

Subtly, all associateships are a little different and often the cause of dispute lies in either lack of clarity as to how the associateship is to function, or a failure to review their relationships when an older associate retires and a new one enters the practice. Young dentists buying an associateship need to understand that they need to come to two agreements, one being the conditions of the buy/sell agreement with the departing associate and the other being the associateship agreement with the continuing associate(s). If you don't do this at time of buy-in, it can become very difficult to do it later and often poorly worded associateship agreements which have lain in drawers for many years contain the seeds of later dispute.

The wrong approach to associateship agreements

It's a mistake to ask a lawyer to draw up an associateship agreement unless the associates have been properly advised on the matters to be considered by an experienced non-lawyer adviser and guided through possible ways each issue can be handled. In the process of considering the issues, they have gathered recommendations, considered them and given feedback, then reached a decision. At the end of the consultative process, when they understand how they're going to deal with each of the key issues, they can then instruct solicitors to embody it into a legal agreement, but not to change the impact of any of the paragraphs. Too often, the process is undertaken by lawyers who mistake dental associateships for partnership, then adapt from a template of other partnerships in local small businesses, which are totally irrelevant. The document they produce is unhelpful and when an actual dispute occurs and the parties dive for their copies, find that it is impractical or that it leads to further disputation or a lawyer advises that since much of the associateship agreement has been set aside by other decisions over the years, it may now lack legal force. Prevention is better than cure, so go through a proper process of forming an associateship agreement in the first place.

Beware resolution templates

Lawyers have a habit of writing into associateship agreements a clause to the effect that in the event of a dispute, the matter will be referred to a legal mediator. To adopt such a formula up front is a serious mistake. Lawyers should only be involved after a series of prior steps have occurred. Generally, those prior steps will solve the problem and the issue never gets to lawyers.

Legal mediators usually prefer to deal with parties represented by lawyers and hence those who approach a legal mediator have usually proceeded through a minefield of solicitors, barristers, expert accountants and other advisers for each of the parties. By the time the legal mediator gets to deal with the parties, there is a very expensive group of people sitting on both sides of the table in the meeting room. Furthermore, I'm yet to meet a legal mediator who actually understood the nuts and bolts of a dental practice. Usually, mediation results in a resolution arrived at through sheer inertia but which bears little or no resemblance to the issues or damages being claimed by the parties. Most parties to legal mediations look back on them with horror and recognise in hindsight that it was a very expensive and delaying pathway to follow. Associateship agreements need to include multiple dispute resolution steps in order to create a pathway whereby disputes will inevitably be solved long before the involvement of lawyers. When disputes occur, this lessens the risk of disruption to practice harmony and is inevitably cheaper.

Decisions not being shared

This came about in a veterinary practice but similar situations occur in dentistry. A young veterinary surgeon buys into a practice with two other partners. One of the partners is aged 62 and does things his way. A second partner is 40-plus and has been there for some years. She also likes to do things her way, as well as jealously guarding her role as partnership manager. The younger veterinary partner finds himself frozen out of decision-making. The other two take decisions assuming that he will agree. It becomes obvious to staff that things are happening without his knowledge, sometimes including the purchase of relatively expensive new items of equipment which he didn't know had been ordered. The practice badly needs renovating, its fee

scales are outdated yet it does first-rate surgery. It needs to promote its skills actively, but the two older partners are uninterested in practice promotion and are resistant to change. Eventually the young veterinary partner can stand it no longer and wants to leave, even though other profitable practices for sale are very hard to source. He asks for valuation assistance and we advise him that he must confront the issues he has, particularly with the older vet. Hopefully this will lead to a modified approach and ideally the older vet will sell out and simply work as an employed vet in the practice. Under such circumstances, while there still may be difficulties, a partnership between two is going to be much easier to manage than a partnership between three. We see many similar problems in dental associateships. Leaving aside the fact that there are practical reasons why veterinarians have partnerships and dentists have associateships, this scenario also occurs across the dental profession.

Astonishing over-valuation

This particular example occurred in respect of a valuation in a regional centre by a local accountant of a solo medical surgical specialist practice for marriage settlement purposes. It could just have easily have been a dental specialist. The accountant concerned valued the practice at close to \$1 million. Subsequently the surgeon's solicitor approached Synstrat. After speaking to the surgeon at length and seeking evidence, we determined that not only were the number of surgeons in the particular specialty quite limited in number, but that the individual practitioner concerned was one of only three in the whole of Australia who performed a particular operation and as a result, received many of his referrals from his other specialist colleagues. The reality was that he had an unsaleable practice. The accountant concerned had done his valuation entirely from financials without speaking to the surgeon. Inevitably that valuation was thrown out but only after a long, expensive delay.

