

MFW RedPaper Series

7 Common Mistakes When Forming A Hospital-Based Medical Group

In this short **RedPaper**, I'm going to reveal seven of the most common mistakes that I see when physicians form hospital-based medical groups.

Of course, there are a lot more than seven, but these seven are strangely common.

Mistake #1

They use a one-size fits all agreement that later leads to hundreds of thousands or millions in litigation and damages.

There are no cookie-cutter agreements that can be used to correctly form *your* medical group. Yet, this doesn't stop someone from cutting and pasting from documents found on the web, or even prevent an association from publishing so-called "best practices" forms.

However, having seen many, many deals over my 30+ years of practice, I can assure you that no two groups have the exact same interests, the exact same issues, or the exact same concerns. They shouldn't have the exact same agreement.

Invest in yourself. Plan first. Only then build the correct agreement for your deal. Now isn't the time to get cheap.

Mistake #2

They don't devote significant planning to the group's governance structure.

Whether you are creating a four-person or a 400-person group, it's essential to carefully consider how the group will be governed. There are multiple governance structures to consider, from strong leader to sophisticated representative models.

Groups can destroy their ability to compete, whether in terms of competing against a third party for their sole exclusive contract, or in terms of competing in the larger market, as a result of a poorly thought out and implemented governance structure.

Mistake #3

They fail to plan for a complete or partial exit strategy.

This is a very broad and complicated category of error.

In today's active M&A market, an error in group formation can lead to creating so much difficulty in respect of a future sale, even one that is currently inconceivable, that it destroys the value of the group. If you believe that these details can be worked out later, you are setting yourself up for a dispute.

Related, there is an entire laundry list of mistakes made in connection with what a physician owner is entitled to when he or she leaves the group. I've seen these errors cost a group multiple hundreds of thousands of dollars, a loss that could have been avoided through engaging in a proper planning process upfront.

Mistake #4

They fail to incorporate a broad range of incentives and conduct-motivators into their compensation plan.

The operation of a successful hospital-based medical group requires more than simply billing unit production. Believing otherwise is entirely shortsighted.

There is no question that you will get exactly what you are motivating group members to provide. That means that if you make an error in motivation, you will get unwanted results, ranging from abusive behavior, to disincentivization of leadership, to outright sabotage.

Mistake #5

They fail to build in the full range of protections for the group's business, opening the group to competition from within when all they believe is possible is competition from without.

Sophisticated concepts go well beyond commonplace attempts to structure covenants not to compete and trade secrets protection.

Mistake #6

They fail to correctly deal with bringing additional physicians into the group and with removing them from the group.

Depending on the specific situation, it may make sense to create multiple classes of partnership. How are new members brought into the group? A real buy-in or a token one?

On the other side of the coin, groups often conflate the many reasons leading to a physician departing the group and treat all as economically the same. They are not.

Mistake #7

They create, whether by design or by error, a club and not a business.

This concept underlies many of the provisions of the formation documents, from the partnership or shareholders agreement to the professional services agreements and so on.

Your group must be a true business. Don't sell it, or yourself, short by failing to understand these concepts and to implement them upfront.

Conclusion

As mentioned at the outset, the above seven mistakes are among the most common that I see.

Of course, there are a lot more than seven.

If you remember only one thing after reading this, it's should be that you should act like a carpenter who knows to "measure twice, cut once."

Plan in advance. Consider all of the issues, even those that you don't believe are currently relevant. Only then document the arrangement.

It may practically be extremely difficult to impossible to correct an error built into your formation documents – but that's the issue underlying mistake # 8.



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