

Medical Economics

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Where do you stand?

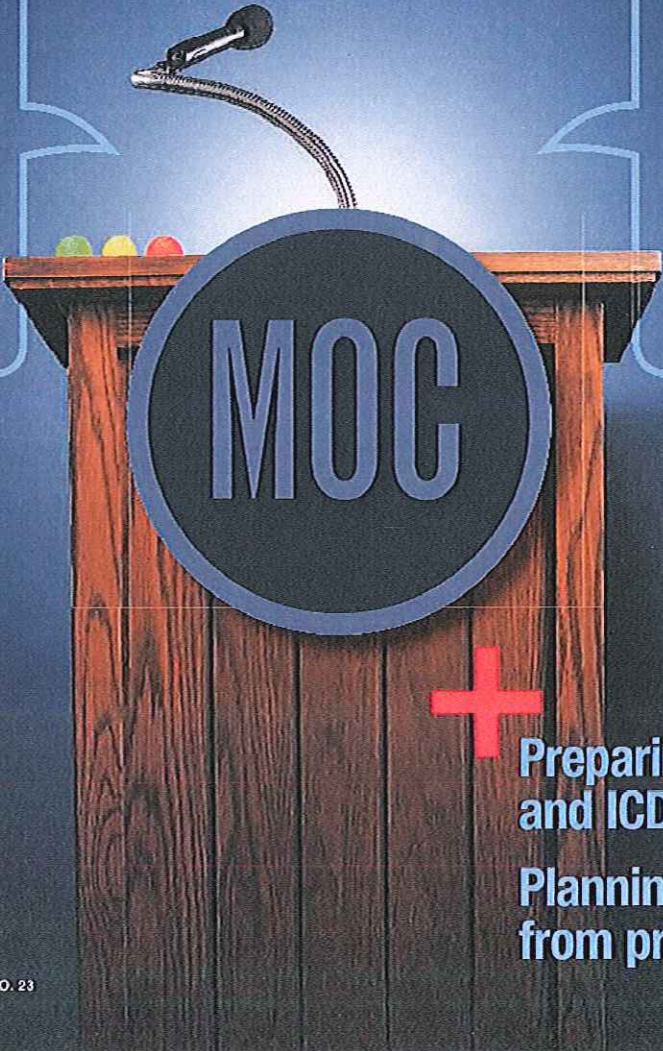
Maintenance of certification process
sparks debate

FOR

"MOC validates
skills and
can improve
outcomes."

AGAINST

"MOC is
complicated,
time-consuming,
and expensive."