Wrong dental practice classification

An accountant not known as a dental practice valuer received an assignment to value a specialist practice in one of the specialties having very low numbers of prac-

tioners. So unfamiliar was the accountant with dental practice that he quoted secondary and tertiary sources of general dental practice data, the source of which he was not prepared to identify. He came up with a substantial practice value. At no time did his report discuss the nature of the practice and had he actually spoken with the practitioner, he would have realised instantly that he was valuing on an unrealistic basis.

At primary fault were the respective lawyers who had agreed to select the valuer from a list of forensic accountants without asking how many dental specialist practices they had valued. This led to the selection of a valuer who had no idea what went on in the dental profession, let alone its specialties and this led to significant delays in settlement as the valuation had to be set aside. Considerable extra involvement of lawyers occurred, with substantial additional cost.

Quick settlement depends on selecting a valuer with such experience and data that their report is unlikely to be able to be challenged and is therefore accepted as a basis of settlement.

Ill-informed banker causes conflict over value

A couple of older dentists are associated in a long-established and profitable practice which employs a couple of younger dentists. Over time, one of the younger dentists stamps himself as a potential practice owner. One of the older dentists proposes to sell his associateship to this dentist, with the approval of the other associate. The price asked is within the bounds of the current market for practice associateships of similar fees in comparable locations.

The younger dentist approaches a well-known finance provider and a particular loans officer offers the comment that the practice price appears to be expensive. The consultant does this without examining the financials. As a result, doubts are created as to the fairness of the older dentist's offer and considerable delay occurs. Eventually as a result of the continuing associate indicating that he wants the matter resolved to restore harmony in the practice associateship, it is independently valued and the valuation proves the initial offer to have been below market price.

As there are a wide variety of good and not so good practice transactions occurring over time, a bank's loans officer who

sees a couple of poor practices exchanged for a valuation which occurs at a low proportion of fees can easily be mistaken that when a profitable, well-established practice comes along, it is over-valued. Often nothing can be further from the truth.

Naïve banker lends too much, leading to disaster

Bankers tend to come in two varieties. The first variety doesn't really understand your dental practice business and refuses sensible financing requests, which is frustrating.

The second variety press money on clients without sufficient regard as to whether their practice has generated enough free cash flow to service the loan and allow the practice owner to pay other expenses and fund a modest lifestyle as well.

While those who won't approve sensible loan requests are frustrating, the second variety are a danger both to the bank which employs them and the dentist who borrows too much.

In the aftermath of the Medicare Chronic Disease Dental Scheme debacle, dentists who built their business plans on a heavy reliance of this scheme's funding had a substantial reduction in income. Prudent dentists who had established patient lists with little dependence on government schemes suffered little effect.

What the sudden change did expose was those dentists who had relied on overly optimistic valuations in purchasing practices and those bankers who simply accepted a bottom line figure without analysing how the income was earned.

In particular instances, dentists who undertook expensive fit-outs and equipment purchasing based on "blue sky" assessments of practice income and growth have been rendered insolvent. Some bankers have relearned an old lesson about understanding their clients' businesses.

In a few cases, dentists whose practices are now worth significantly less than the cost of fit-out and equipment and who have insufficient fees to generate the cash flow to meet their financial commitments are insolvent. The best that they can hope for is if they get to a liquidating accountant first, that liquidator may be able to do a deal with the bank on the basis that a debt write-down and partial payment is better than taking possession of the practice and trying to sell it. Selling such a practice

without the principal dentist remaining for a handover with the risk of that dentist being employed elsewhere in a local practice is poison to buyers.

Ethical disputes involving treatment of patients

Such matters need to be nipped in the bud quickly by other dentists in a practice. If not dealt with quickly, they become culpable of condoning the practice.

Unethical behaviour of one associate towards another

A dentist sells their practice to an assistant dentist who then employs the vendor. The vendor works for the new owner for several years, during which time the exclusion clause arrangement expires. One day, the vendor dentist says to his employer "I'm leaving the practice with effect from tomorrow". Subsequently they re-establish themselves with a dental colleague nearby. All the patients that had been booked to the vendor dentist's surgery are suddenly cancelled and subsequently it is found that they reappear in the vendor dentist's book in the new practice.

A forensic computer expert determines that large numbers of patient records were downloaded from the practice computer after hours to a computer owned/controlled by the vendor dentist. Furthermore, building security system records reveal that the vendor dentist had entered the practice after hours when this occurred. Initial legal advice to the practice owner was that as the exclusion period had expired, he had no case.

