

Top Four (4) Tips on Negotiating Physician Employment Agreements¹

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Physicians are increasingly choosing employment over self-employment² for a variety of reasons including, perceived lifestyle benefits, job security, reduced practice management considerations, better negotiating opportunities with third party payers and vendors, and new incentives under quality-payment programs. As physicians continue to opt for employment and practices recruit physician employees, understanding the importance and art of negotiating physician employment agreements is critical for both parties.

This article summarizes the top four (4) tips for negotiating physician employment agreements both from the perspective of the physician employee and practice employer.

1. Choose Wisely.

Entering into a physician employment relationship is not much different than any other relationship. Each partner to the relationship should do their respective due diligence on the other to make sure that the relationship will be a good fit from a business and culture standpoint. Like in most new relationships, everyone puts their best foot forward. Thus, making sure any oral promises and commitments made at the outset of the relationship are reflected in the ultimate agreement is critical to avoid issues in the future. Additionally, having a potential physician employee candidate meet other members of the practice is a great way for the physician to gauge whether he/she can see himself/herself working with others in the practice and also the practice to determine if the physician will fit within the existing culture of the practice.

2. Understand What is Being Offered.

From both the practice employer's and potential physician employee's perspective, making sure that each party understands the terms and conditions of employment is key. Clearly outlining expectations, rights, and duties in the employment agreement helps avoid miscommunication and relationship challenges in the future.

Each party should also consider what terms are "deal breakers" and address them at the outset. Creating a checklist of these items may help facilitate and guide the negotiations. Terms or

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² Carol K. Kane, PhD, Policy Research Perspectives, *Updated Data on Physician Practice Arrangements: Physician Ownership Drops Below 50 Percent*, American Medical Association, available at <https://www.ama-assn.org/sites/default/files/media-browser/public/health-policy/PRP-2016-physician-benchmark-survey.pdf> (last accessed on 12/12/17).

conditions that give one pause initially generally tend to create problems later so it is best to address them immediately.

Parties sometimes provide or receive offer letters that contain the essential terms of the employment relationship such as the proposed compensation, duration of the agreement, termination rights, and restrictive covenants. Offer letters typically are not binding on the parties (although this could vary depending on the applicable jurisdiction), but serve as a negotiation tool to get the conversations started. Once the key terms are agreed upon, the terms are memorialized in a formal employment agreement.

Others simply offer an employment agreement and the parties negotiate the terms of the agreement. Ultimately the strategy taken is a business decision for the practice employer and may depend on the particular circumstances for the employment arrangement, including the timing of the anticipated employment.

3. Know Your Rights and Obligations.

Most employment disputes result from one party not clearly understanding what the party executed and agreed to in the employment agreement. To avoid potential dissatisfaction and disputes down the line, each party should carefully read and understand the terms of the employment agreement. Any items or provisions that are important to the contracting party – whether the party is the employee or employer – should be memorialized in the employment agreement. For example, if buying into a practice or specific benefits are critical for the physician, the physician should negotiate to include those specific terms in the employment agreement. At the end of the day, if the provision is not included in the employment agreement, the contracting party will have very little options to enforce the purported right.

Each party should engage experienced legal counsel who can assist the party in navigating not only potential healthcare regulatory issues that may arise as a result of the employment relationship, but also the contractual pitfalls that may exist as a result of a poorly drafted and negotiated employment agreement.

Every employment agreement should clearly address certain key areas including, for example:

Practice and Physician Duties and Obligations

Employment agreements should contain clear descriptions of the responsibilities of both the practice and the physician employee. While parties can be flexible in describing this information, it can be difficult to enforce any contractual language that is ambiguous or imprecise. Therefore, to the greatest extent possible, these obligations should be spelled out in detail.

Additionally, the agreement should specify the scope of the services to be provided by the physician, the generally expected hours, and the locations where the physician will be providing services. If a physician is expected to perform certain administrative services, these services should be spelled out in the agreement. Understanding whether call coverage responsibilities (including the frequency and scheduling of call coverage), supervision of mid-levels, and other duties will be imposed on the physician as an employee is critical both from a services and compensation standpoint (i.e., is separate compensation paid for these additional duties or are the

duties considered part of the overall scope of services expected in exchange for the proposed base compensation?).

Similarly, the agreement should describe the practice's responsibilities to provide space, equipment, non-physician staff, and other resources relevant to the physician's practice or as may be specifically needed by the physician to perform his/her duties. For example, if the physician is a vascular surgeon employed by a hospital and requires specific access to a catheterization lab or interventional procedure suite, the physician likely will want to spell out the physician's right to access and the specific schedule for such access in the employment agreement.

Day-to-day activities and operations may be governed by practice or hospital policies and procedures. Thus, compliance with practice policies and procedures may be included as a contractual obligation in the agreement. To ensure compliance with the same, copies of those policies and procedures should be shared (subject to potential confidentiality requirements if they are shared prior to the commencement of employment). Transparency by each party helps foster an open relationship from the beginning.