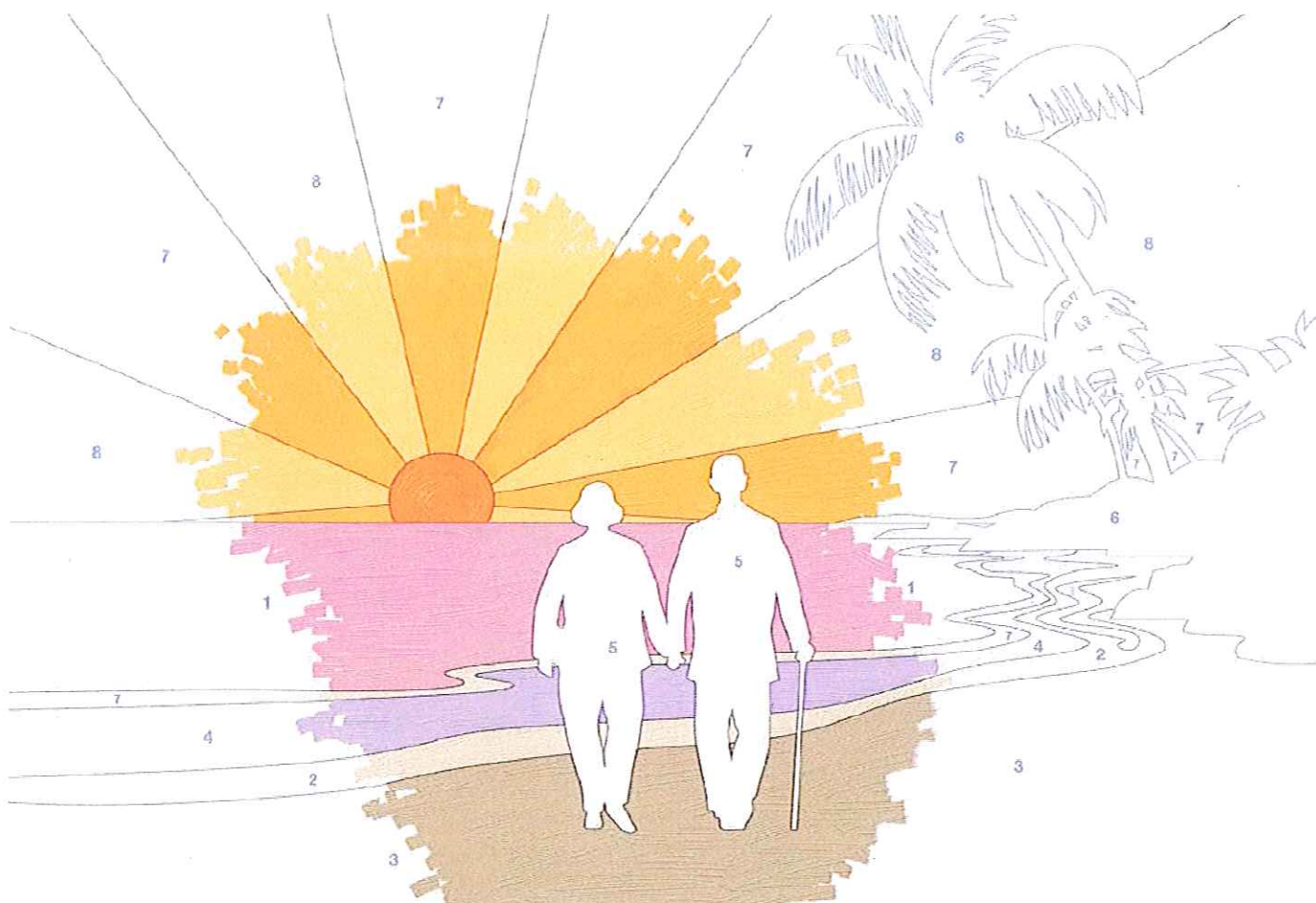


MOC



Preparing for 5010
and ICD-10

Planning your exit
from practice



Planning your exit strategy

A SMOOTH TRANSITION TO A COMFORTABLE RETIREMENT REQUIRES YEARS OF ADVANCE PREPARATION

[By **JOHN F. HILL, CFP**, and **ANDREW P. RHEA, JD** | Illustration by **JEFF SUNTALA**]

Many physicians spend the majority of their adult lives training for and practicing their specialty. For most, it's 8 to 10 years training and another 30 years or so of practicing. That's a significant investment of time and financial resources, so it makes sense to approach your practice as a true "going concern." A comprehensive plan will protect earnings and assets, create diversified sources of retirement income, and redeem ownership share in your practice for its maximum value.

Develop a retirement and succession plan long before you exit—to allow financial strategies to work over time and to preserve the value of your practice and ensure future revenue by recruiting and training younger physicians.

FEAR OF OUTLIVING ASSETS

The most common retirement concern is outliving your assets. This is because of longer life expectancies and the uncertainties of returns in the stock market experienced over the last decade or so. According to the

2000 annuity mortality table, spouses who are both 65 years old have a joint life expectancy of age 92 (that is, at least one spouse can be expected to reach that age). Because retirement years can last as long as your peak earning years, putting the correct benefits and plans in place to handle retirement is critical.

We've seen more physicians working part-time or serving as consultants for at least 3 years before full retirement. Doing so allows them to maintain some income, remain professionally challenged, and evaluate and groom potential successors. Our clients frequently remind us that, after decades of building a successful practice and a sound referral base, it takes time to transition that hard work and goodwill to younger partners. This partial retirement period can bridge the gap between patients, referral sources, and the next generation of physicians.

The timing of your retirement can be influenced by your ability to maintain health insurance, disability income, and long-term care insurance. Company-sponsored healthcare plans are relatively affordable,

but private insurance premiums can be very expensive, especially if there has been a serious illness or injury in the past. Because Medicare coverage doesn't begin until age 65, consider the availability of health insurance when you are contemplating retirement.

"If your practice employs multiple physicians, contact your employee benefits agent or broker to discuss ways to maximize your purchasing power for long-term disability, long-term care, and life insurance," says Dudley Wooley, CPCU, CRM, CIC, president and chief operating officer of Ross & Yerger, an insurance firm with offices in Mississippi and Louisiana. "Purchasing these types of coverage on a group basis affords you the broadest coverage and terms for the lowest cost. Also, it can be advantageous to explore how to pay for these benefits in full during your highest wage-earning years."

THE ROLE OF LONG-TERM CARE INSURANCE

Regarding long-term care, no doubt you are well aware of elderly patients or family members who need in-home care or an assisted-living facility. Seventy percent of retirees will need some form of long-term care, and the median daily cost of a semi-private room in a skilled nursing facility is \$193 per day, according to the Genworth 2010 Cost of Care survey.¹ Expenses such as these can invade lifetime savings and erode retirement plans quickly.

One tool for combating these expenses is long-term-care insurance. Depending on entity structure, policy premiums could be tax deductible for employed physicians. Policies can cover different services, including skilled in-home care, family reimbursement for care, and nursing home care. Policies paid for by the practice can be a valuable benefit for retiring physicians and part of their practice buyout.

