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A Practical Guide to Understanding and Negotiating Your First Employment Agreement

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INTRODUCTION

This course is designed to enlighten the young doctor as to the process of negotiating and signing his or her first employment contract, the do's and don'ts, so to speak, of negotiating the contract and some of the major issues typically associated therewith.

THE PROCESS

The process formally starts with an interview and is often followed by one or more interviews and/or visits to the practice. It is okay to begin basic contract discussions at this point, but you should be careful not to get boxed in, as discussed below. Ultimately, the practice will offer an employment contract to you. Under no circumstances should you feel compelled to sign the contract as initially presented. It is customarily understood that this represents a "first draft," of sorts, and that you will engage an attorney to review the agreement and discuss it with you. It is also commonly understood that you may have issues with the contract and that negotiations are likely to take place. Therefore, at the time you receive the contract, it is advisable to engage an attorney to review and discuss the contract with you. At that time, you and your attorney should create a list of all issues, comments and questions so that they can be presented at one time. The attorney can negotiate changes with the practice on your behalf. However, it is preferable that the doctor negotiate directly with the practice, having the attorney coaching on the sideline. This reduces costs and, perhaps more importantly, demonstrates your willingness to deal directly with your employer on issues. Negotiations typically result in changes being made to the contract. If the parties carefully dispense with all issues, comments and questions, then the next version of the contract should be ready for signature.

IMPORTANT ISSUES

I. Term. The employment agreement, like most personal service contracts, has a term of one year and is renewable automatically from year to year thereafter. However, the contract *should* be terminable by either party *at any time* on some notice to the other, typically 60 or 90 days. You should definitely want the right to exit the arrangement at any time. However, the quid-pro-quo is that the practice will almost always have the same right. Even if having an out clause means permitting the practice to have the same, it's still worth it. Don't yield to any sense of insecurity. Most practices will simply not terminate without extreme cause for at least a year. Hiring outside of the "cycle" is not always an easy thing to do. In addition, the practice will have expended time and energy into bringing you on and will almost always give you the

benefit of the doubt. Often, however, many practices actually wait too long to terminate a relationship that isn't working.

What's the right amount of notice? Well, between 60 and 90 days. Obviously, the longer period works better if you're the party being terminated while the shorter period works better when you're the terminating party. The truth is, in most 90 day contracts, the parties agree to an earlier split. Lame-duck relationships tend to go south quickly. Therefore, shoot for 90 days and hope that if you're the terminating party, the practice will allow you out earlier.

II. Compensation. Most contracts provide for base salary and incentive bonus provisions. Make sure you're happy with the base salary. It's almost always better to have guaranteed money versus non-guaranteed money where the conditions for non-guaranteed money are largely outside of your control. For example, the typical bonus clause allows the doctor to retain for each employment year some percentage of collections from his/her direct patient services that are in excess of some stated threshold – usually determined to be roughly 2.5 to 3 times the base salary number (*i.e.,* 25% of collections from direct patient services which exceed $450,000 (e.g., base salary of $150,000 times 3) for the year. Working hard and efficiently is usually within the doctor's control. Patient volume is not. Unless the doctor is coming into the practice as a replacement for a departing doctor, then there generally isn't enough work to keep the doctor busy full-time for a year or two. Furthermore, in the first employment year, the lag time on billing to collection usually results in a 2 or so month period before the doctor will even begin to see collections. So, he/she is behind the eight ball right off the bat.

Also, make sure the contract is specific as to what happens to the bonus calculation when the contract is terminated prior to the end of a given bonus year. In particular, the contract should state that the threshold would be prorated through the termination date and subsequent collections considered in the calculation. For example, for a termination at the mid-way point of an employment year, the threshold would be cut in half, and all collections received after the termination date for at least 3 months would count toward the bonus. In the absence of specific contractual language, there is little chance you'd see money post-termination.

However the bonus is structured, be sure that it is attainable (so as to actually provide incentive) and simple in its terms. The bonus clause is probably the most disputed term contained in the contract and is often poorly constructed and seldom well thought-out in terms of its applicability.