Compensation and Benefits

What the physician is paid both from a cash and benefits perspective is frequently the most heavily-negotiated aspect of physician employment arrangements. A variety of distinct compensation models may be used depending on the economic interests of the physician and the practice. Most parties are familiar with annual base salary models, and such models are generally the easiest to administer. However, with the changing healthcare regulatory reimbursement landscape (i.e., shift to value-based reimbursement models), many practices provide bonuses, implement withholds, or share in savings based on the productivity and achievement of certain quality and other metrics.

Many practices continue to utilize the "eat what you kill model", which is essentially a net revenue minus expense model. As an employed physician, understanding what revenue (e.g., personally performed clinical services and ancillary services) is counted towards the physician's total net revenue and clearly defining the same in the employment agreement is important to ensure the expected compensation is properly paid. Similarly, the employment agreement should clearly define what expenses – direct (e.g., fringe benefit cost) and indirect (e.g., proportionate share of rent, salaries and benefits of support staff) – are attributed to the physician for purposes of compensation.

Regardless of the type of compensation model utilized, the compensation terms, formula for the applicable compensation, and productivity or quality bonus amounts and metrics should be clearly described in the agreement. For example, many employment agreements include potential bonus payments for the achievement of certain "quality" metrics, but fail to outline in the employment agreement what those metrics actually are and how achievement of the same is measured. From the physician's perspective, having a clear understanding of how and when bonus payments will be earned and paid is imperative to ensure that compensation expected is actually paid.

Additionally, if any other services beyond direct patient care are being provided by the physician such as call coverage (e.g., compensation for call coverage services in excess of X days per month), supervision of non-physician staff (e.g., physician assistants and nurse practitioners), or

performing administrative services, compensation associated for such additional services should be clearly set forth in the employment agreement. If expectations do not align with the contractual language in the employment agreement, problems between the parties likely will ensue.

The specific fringe benefits and other compensation paid to the physician employee also should be included in the employment agreement including, but not limited to, health insurance, malpractice coverage (potentially including prior acts coverage for services rendered prior to the commencement of employment; coverage during the duration of the employment; and “tail” coverage), continuing medical education benefits, student loan repayment, licensure and association fees, moving expenses, and signing bonuses. Physicians should be aware of certain benefits (e.g., moving expenses, signing bonuses) that are treated as “loans” and expected to be repaid if, for example, the physician’s employment with the practice terminates within a certain period of time.

Regardless of the compensation model used, both parties must be mindful that the employment arrangement and compensation terms may raise issues under applicable fraud and abuse laws (such as the federal Stark Law, Anti-Kickback Statute, and similar state laws). Thus, the employment arrangement and associated compensation terms should be carefully vetted by experienced healthcare counsel to ensure the employment arrangement is structured in compliance with applicable federal and state laws.

Ability to Buy-In or Achieve Tenure

If the employment is in the private practice context, the parties may wish to specify the terms for the potential physician employee to buy-into the practice. Similarly, the terms of how and when a physician employed by an academic medical center may achieve tenure may be included in the employment agreement. Although physician employment agreements may include specifics related to potential buy-ins and achievement of tenure, often times the specifics with respect to the timing, cost, and process with respect to eligibility to buy-into (and, how ownership interests are redeemed) a practice are typically addressed in separate governance documents such as shareholder agreements or operating agreements. Similarly, specific terms related to tenure may be addressed by the academic medical center’s policies or other external documents.

If such is the case, as part of a potential physician employee’s due diligence of the potential employer, the physician should request to review such documentation in addition to the financials of the practice to get a clearer picture of what the physician may be investing in both from a financial and career standpoint. Be aware, however, that many potential employers will require the physician to execute a non-disclosure agreement prior to sharing any confidential information such as financials, which the physician should have reviewed by experienced legal counsel prior to execution of the same.

As noted above, at the end of the day, if these specific issues are of importance to the negotiating party, the issues should be included in the employment agreement.

4. Have an Exit Strategy

Ideally, no one starts a relationship with the intent to end it. Unfortunately, the reality is that not all relationships last. Thus, the parties should ensure that each has an exit strategy.

Typically, employment agreements include the following types of termination rights: (a) termination for cause (i.e., one party violates the terms of the agreement and such violation is not cured within a certain period of time); (b) termination without cause (i.e., a party can get out of the relationship for no reason as long as notice is provided within a certain period of time); (c) immediate termination if certain events occur (e.g., practice goes bankrupt; physician dies); and (d) mutual termination (i.e., both parties mutually agree to end the relationship).

With respect to terminations for cause, from the physician's perspective, the physician will want to make sure that the practice can only terminate the physician "for cause" if certain material events occur such as the loss of the physician's license to practice medicine or exclusion from participation in the Medicare or Medicaid programs. Be wary of subjective and ill-defined grounds for termination for cause such as "immoral actions" or "damaging the practice's or hospital's reputation". Since other provisions within the employment agreement can be affected by the method of termination (e.g., non-compete provision may be triggered; certain compensation may not be paid or be reduced), ensuring that the employment agreement includes only objective and material reasons to permit a "for cause" termination is essential.

