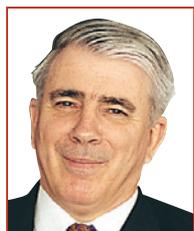


When associateships break down into legal conflict

By Graham Middleton, BA, MBA



“None of the employed dentists... own goodwill. They have no property rights in respect to the practice name, website, telephone number or equipment... and no right to remove practice records without agreement...”

Bryan was an old-school Sydney dentist. He had achieved good results at dental school, joined an established practice and after a few years, bought an associateship in that practice. He’d also given back to his profession, having done a period on an ADA committee, taught part-time at the dental school and become an examiner of dentists. Over the years, he became the busiest dentist in the practice. Bryan had an older associate, Henry, who had slowed his output down to about half that he had at his peak. Henry eventually sold out to an employed dentist, Denzel. At the time of Denzel’s purchase, Bryan was at his zenith and had the largest referral base in the practice. After he bought Henry’s associateship, Denzel’s referral base improved due to the overflow of referrals of Bryan’s patients, but it was still well below Bryan’s.

Structure of the practice

The practice now consisted of the two associated owners, Bryan and Denzel, plus three employed dentists working two and a half; two; and one and a half days each, plus an hygienist working four days per week. The employed dentists and hygienist together shared two surgeries. Bryan and Denzel each had a dedicated surgery. Bryan and Denzel owned the premises.

Bryan’s production

Bryan had long understood that the production in his own surgery was central to how well his associateship fared. He also remained the principal rainmaker in the practice. While the dentists and hygienist were good people, the profit they produced after being paid their salary packages based on the usual formula was not great. Their profits contributed toward the joint overhead of the practice but Bryan and Denzel each had to pay a substantial sum to the non-profit entity that administered the overall practice to restore its float at the end of each month. This common element was run on a break-even basis.

Denzel’s production

Denzel produced about 80% of the fees of Bryan. Denzel was not as engaged in matters affecting the dental profession as was Bryan and he chose not to work quite the same hours; instead he made personal lifestyle choices.

Denzel was also a little slower in some procedures than Bryan and he hadn’t grasped the central importance of his own surgery’s output. The underlying reality was that not only did Bryan produce 20% more fees than Denzel, he was significantly more profitable because at the margin, there was

much more profit per dollar of fees in the last 20%. Bryan got greater efficiency out of his chairside assistant than did Denzel and she was happier because of the constant flow of work. Bryan banked about \$130,000 per year more than Denzel and even though Bryan was busier clinically, when it came to dealing with practice administrative issues, it was usually Bryan who took the lead as well. However, Denzel got on well with Bryan and their associateship ran smoothly for several years.

Slick enters Denzel's life

Denzel was attending a barbecue at the home of a close friend. Several businesspeople were present, as was James Slick, a 'consultant'. The talk drifted to business and it appeared to Denzel that some of the people present were operating successful businesses. The conversation drifted through comments about business, overseas holidays and the various cars owned by members of the group. It gave Denzel the impression that others in the group were more successful than he. There had been a bit of polite exaggeration and Denzel didn't realise that all he had to do to be as successful as anybody in the group was to increase his own output to Bryan's level - something he was capable of doing. He simply hadn't stretched himself. Somebody mentioned that Slick had helped them sort out a few of their business problems. Slick had participated in the conversation in an understated manner, wondering whether there were other business consulting opportunities among the group. A couple of members of the group were confident, self-made people who he mentally dismissed as being unlikely to entertain his services. The most likely person appeared to be Denzel and he patiently waited for an opportunity to speak to him. As the group revolved around the barbecue, Denzel found himself talking to Slick. Slick politely expressed interest in a couple of comments Denzel had made about his dental practice during the general conversation. In no time, Denzel was talking about the practice, mentioning that he was in practice with Bryan. When Slick asked Denzel what future plans he had for the practice, Denzel mentioned that apart from minor changes, it was business as usual.

Slick captures Denzel's mind

Slick mentioned that he had helped lots of businesses develop successful business plans. This was actually an exaggeration, as his impact on most had been marginal at best, but Slick was good at exaggerating his successes and glossing over his failures – and for taking the credit of others. The only dentist Slick had actually met was the one that drilled his teeth. Slick in fact was a good deal less successful than he appeared, but like Jimmy Brad-dock's manager in *Cinderella Man*, he was good at keeping up appearances.

