Old-school physician-retirement plans often flunk today’s practice viability tests

The biggest issue that group practice administrators have to deal with related to physician transition and retirement is partner buyout. Bruce Johnson, JD, MPA MGMA Health Care Consulting Group consultant, says the cost of buying out a retiring physician used to include the stock purchase of his/her shares based on the depreciated book value of the practice’s hard assets paid over a five-year period with interest. Buyouts also included payments of “deferred compensation” equal to a portion—say 80 percent—of the retiring physician’s average W-2 compensation over the previous three years, with value considered an exchange for a share of his/her accounts receivable plus a premium for goodwill.

Today, many groups have a difficult time living up to such terms and staying financially healthy, Johnson says. Even though the buyout may have seemed reasonable when drafted years earlier, many of those formulas can cause substantial financial hardship to the practice and the physicians who remain. The cash flow and other implications of these buyout arrangements may force the practice to either revisit the buyout or risk destruction of the group.

A medical practice can avoid the trap of unrealistic physician buyout terms by carefully reviewing its basic legal documents, including the shareholders’ buy/sell agreements, employment and partnership agreements, facility corporation documents and more. Physician compensation formulas also may need review.

Johnson advises you to:

- Discuss physician retirement and practice slowdown options in strategic-planning sessions;
- Make it clear that the interests of the group supersede those of individuals;
- Create practice buyout options based on realistic values;
- Make sure buyout terms focus on real money (the physician’s accounts receivable);
- Include provisions for the group lengthening the buyout terms when two or more physicians retire simultaneously;
- Establish clear rules for physicians who want to slow down before retiring, which might include offering fewer perks, reducing compensation for less participation in on-call coverage and termination as a shareholder/partner;

- Not to expect substantial reductions in operating costs; and

- Revisit the buyout terms and the group’s financial health related to the terms every two years.

Physician employment agreements should include statements about how much notification a physician must provide the practice before retiring. Those agreements should be reviewed for that and other issues such as deferred compensation, retirement benefits and malpractice tail coverage.

Once you complete that process, note the lessons learned during the transition and apply them to the next physician’s retirement. Also, review all your physicians’ contracts and remind yourself of the terms and issues you may need to prepare for now.