III. Malpractice Insurance. The practice usually pays for the doctor's malpractice insurance. However, too often the contract says nothing more, ignoring the important issue of which party has the financial responsibility for "tail coverage" under a "claims-made" policy. Malpractice policies are generally either "occurrence-based" or "claims-made" based. Under an occurrence-based policy, the doctor is covered against a legal claim for liability as long as the insurance was in place while an act of malpractice occurred. Thus, if the doctor's employment terminates, his or her "occurrence-based" malpractice policy can be canceled, and he or she will be covered for any claims that are brought post-termination. Conversely, under a "claims-made" policy, insurance must be in place when the claim is brought. Consequently, at the time of employment termination, the doctor must acquire "tail" insurance to cover post-termination claims.

The cost of "tail" insurance is roughly equivalent to 1 to 1.5 times the cost of the annual premium for the malpractice policy.

This issue is more concerning to the doctor because, in the absence of specific language in the contract requiring the practice to pay for tail coverage, financial responsibility lies with the doctor. Therefore, it is important that the employment contract specify that in addition to the employer's paying for the cost of the doctor's malpractice coverage, it will also pay the cost of any "tail" if the coverage at the time of termination is under a "claims-made" policy.

Be advised, though, that the responsibility for paying for the "tail" is often a point of contention as the hiring practice will often not want to be responsible for all or a portion of the cost of the "tail" coverage, especially in the circumstance where the employed physician voluntarily leaves the practice. In the end, the financial responsibility for the "tail" coverage will end up being a product of the parties' negotiation and will often end with some form of compromise as to payment responsibility.

It is also worth noting that even if the practice currently maintains occurrence malpractice coverage, insurers and insurance policies can, and often do, change during the course of employment. It is therefore advisable to make sure the contract addresses the issue of tail coverage in the event the basic malpractice insurance policy should change.

IV. Non-Compete Clauses. The non-compete clause is that part of a restrictive covenant that restricts a doctor from "competing" with the practice following the termination of his or her employment with the practice. Regardless of what you might hear, except in a couple of states, non-competes are definitely legally enforceable -- although a few states provide stipulations for enforcement. Regardless, the non-compete cannot be taken lightly.

Often, a young, single doctor without family will say: "I'm not worried about the non-compete. If this job doesn't work out, I definitely do not intend to stay in Smithville". However, one should keep in mind that circumstances can change. It could be as a result of meeting someone special or just falling in love with the community that one's intentions can change. The point is that you just never know and, as such, it is prudent to first understand the scope of the non-compete provision and, if necessary, try and negotiate its terms so that it is something you can be comfortable with.

Non-competes generally must be reasonable in their geographic scope to be enforceable. Sometimes they are not. Here again, many doctors figure that where a non-compete seems ridiculously broad, they don't need to be overly concerned with enforcement down the road. This is not an advisable position to take. In most states, a court can reduce the scope of the non-compete to something it deems reasonable and, hence, the doctor could still wind up having to relocate.

That said, the non-compete is generally the toughest clause to negotiate. These days, practices are pretty serious, and most often adamant, about their inclusion in the contract. Still, they can be modified in ways that may make them more acceptable.

For example, the doctor's worst fear is that he or she will be fired from employment and then, as a result of the non-compete clause, be required to relocate.

The contract could provide that the non-compete will not apply if the doctor is terminated by the practice not for cause. From the practice's standpoint, this kind of clause is not favorable because often it is more difficult than it might seem to pinpoint the precise reason for the breakup of a relationship. However, from a young doctor's perspective, this language is very beneficial.

Also, the contract might provide that the non-compete won't apply for any termination that occurs within the first year of employment. This makes sense because the young doctor typically is not in a position of damaging the practice through competition if he or she is still new to the area, relatively inexperienced and isn't much of a threat to influence existing referring sources. This provision is particularly helpful to the doctor who is moving, or returning, to a desirable area where he or she wishes to remain regardless of how things turn out with the practice. It gives the doctor some time, anyway, to make a determination whether joining the practice was, in retrospect, a mistake or to proceed forward subject to a non-compete.