On the flip side, practice employers will want flexibility to terminate a physician and may include certain rights to terminate the physician "for cause" that are more subjective in nature such as violations of the practice's policies and procedures by the physician or actions taken by the physician that adversely impact the practice's operations or business.

Additionally, many employment agreements permit either party to walk away for no reason – i.e., without cause termination – if notice is provided to other party within a certain period of time (e.g., 90 days prior written notice). Some employment agreements, however, may impose penalties for terminating an agreement if the requisite notice is not provided or if the physician resigns within a certain period of time from the commencement of employment (e.g., loss of any potential bonus payments earned, loss of accounts receivable credits toward net revenue for the applicable period).

Each party should weigh the pros and cons of having a without cause termination right in the employment agreement. For example, from the practice employer's perspective, presumably a lot of time, money, and energy were spent to recruit the physician, build the physician's practice and patient base, and integrate the physician within the practice. So allowing the physician to walk away for no reason may not be ideal unless that right can only be exercised after a set period of time (e.g., after the first two years of the employment agreement) or not at all by the physician (i.e., the practice can terminate the physician without cause, but the physician cannot terminate the agreement without cause). In contrast, from the physician's perspective, the physician will want the flexibility to get out of the relationship in the same manner as the practice employer. Moreover, the physician will want to ensure that the notice period for the practice employer's exercise of its termination without cause is long enough to allow the physician to find another job if the practice were to exercise such termination right.

Finally, if the physician is reaching retirement age, the physician may want to specifically negotiate to include a right in the employment agreement to terminate the agreement upon the retirement from the practice of medicine.

Effect of Termination

Further, the parties may want to consider and negotiate whether certain provisions of the employment agreement are affected by the method of termination. For example, obligations for the practice to purchase extended reporting endorsement coverage (commonly known as “tail” coverage) may be triggered only if the practice terminates the physician without cause or the physician terminates the agreement as a result of a breach of the agreement by the practice.

The effect of a termination as a result of retirement should be treated differently than other grounds for termination with respect to things like, for example, tail insurance (many insurers do not charge for tail coverage if the physician is retiring completely from the practice of medicine) and restrictive covenants. If the physician is also an owner of the practice, generally the terms for the physician’s buy-out from the practice are governed by the practice entity’s governance documents (e.g., operating agreement or shareholders agreement) and, thus, review and an understanding of the same is recommended.

Additionally, the parties will want to clearly outline what compensation is due upon termination. For example, if a “net revenue minus expense” compensation model is used, how accounts receivables that may not be collected until 90 or 120 days after termination will be credited for purposes of compensating the departing physician should be clearly specified. Physician employees may also want to specify that any bonus payments earned, but not yet paid (e.g., bonuses are paid within 30 days of the end of the calendar year and the effective date of termination is in the middle of the year) are paid to the departing physicians. On the flip side, practices may want to specify in the employment agreement that if a bonus is earned, but the physician is not employed as of the date bonuses are paid, the bonus is not paid to the physician.

Post-Termination Obligations – Restrictive Covenants

Many employment agreements include post-termination obligations such as non-solicitation provisions (i.e., the physician is prohibited from soliciting patients or employees of the practice for a certain period of time post-termination) and non-competition provisions (i.e., the physician is prohibited from practicing within a certain geographic scope for a specified period of time). Generally, non-solicitation and non-competition provisions are governed by state law and, thus, their reasonableness and enforceability varies state-by-state. Therefore, restricted covenants should be drafted in accordance with and reviewed under applicable state law.

That being said, there are many ways to negotiate restrictive covenants from the employee’s and employer’s standpoint. For example, the circumstances under which the restrictive covenants apply could vary such as the triggering of a non-competition provision if the agreement is terminated without cause by the physician or as a result of a breach of the agreement by the physician (i.e., non-compete does not apply if the physician retires, the practice terminates the agreement without cause, or the physician terminates the agreement for cause). Additionally, the scope of the restrictive covenant could be restricted in a variety of ways including, for example, by limiting the restriction to a specific geographic scope (e.g., 10 miles of each of the office locations at which the physician worked while employed) or type of service (e.g., prohibiting the physician from practicing vascular surgery, but not the practice of medicine generally; prohibiting the physician from practicing in an independent practice, but allowing the physician to work for any hospital).

Many large hospital systems and practices may take the position that the restrictive covenants (and, perhaps the employment agreement as a whole) are non-negotiable. Given the significant impact restrictive covenants and other provisions within an employment agreement can have on a physician's career (especially if the relationship does not pan out as expected), the physician should pause to consider whether the employer is one with which the physician wants to work, take the time to carefully review and understand what the physician is signing, and get the appropriate legal support needed to ensure the physician's interests are protected.

Conclusion

As an increasing number of physicians move into employment models, practices and physicians need to be aware of the most common areas of negotiation and potential legal risk. By being educated of the potential differing legal and economic interests of the employer and the employed physicians, both parties will be better equipped to form a lasting and successful relationship, which hopefully leads to accomplishing the presumed goal of both parties - the provision of high-quality patient care.

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