Subsequently I was able to advise the dentist that it wasn't a matter of exclusion zone but rather a matter of theft of practice records. In due course, lawyers were involved and after a lot of delay and expense, the vendor dentist paid a substantial sum to the purchaser of his practice. Unfortunately, that sum did not fully compensate the purchaser for the loss of fees as well as all the expenses associated with seeking redress.

Bad sale contracts

The owner of a vibrant practice employs a number of other dentists and decides to sell part of the practice to the two best performers. After a thorough valu-

ation, a price is agreed on the basis that each will purchase an associateship. So far so good. The vendor dentist appoints a solicitor from a substantial legal practice to draw up the contract of sale. The solicitor doesn't understand the concept of a dental associateship and produces a partnership sale contract. The vendor's accountant and practice bookkeeper start structuring a partnership. Fortunately in advising the purchasers, we recognise the problem and see from voluminous correspondence that the deal is getting off the rails. A meeting is called of both vendors and purchasing dentists, their accountants and lawyers and the contract is modified. The expensive lawyer who drew up the wrong contract and partnership agreement has to rework the matter. The outcome is good but leaves us wondering how many dentists have been drawn down the wrong path by uninformed lawyers.

Falsified accounts for family law purposes

A couple of solicitors engage us to do a joint valuation. When the accounts are presented, the practice expenses are highly unusual as a percentage of fees. Close examination reveals that practice purchases lie well beyond the percentage of fees displayed in the extensive range of practices in our database. As appointed joint valuers, we have a duty to ask for an explanation, but none is forthcoming. We then ask for supporting data, such as suppliers' invoices. That too is not forthcoming. In due course we have to report to the respective solicitors that we have been unable to complete our task. The matter is raised in a preliminary hearing by the solicitor of the non-dental marriage partner. The family court judge then rings us to confirm for herself whether the information requested by us has been supplied. Obviously we have to say that it hasn't. The dentist concerned has destroyed their own credibility.

Doctored MYOB accounts

Most dentists are scrupulously honest when dealing with practice buyers, but on odd occasions over the years we have found situations where buyers have come to us with MYOB type accounts printed off by the vendor, but not supplying the year-end accounts as prepared by practice accountants over

the past three years. When asked for these, in particular instances they have not been forthcoming, indicating that the vendor dentist concerned felt that they had something to hide. Proper valuation requires us to examine accounts prepared by practice accountants precisely because they have been subjected to third party scrutiny and if necessary, the supporting tax returns. It's necessary for us to check whether there have been unusual variations over a period of three years and seek explanation. This has particularly been the case recently because of the cessation of the Medicare Chronic Disease Dental Scheme. It's also prudent for the buyer to check recent and forward practice patient bookings and fee structures and ask to see the most recent BASs. It's far better that buyers determine these matters prior to signing a contract. Trying to achieve legal redress after having taken over the practice is an expensive and slow process and by no means guaranteed of success.

Incompatible dentists

A successful dentist sells an associateship to his employed assistant dentist. The vendor has a high profile and ran the practice in a particular style. He automatically assumes that on becoming an associate, his former assistant dentist will be content to work in the same manner as she has in the past. However, the new associate has a stronger personality than he may have anticipated. She stands her ground on some key issues. He views her as obstinate, while she views him as domineering. In its own way it's the old story of the (almost) irresistible force meeting the (almost) immovable object. Long and patient consulting takes place, with at times new disputes breaking out over often minor matters.

It's obvious from the beginning that the associateship cannot last, but it takes a long time to get to the point where the original owner buys out the newer associate at a premium to the original price. She leaves the practice and after a relatively short exclusion period gains employment in another practice nearby. The once-again owner of the practice in which he had been an associate continues to conduct a high profile practice successfully. Probably both recognise in retrospect that their associateship was incompatible from the beginning.

About the author

Graham Middleton personally has been advising dentists on strategic, practice management, valuation and conflict resolution processes for 26 years, the last 19 as a founding partner and director of Synstrat Management Pty Ltd and Synstrat Accounting Pty Ltd. He was once a regular army officer, and later Director Human Resources Manager, Attorney General's Department of Victoria. He is considered an expert on dental practice valuation and practice performance benchmarking. He has spent many years advising dentists in respect of their business and financial strategy and measuring their practice and financial performance. He is the author of the Synstrat Guide to Practice Management, 50 Rules for Success as a Dentist and Buying & Selling General & Specialist Dental Practices. He is a long-term contributor to the Australasian Dental Practice magazine. The Synstrat Group is an independent data-based organisation providing management, benchmarking, valuation, financial and accounting services to the dental profession. Synstrat Management Pty Ltd is a Licensed financial services company owned by its directors who work within the Synstrat Group. For more info, call (03) 9843-7777 Fax: (03) 9843 7799 visit www.synstrat.com.au or email dental@synstrat.com.au.

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