A common misperception is that the non-compete prevents the doctor from establishing an office or joining a practice that has offices within the restricted area (*i.e.,* 7 miles, perhaps, from the employer's office). However, most non-compete provisions are more restrictive than this. They work to prohibit the doctor from practicing ophthalmology of any kind and in any manner within the restricted area, in effect prohibiting the doctor's practice at hospitals and surgery facilities. A contract could, however, be less restrictive and allow the doctor to retain his or her privileges with hospitals and surgery facilities so long as he or she opens an office or joins a practice that has offices outside of the restricted area. This type of "limiting" the scope of the covenant is worth pursuing in your contract negotiations.

V. Partnership. These days it seems that practices are reluctant to address the issue of partnership in the employment contract. However, presumably you're in this for the long-term. So, you should get answers to the following questions, even if language isn't incorporated into the contract:

- How long until partnership is offered? In most situations, an employed doctor is required to work 2 or 3 years until partnership is offered. Often, partnership commences on the first day of the practice's fiscal year. Thus, for example, for employment starting August 1, 2013, partnership might commence January 1, 2016, or after 29 months of employment.

- Will the offer be for an equal, or full, partnership interest? Typically, deals are structured in a way that gives to the partner an immediate full and equal partnership interest. This can be a source of contention if it is a solo practitioner bringing on a partner.

- How will the buy-in price be determined? It is unrealistic to expect the practice to tell you how much a buy-in would be at the commencement of employment. After all, the practice's value will change before then. But you should know the method which the practice will use to determine its value, and therefore the purchase

price. Your attorney should know if this is likely to yield a fair buy-in price.

- How are the buy-in payments to be structured? Only some portion of the buy-in will relate to your purchase of an interest in the practice's tangible assets (*i.e.,* furniture, fixtures and equipment). The bulk of it may relate to the practice's accounts receivable and goodwill values. Thus, the larger part of the buy-in is typically structured in compensation reductions so that the doctor's partnership compensation more or less phases up in time to a full compensation share. This is beneficial to the doctor from an income tax standpoint.

Even if these issues are not committed to in writing in the contract, getting answers will give you a good idea about what you can expect in a few years and will create, at least, a moral obligation of the practice to follow through.

THE TEN COMMANDMENTS OF NEGOTIATING

I. Thou Shalt Learn. Through the negotiation process, you can learn more about the personalities of the doctor(s) you are seeking to join than you will from the collective phone conversations, interviews, and dinner discussions leading to the point of contractual negotiations. Most of your potential employers will be small ophthalmology practices ranging from the solo practitioner to three-four-or five-doctor groups. The meshing of personalities is important if the employment relationship is to survive and prosper into partnership. One of the most, if not the most, common reason for the failure of employment relationships is a clashing of personalities. Too many relationships, frankly, do not stand a chance from the very start. However, it is difficult to assess one's personality over dinner or during an interview when everybody is wearing their best face. Pay attention to how a doctor responds to your request for a higher salary or for the practice's financial information or the elimination of a non-compete clause or any number of requests or comments you may make in the contractual negotiation process. Is the response a guarded one? A forceful one? Ask, listen, and learn!

II. Thou Shalt Be Respectful. See Commandment I, above. The practice will also have its opportunity to see the real you and will be looking to assess your actions away from the dinner table. Will you *demand* a certain salary or *require* one? Don't confuse respect with being timid or non-forceful. There's nothing wrong with letting a prospective employer know up front that you will not accept any contract that includes a non-compete clause or that contains a salary below your required level. Doing so can save time for both parties. However, the way you do so is important. After all, the practice is also interested in hiring a personality that will mesh with the personalities of its doctors.

It is important to be aware of boundaries. A practice may be more likely to turn down a candidate who tries to tell the practice how things *should* be done to make *its* practice more efficient, or make more money, etc. The young doctor might, well, be more business or practice savvy than the practice doctors, but there is a time –

specifically, a year or two down the road after the doctor has made a nice showing as part of the practice and has gained the confidence and respect of the practice doctors.