Sensing that he had Denzel's attention, Slick suggested he could be vastly more successful. In no time, Denzel made an appointment to follow up with Slick. Although Slick gave the impression of being well-connected, he operated from a meeting room in a serviced office arrangement shared by a variety of consultants and one-person businesses. Each of them paid a fee to a common receptionist who answered each of their lines as though she was their personal receptionist and forwarded their messages. Each consultant in turn would return calls with "I'm out of the office but how can I help you?" Slick was actually living by his

wits and at any given time, only had a few clients. His was a precarious existence and he often struggled to pay his bills.

Slick suggested he meet Denzel at a convenient location near his practice. Slick then set out to convince Denzel that he could help him be much better off. It was convenient to suggest that Bryan was a stick in the mud, holding the practice back. In Denzel's mind, the practice had the potential for significant growth by employing more dentists. However, he hadn't really thought about the relative economics of employed dentists as opposed to Denzel producing more fees in his own surgery. Neither had Slick, who only had a vague idea as to what happened inside a dental practice. After meeting Denzel at the barbecue, Slick had done a quick check through a number of dental websites and had acquired a veneer of dental business language. When Denzel indicated that he'd have to run new plans past Bryan, Slick suggested that Bryan would politely hold off backing any plans. Instead he suggested that Denzel should acquire control of the practice so that he could "work *on* the business rather than *in* the business". Furthermore, he should expand quickly with a view to making his practice a hub for satellite practices. To Slick, who knew nothing about the economics of dentistry, it all looked very simple. He could advise Denzel how to expand until he was employing large numbers of dentists and making heaps of money, with Slick himself acquiring a juicy retainer. Slick's ambition was to have maybe ten high-income business clients all reliant on his advice, paying him an impressive annual sum as a retainer.

Slick's advice flawed

Slick was better at quoting adages out of coffee-table management texts than actually implementing business plans. Up to this point, Denzel had been content to float along in Bryan's wake. Life had been fairly comfortable and he hadn't begrudged the fact that Bryan earned more than he. Nor had Bryan ever been unfair. He'd been in the practice longer and he had a larger following of patients. Bryan's patients on average were older than Denzel's and more able to afford better treatment options. However, Bryan had been unable to treat all of his referrals and quite a few had spilled into the hands of Denzel or the employed dentists within the practice. Bryan had been personally used to working faster and slightly longer hours than Denzel over a long period of time. Success had bred success. Slick had little idea of how patient contacts originated and this led him towards giving seriously flawed advice.

Slick didn't understand why Bryan generated significantly higher fees, but he picked up on it and started to subtly work on Denzel's mind. Denzel started to wonder about the future of the practice and his own future in it. Slick, for his part, was trying to learn enough about the business side of dentistry to stay slightly ahead. He even booked an appointment with his own dentist to have a minor matter attended to and used the occasion to ask a few questions of his dentist and the practice receptionist and swallowed the contents of a few articles in dental magazines and dental-related websites. He discovered that Denzel and Bryan didn't use laser technology and didn't promote cosmetic dentistry. Bryan and one employed dentist did a small number of implants, but orthodontics and a number of other specialist procedures were referred out. Denzel had suggested a few items of equipment which Bryan saw little use for.

Denzel's bid for control

Slick emphasised to Denzel that he must “work on the business rather than in it”, implying that perhaps Bryan was holding the practice back. Naturally, Slick had found that a few prominent dentists appeared to have much bigger practices and a bit of detective work found that those dentists lived in expensive homes. Slick suggested that Denzel needed to work to his own business plan and not rely on Bryan: if he did that he could be a lot better off. Denzel started to view Bryan critically, while in the past he had always trusted him – and indeed Bryan had always been worthy of that trust.

At Slick's urging, Denzel asked to meet with Bryan and Bryan's adviser concerning the practice. He suggested to Bryan that the practice could be doing better overall and that Denzel wished to take over the management of it. As Denzel had never shown a significant interest in the administrative and management side of the practice, this came as a surprise to Bryan. Denzel further proposed that he purchase from Bryan his share of the common elements of the practice, consisting of the fee generating employed dentists and hygienist and the equipment that they used, together with increased equity in the premises. Denzel would then manage the practice as well as practising in it and in Denzel's plan, Bryan would only see the patients he was able to in his own surgery.

Bryan's reaction

Bryan and his adviser questioned Denzel as to how he intended to manage the practice. Denzel's reply was unconvincing, consisting of an iteration of a string of management clichés.

