

STEPPED PURCHASE OF A DENTAL PRACTICE

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A stepped purchase of a dental practice is becoming more prevalent in recent years, particularly for specialty practices. A stepped purchase occurs where the purchaser dentist (Purchaser) buys a dental practice from the selling dentist (Vendor) in two or more steps over an extended period of time. This transaction is used where the Purchaser is not prepared to purchase the entire dental practice immediately, but wants to enter into a long term plan and a legally binding agreement with a Vendor that clearly set out the stepped purchase that will occur over time.

A stepped purchase which extends over a period of several years is not the typical arrangement when purchasing a dental practice. The more usual route is the Purchaser buys 100 per cent of the Vendor's practice, purchasing shares of the Vendor's dentistry professional corporation or by a purchase of assets. Where the Purchaser wants the Vendor to remain at the practice and continue practicing dentistry after the purchase, the Vendor does so as an associate of the Purchaser. An associate agreement is entered into with the Purchaser as principal and the Vendor as the associate typically receiving 45 per cent of collected billings. While the norm is 40 per cent for associate remuneration, since the Vendor provides mentoring and assistance in the transition of the practice to the Purchaser, 45 per cent is typically the remuneration level.

In a stepped purchase, the Purchaser is often already an associate of the Vendor and has worked with the Vendor at the dental practice for a number of years. The parties have worked well with each other and share the same practice philosophy and values. The Purchaser wants to buy the practice but, for various reasons, wants the Vendor to retain an ownership interest in the practice and continue to practice dentistry as a co-owner.

The associate wants to buy the practice and agrees to do so over time. Why? Having the Vendor remain as a co-owner of the practice is excellent support for the Purchaser. The Vendor may have far more experience in dentistry and has run the practice successfully for many years. That wealth of experience can be invaluable to the associate. Having an in-house mentor on an ongoing basis is a wonderful resource to the associate.

The arrangement often works as follows. The parties enter into a purchase and sale agreement whereby the Purchaser buys a portion of the Vendor's shares of his or her dentistry professional corporation. Or in the case of an asset sale, the Purchaser buys an undivided interest in the Vendor's dental practice assets. From the Purchaser's perspective the initial percentage purchased is typically not less than 50 per cent, so that the Purchaser has equal control of the practice.

The Purchaser and Vendor become common shareholders in the case of a share purchase or partners where assets are purchased for a period of time until the stepped purchase is fully completed. A detailed shareholders agreement or partnership

agreement is the primary document governing their ongoing relationship during the stepped purchase. The shareholders agreement or partnership agreement will provide that the Purchaser agrees to purchase the remaining portion of the dental practice from the Vendor at a future specified date or dates for a specific price. The price may be a fixed price or based on a formula that is sufficiently clear that the parties will easily be able to determine what the price will be for the next step or steps of the purchase.

If the Vendor dies or becomes disabled, the agreement should provide that the future stepped purchase dates for the Purchaser's purchase of the Vendor's remaining interest in the practice will be accelerated upon such triggering events. To ensure the Purchaser can fund the buy-out in such events, the Purchaser typically obtains life insurance and disability insurance policies on the Vendor, with the Purchaser as beneficiary.

Similarly, from a Vendor's perspective, the Vendor may obtain life insurance and disability insurance on the Purchaser. If the Purchaser dies or becomes permanently disabled before completing the final purchase step, the Vendor might have the right to re-purchase the Purchaser's interest in the practice at a specified price.

Insurance issues in stepped purchases can be complicated and require careful tax planning. The parties need to retain insurance advisors who have expertise in advising dentists and who understand these issues to provide appropriate advice to the parties. Insurance policies should be arranged early in the process to ensure that the parties qualify for such insurance and that appropriate buy-out funding is in place.

A stepped purchase can be an excellent arrangement for both Purchaser and Vendor in certain circumstances. However, stepped purchases are complex and require careful planning and extensive legal agreements. The best advice is to retain professional advisors, including an insurance advisor, accountant and lawyer, who are all very familiar with these structures and who focus on advising dentists in purchasing dental practices.

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