III. Thou Shalt Ask. You can't get what you don't ask for. Paying homage to Commandment II, if you are firm, but respectful and courteous, then you aren't likely to lose a job opportunity by requesting, for example, a signing bonus. While the request might be denied, the opportunity is not likely to become a casualty due to the request.

There is also the theory that the more you ask for, the more you are likely to receive. In practice, this is often true. Thus, your request for a signing bonus, though denied, may result indirectly in your "winning" another benefit that may otherwise have been lost.

Additionally, do not hesitate to ask tough questions:

Ask about practice finances or request to see practice financial statements. It's not wrong to want to see how a practice performs and what kind of money you might expect to make down the road (*i.e.,* as a partner). Generally, about eight out of ten young doctors join a practice with every intention of having a long-term relationship. In many cases, joining a practice means relocating yourself and possibly a family too. So, it's only prudent to know what you're getting into and what your future prospects are. Some, especially solo doctors, are very guarded about their financial information. Sometimes, they never open up. Not even after employment starts. It is not uncommon for one to feel shy about asking for such information. But not only is it a prudent question, it's a good test for how the practice will respond to a tough question. Most times, the practice will respond with flying colors. This question might just be the best question you will ask the practice because it demonstrates your interest in a long-term relationship. The doctors will more than likely happily forward the information to you.

Ask about partnership. How long until partnership if all goes well? What is anticipated in terms of a buy-in? To illustrate, a general ophthalmologist accepted employment, worked two years and was ready for partnership. Things were going really well until he and his employer discovered that they had two completely different notions about what a buy-in would be. When they couldn't agree to a compromise position, he left for another area of the country. Things worked out well for him, but he probably wishes that he had those two years back. The moral here is: Don't wait to find out that the relationship won't work long-term! Be proactive.

Ask about the circumstances of your hiring. What kind of situation would you walk into? What will be expected of you? A typical situation finds a two-doctor practice, for example, with the equivalent patient volume of 2.5 doctors. In other words, the practice is "larger" than a 2-doctor practice but not yet the size of a 3-doctor practice. Yet, you'll be the third doctor. This can impact your hiring on a few different levels: First, you might not be as busy as you might like for the first year or so. This might have an adverse impact on your overall compensation, as many incentive bonus clauses tie directly to the level of collections from one's direct patient services. Thus, if you're not busy, bonus compensation will be difficult to achieve. Second, you might be expected to be more of a "rainmaker" than you might feel comfortable being. If shaking hands and having dinners with potential referring sources is not in your personality, then you might not have a full patient schedule until the patient volume more naturally, or as a result of

other circumstances, builds. In the meantime, this can cause tension and result in termination or, at the least, in the deferral of your partnership. On the other hand, if the circumstances of your hiring are that you would be replacing a departing doctor, then patient volume and productivity may not be an issue.

So, for sure, ask away and learn. But be respectful and courteous in doing so and, please, pay special credence to Commandment IX, below.

IV. Thou Shalt Be Honest. Just as Commandment II states, during the negotiation process the practice has a chance to see the real you. It is the first step in developing a long-term business relationship hopefully leading to partnership, therefore it is important for you to be honest throughout the process and maintain your credibility. While you do not need to divulge all of your priorities upfront, hiding information that is crucial to specific aspects of the contract will most likely come back to haunt you. Furthermore, it is not the time for manipulation and dirty negotiating tactics. How you behave and handle negotiations sets the tone for your future relationship with the practice.

V. Thou Shalt Know the Extent of One's Leverage. Negotiating leverage isn't merely important in negotiations. It's almost everything – particularly with respect to the more important issues of compensation, non-compete clauses, and the like. You need to assess, as best you can, what leverage you have. Is the position a highly desirable and competitive one with numerous candidates? What are your credentials and how do you suspect you measure up with the other candidates?

Usually, the more desirable the position, the lesser the negotiating leverage. The flip side is that there are many opportunities – particularly in the more rural areas of the country – where the young doctor, and not the practice, possesses most of the negotiating leverage.