Bryan and his adviser politely ended the meeting and in subsequent discussions, decided that Denzel's outline plan left Bryan's surgery in a vulnerable position, since he would no longer have any managerial influence over the practice receptionist or support staffing. Whatever had got into Denzel's head was unknown to them, but they found it disturbing. Bryan decided that selling the common parts of the practice and allowing Denzel complete control of the front desk and conduit to Bryan's surgery was a step he was not prepared to take. In time, it would make the residue of Bryan's practice unsaleable. It would also take from Bryan any economic benefit in attracting referrals into the practice and

since he was already busy, they would all flow to Denzel and the employed dentists. Bryan and his adviser thought about the issues and rejected Denzel's offer.

Denzel's antagonism grows

Slick had invested a lot of time and energy with Denzel, who had come to feel aggrieved at Bryan. From now on, he was progressively more likely to become frustrated when small things went wrong in the practice. His relationship with Bryan, which had previously been healthy, became distant and Denzel began to sponge up more of Slick's ideas. Slick had a few dissimilar businesses in his portfolio of clients, but each had significant limitations, albeit that he was able to work out enough small improvements in each to maintain his relationship and retainer over time. However, he badly needed to grow a business and having noticed that several dental corporates had apparently achieved significant success, he dreamed of Denzel taking control of Bryan's practice, employing several more dentists on his way to creating satellite practices, ultimately buying other practices via borrowing for acquisitions and eventually proceeding towards an IPO and listed public company status. Slick still knew too little about dentistry to understand the significant constraints. Since meeting Denzel, Slick had approached several other dentists and been dissatisfied by their disinterest. The dentists, for their part, sensed that Slick's motivation was personal greed rather than interest in them or their practices. In reality, Slick was too late into the market, had too little knowledge and negligible personal capital.

Denzel was the only dentist who took Slick seriously and Slick urged him to work on Bryan to get him to see reason.

Denzel was still unable to properly articulate his plans to Bryan, but the more he persevered on his quest, the more Bryan felt the necessity to maintain the status quo in order to protect his own interests. Bryan was longer-established and financially stronger than Denzel. Denzel had become irritating, but Bryan figured that he could outlast Denzel's demands. Bryan continued to work his traditional pattern of clinical hours, slightly tightened up his fees and ensured that the right patients among his extensive list found their way into his surgery. In fact, Denzel's entreaties had motivated Bryan to concentrate *more* on his book and as such, his fee output strengthened.

Denzel still doesn't get it

Denzel and Slick still didn't get it: Denzel was still working less clinical hours and producing less output than Bryan and had practiced in the area for a much shorter period. As a result, he had fewer personal referrals. There was a disconnect somewhere in Denzel's mind. Despite Slick's grand plan, he was far from breaking any records in his own surgery. He became jealous of Bryan and Slick advised him that the only way to resolve the issue was to separate his practice from Bryan. Slick still didn't understand fully the intricacies of a dental associateship, but he had determined that Denzel was not going to be able to push Bryan into selling him control of the practice.

Toward separation

Denzel now advised Bryan that he wished to separate. Bryan's advisers told him to sit and wait, as Denzel had brought a series of inconclusive proposals and there was doubt regarding his intentions and, more importantly, his ability to follow through. Bryan made it clear that he wasn't moving and suggested to Denzel that if he wanted to be more successful personally, he needed to find his own premises. Bryan might be prepared to buy him out of his equity in the premises and since Denzel had once tried to buy Bryan's share of the common fee element of the practice, Bryan now reversed the situation and offered to buy out Denzel's interest in the common element.

Denzel begins his search

Denzel went searching for premises, but found that suitable premises were scarce and they were more expensive to buy or rent than he had figured on.

When Denzel advised Bryan that he had finally secured premises, he proposed that the employed dentists be free to be employed by either Bryan or Denzel. He also had his lawyers serve legal demands on Bryan. The lawyers had an incorrect understanding of how a dental associateship functioned and where the goodwill actually resided. Their demands caused Bryan significant expense in legal and accounting fees, inflaming the situation.

Bryan's response was:

“None of the employed dentists nor the

hygienist own personal goodwill. They have no property rights in respect to the practice name, website, telephone number or equipment, no control over the practice receptionist and no right to remove practice records without agreement. If you wish to fight over this, the dispute will be a very drawn out one."

Slick's star fades

By this time, Denzel had begun to lose faith in Slick. The practicality of separating a practice and negotiating agreement with Bryan were looking harder and more expensive.

Slick, for his part, had seen the signs. He was now concentrating his dubious skills on a pair of chiropractors, an optometrist, a small IT consulting business, a podiatrist and the owners of a gun shop. He kept hopeful contact with Denzel but the amount of advice Denzel was taking had reduced significantly. Some proposals to meet had been deferred by Denzel being too busy. However, Slick's relationship with Denzel had been preserved - to a point. By this time the dispute had cost both Bryan and Denzel a significant amount of cash. Denzel's expenses were a lot higher than Bryan's, since he had been paying Slick heavy advice fees for two years and had a lot more accounting fees in getting information into a form that Slick demanded. His lawyers added considerably to his expenses.

Denzel faces more expense

It was about to get a lot more expensive for Denzel. His search for premises had led him to an auction for a recently vacated building within about half a kilometre of the existing practice. The building had more problems than were apparent upon a quick inspection and Denzel significantly underestimated the cost of the renovation. As the building was being auctioned, there was no cooling off period. To Denzel, it was the best of a poor lot of options and he determined to buy it at the auction. Unfortunately for Denzel, there were a couple of other bidders wanting to redevelop the site and he found that he had to bid about \$350,000 more for the building than he'd anticipated. Having bought the building and acquired a debt of around \$1.2 million, Denzel then set out to get quotes on renovation and equipment. He planned to fit out three surgeries initially, with a fourth one plumbed and wired without a chair. The fit-

out consultants, on inspection, had reported that he needed to do some structural modification, and when he approached a builder with plans, he found that it was necessary to install ramps for wheelchair access and that all of the internal doorways had to be widened. There was an extensive list of other requirements to which he had to agree in order to get the necessary permit from his municipality. At this point, Denzel had come too far to go back and he decided to press on. As the whole project was going to take about a year, he needed a location from which to practice in the interim if he separated from Bryan. Looking around the area, he found that there was an allied health group of psychologists, podiatrists and speech therapists who had a couple of rooms spare and he arranged to rent there while the new building was being fitted out. The temporary fit-out of two surgeries in these temporary premises, however, also proved to be more costly than he had anticipated; meanwhile, additional problems were emerging with the purchased premises and he was finding that each problem uncovered was accompanied by an additional expense to fix and also created a further delay.

In his negotiations with Bryan, Denzel demanded that Bryan allow him to take two of the employed dentists, that Bryan buy his share of the premises and that the telephone number be shared. Bryan's response, via his lawyers, was:

"I'm prepared to buy out your half of the premises but only if you agree to depart the building and only take one employed dentist with you. Since you're moving, it's your problem to market your own practice. I'm therefore not prepared to share a telephone number with you, nor give up the practice name nor practice website. Any agreement is subject to your share of practice overheads being maintained up until the date of departure and if not maintained, they'll be offset against any goodwill adjustment or price paid for your half of the premises. You are able to remove one surgery of equipment and a few other specified items."

Irreversible

The steps Denzel had already taken had made his decision to separate from Bryan irreversible and in negotiation, he found Bryan's attitude and that of Bryan's advisers hardening. He had already cost Bryan a great deal of stress in addition to legal fees, extra accounting fees and valu-

ation advice fees. Bryan had once regarded Denzel as a friend, but now loathed the sight of him. Bryan's reply to some of Denzel's demands via his solicitors had become terse and uncompromising.

Finally, Denzel accepted the best deal he could negotiate with Bryan. He, one part-time dentist and three support staff departed for Denzel's temporary premises. The renovation and fit-out of Denzel's intended future premises had already been delayed beyond his anticipated forecast. Denzel was now paying rent and a share of overheads in his temporary location and the debt and interest cost on his purchased premises was mounting with each complication and delay arising in the renovation and fit-out.

Peace of mind

Bryan had bought peace of mind and as he had always been the main practice drawcard, his existing practice base continued to refer their family, friends and relatives following the split. Bryan now had spare space but effectively already had enough patients for a two and a half surgery practice. Bryan figured that with patience, he'd quickly get back to about a three-surgery practice and there he'd be comfortable. He redecorated the front of the practice, improved his recall systems and stationery and sent tasteful brochures about his practice to all patients on his and his employed dentists' treatment lists.