Still, it's difficult to determine the precise extent of your leverage. Do what you can to assess it. For example, look for comments that the practice doctors or their administrator may make with respect to the number of, or the qualifications of, other candidates, or the level of need that the practice presently has for a new physician. Is your position generally one of planned growth or is the practice in desperate need of a replacement physician?

That said, while one can get a pretty good idea about the degree of their negotiating leverage, he or she usually won't know for sure. So, it's best to use any leverage you might have with – you guessed it – respect and courtesy.

VI. Thou Shalt Not Commit (To Terms) Early. Generally, a young doctor contacts an attorney at the time he or she receives a contract offer. Usually, by that time, certain things have been discussed, chief among them, compensation. Usually, there's still some room to reopen the issue at this stage – but you'd rather not be caught in a position of renegotiating what's been "agreed to." Still, unless you absolutely have to (which isn't often), it is usually not a good idea to commit to any term until an offer has been made in its entirety (*i.e.,* the contract has been tendered).

One reason is that what may seemingly be satisfactory may not be acceptable when all terms are considered. Perhaps, for example, you might desire a higher rate of

compensation if the practice doesn't pick up the cost of your malpractice expense or, say, fringe benefits aren't what you thought they might be.

Another reason is that a subsequently-engaged advisor might lend more insight as to what level of compensation is the "going rate" or more appropriate for that locale.

VII. Thou Shalt Choose One's Attorney Wisely. Choose the right lawyer. Location isn't important. Specialty is. Most wise people wouldn't see a cardiologist if they had an eye condition. Similarly, you shouldn't necessarily hire a general practitioner local to the practice you're seeking to join to have your contract reviewed. You should seek health care counsel who has experience in the drafting and reviewing of medical practice employment contracts. Such an attorney is more likely to understand the industry-related issues and will have a better feel for the opportunity and the personalities involved. Besides, state-specific issues aren't typically invoked in the employment contract.

For example, non-compete clauses are common in many contracts, but each state has different laws regarding these clauses, particularly those in physician employment agreements. Some states may allow non-compete clauses generally, but specifically prohibit their inclusion in physician employment contracts. This is a case where a specialized, out-of-state attorney possessing knowledge on a particular industry specific issue may be more beneficial than a non-specialized, local attorney. Experience does matter.

VIII. Thou Shalt Use One's Attorney Wisely. You should use your attorney wisely. Remember the importance of perception. If you are uncomfortable sticking to your guns on one or more issues, then let the practice know that your lawyer is advising you as such. Your attorney would presumably rather the employer be agitated with him than with you.

But be careful not to rely too heavily on the lawyer to do your negotiating for you, though. Employers sometimes have a tendency to take an issue less seriously unless they know that it's ultimately coming from you. Again, your attorney will probably be happy to negotiate for you; however, if there is a stalemate on an important issue, then at some point you must speak for yourself. The employer is more likely to respect your position as hard-lined if, at some point, you are willing to stand up and declare, respectfully, of course: "*this isn't about my lawyer trying to win a point for me; I simply cannot accept the offer as is.*"

IX. Thou Shalt Not Attempt a "Third Bite at the Apple" (Without proceeding very carefully). There's little more annoying than one who keeps asking and asking and asking. Ultimately, this will work against you. Remember, the practice is learning about you during the negotiation process. And it is highly annoying to field the same requests time and time again. So, while asking is encouraged (Commandment III), it is important to ask no more than twice. Chances are, you're not going to receive something that's been denied twice, and it's disrespectful, and dangerous, to keep asking.

X. Thou Shalt Remember: There is a Time for Everything. Recall Commandment V about the concept of leverage. Leverage occurs at a couple of stages. You may not have leverage at the negotiation stage. However, if through your

employment you become a valuable, contributing member of the practice and build congenial relationships with the other members, then you will have created leverage to effectuate a modification to your contract. You're not necessarily stuck forever with your contract. Contracts are made to be amended. So, rather than risk losing a job opportunity over an issue that the practice will not give in on, move on and wait until you've acquired the requisite leverage to reopen discussions (assuming, of course, you're willing to accept employment in the first place).