Denzel's challenge

Following the split, Denzel found that the challenge was only just beginning. The new temporary surgery fit-outs had run well over budget, while the total cost in the premises he had purchased plus renovation plus fit-out plus incidental expenses had soared to about \$2.5 million. Denzel now found that his bankers wanted every ounce of flesh. He had mortgaged his house and the premises and had secured his practice. He and his wife had given personal guarantees to the bank, as well as guarantees as directors of their family company. The bank, for its part, had imposed onerous repayment schedules. This left Denzel cash poor.

Denzel's plans, prepared by Slick, had included a significant marketing exercise mainly aimed at existing patients and through his existing patient list to others in the community. The severity of his cash

flow meant that this had to be curtailed. He was now realising that he had taken a perilous path. He also had lots of legal, accounting, consulting and town planning fees associated with his move.

For his part, Bryan borrowed to pay for Denzel's half of the premises and paid the differential in respect of the greater part of the common element that he had retained, but Bryan was older, more established financially and was still able to produce significantly more income in his own surgery. Bryan was coping comfortably.

Denzel sacks Slick

Denzel now realised that Slick's management advice had been superficial at best. Slick had glossed over dental fit-out as of little consequence – Slick's personal experience consisted of coping with a personal computer, a mobile telephone and little else. As Denzel looked at the expensive plans for the fit-out with what seemed to be a vast amount of cabling and plumbing plus associated dental cabinetry, lead shielding for the OPG, widening doorways for wheelchair access and copious other changes required by the town planners, plus the interior decorating consultants for the reception area, quotes on new furniture and dental equipment, he realised that while Slick had filled his head with management clichés and poisoned his mind about Bryan, he had not come remotely close to warning him of the expensive and dangerous path he was advocating. Denzel and his wife were now doing it tough, but they recognised that Slick's advice had been the underlying cause of the unfortunate path they had trodden. They advised Slick that his advice would no longer be required.

A new start

Over the next five years, Bryan rebuilt the practice, which had retained its name and identity as a long-established local dental group, then began to cultivate the employed dentist who showed the greatest aptitude for running a practice. In due course, Bryan sold this dentist the practice about seven years after Denzel's departure, after agreeing to work for him for three days per week initially, reducing to two and a half days and then two days over time. That suited the new owner, who was able to retain the benefits of Bryan's personal following and gradually wean it to himself and his employed dentist. The new owner was very successful.

Denzel trapped

Denzel found himself trapped by the amount of debt he was carrying. He now found himself working harder than he'd ever worked before and producing more fees in his own practice. However, his inability to substantially market the practice meant that to a significant degree, the extra fees he produced were at the expense of his only employed dentist, who continued to be pinned to part-time production. He hadn't realised the significant influence Bryan's patients had had on referrals and had erroneously assumed that new patients would divide equally between Bryan's practice and his own post-separation; in reality, he found that he received only a small proportion of new patients and competition in the surrounding area had increased with new practices opening. The business of dentistry was a lot tougher. Denzel's level of debt had fallen a little and by arrangement with the bank, he had managed to pay out the non-deductible home loan portion of his debt as a priority over the tax-deductible portion. Nonetheless, he still found himself with a huge core debt, though a fair amount of the equipment and parts of the fit-out had been paid off on a chattel mortgage over five years. During that five years, Denzel and his wife had not been able to afford a significant holiday, settling for a week or two at a time in rented cottages near local beaches. They hadn't traded in their cars for a number of years, their home was badly in need of maintenance and personal expenditure had been pared to the bone. Although Denzel's wife, Flora, had previously taken time off work to look after their younger children, the financial situation had now become so tough that she had displaced the receptionist in Denzel's practice as well as taking on most of

the burden of practice administration. This cost-cutting had enabled them to satisfy the banks and meet family expenses. However, their life had become much tougher than before Slick had persuaded Denzel to break out on his own.

When they heard that Bryan had sold his practice to one of his assistant dentists, they realised that had they only been patient, Denzel could have worked with Bryan for the past seven years and then purchased the practice from him. That would have been vastly less expensive, would have led to none of their current problems and they would have been much better off financially. It was a lesson learned slowly at great cost.

Slick's future

Slick continued to work as a one-man band but somehow the ability to become an essential part of a client making a killing in the market eluded him. He'd managed to get just enough work to put food on the table, but his dream of being central to a high-powered advice business network with a lot of wealthy clients on retainer had failed. A friend in the motor trade had offered him a job as a car salesman and while it was something that Slick had never envisaged himself doing, he found that selling cars was his true forte.

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