BUY/SELL AGREEMENTS

If you are like most physicians, your interest in your practice likely makes up a large part of your net worth, and therefore your retirement income. Consequently, it is imperative to have a buy/sell agreement in place. The agreement should contain provisions on how the practice is valued and how it can be transferred or sold if you retire, die, have your employment terminated, or become disabled. The agreement also must address how the practice will be dissolved should the involved parties fail to reach an accord.

"There are many ways to value a physician's interest in a medical practice as of his or her exit date," says Jody Varner, a member of the Jackson, Mississippi, law firm Brunini. "I've seen everything—hiring an appraiser to value the interest, making the purchase

price a function of earnings in previous years, paying the departing physician a share of his or her accounts receivable, and just picking an agreed-on number. There is no one size fits all." Whichever method is selected, Varner recommends that the group revisit the valuation method every year at the practice's annual meeting.

Events such as disability and death should define your funding options and payment methods. Life and disability buyout insurance is a popular option because it provides tax-free liquidity that allows the remaining physicians to purchase the departing physician's share immediately. Any value in excess of insurance proceeds is paid out monthly over a period of no more than 5 years. Retiring physicians typically receive installment payments for their share of the practice. Because these payments represent retirement income, it is critical that the transition go as smoothly as possible to maintain the success of the practice.

ENDING PRACTICE TIES

Generally, you can end your partnership interest in a practice either by selling it to an existing partner, or selling the partnership itself. A sale to a current partner means that the partner purchases all of your interest in the practice. This type of accord is commonly referred to as a cross-purchase agreement. It is the preferred method when the objective is to give younger physicians more interest in the practice. Or the partnership can purchase the physician's share and give all remaining partners a proportionate share of the sold interest.

Selling to an outside party, such as a larger health-care provider or hospital, is becoming more common. This strategy usually is considered when physicians in a group are seeking enhanced benefits and reduced professional liability.

Of course, the sale of a business interest carries tax implications. Although most partnership sales are taxed at capital gains rates, this is not always the case. Sale proceeds that represent accounts receivable and inventory are treated as ordinary income. According to Raleigh Cutrer, CPA, of Matthews, Cutrer and Lindsay, PA, an accounting firm in Ridgeland, Mississippi, "If the physician is selling his or her stock in a professional corporation, the treatment should be long-term capital gain," which at the federal level is taxed at a 15% rate.

If you're selling your interest in a partnership, however (either general, limited, or a limited liability company), at least a portion of the sale will be treated as ordinary. Seek advice from a qualified adviser such as a tax attorney or CPA before executing such a transaction.

BUILDING YOUR RETIREMENT NEST EGG

In retirement, you'll need different sources of income or benefits from which to draw. Many physicians think their qualified retirement plan balance will be sufficient to support their desired retirement lifestyle.

Unfortunately, this is seldom the case for high earners. Because of IRS limits on retirement plan contributions, you may need other sources of post-retirement income and benefits. For instance, in 2011 your annual contributions to a 401(k) from all sources may not exceed \$49,000, or \$54,500 if you're over age 50.

Because physicians are typically high earners, the money sourced from a qualified retirement plan and Social Security may account for as little as 50% of a doctor's desired income. A nonqualified deferred compensation plan—an arrangement that allows you to defer income until a later date—is one way to fill this gap. The deferred income is not taxed until you receive it, and then it's usually taxed at a lower

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rate because retired physicians almost always are in a lower tax bracket than active doctors. Deferred compensation plans also can be structured to include contributions and deferrals from both you and the practice, resulting in a significant income supplement.

You may also consider after-tax plans. Depending on how the after-tax money is invested, you can establish a fund that grows tax-deferred and can create tax-free income during retirement. Physicians and practices can take advantage of high cash value life insurance policies to create this income. Policy cash values grow tax deferred and can create tax-free income streams. These plans are similar in structure to the ones that large corporations use for their executive benefits. The benefits can be practice-sponsored and/or part of a buyout agreement.

Important investment decisions come with the sale of practice interests and the rollover of 401(k) plans. Many physicians contemplating retirement assume distribution rates of 6% to 7%, that is, they plan to withdraw 6% of their investment balance annually during retirement. Studies indicate that with a bal-

anced portfolio and a 6% withdrawal rate, a portfolio lasts 17 years on average.²

As suggested earlier, retirement periods are often much longer because of increased life expectancies. Most financial advisers recommend a 4% withdrawal rate. At that rate, a portfolio lasts an average 26 years.

Although it's wise to invest more conservatively after you retire, many retirees invest too conservatively too soon and risk outliving their assets.

DIVERSIFYING TO ACHIEVE GROWTH

Not only should investment allocations reflect a long-term horizon; you need to achieve growth in your asset portfolio to offset the effects of inflation. And it's important to include other asset classes with a traditional stock and bond portfolio—managed futures, private equity funds, and real estate investment trusts—to further diversify. (Be aware, however, that using diversification as part of your investment strategy neither ensures nor guarantees better performance and cannot protect against loss of principal due to changing market conditions.)

Also consider variable annuities with deferral credits and minimum lifetime withdrawals. These benefits provide a predictable, sustainable, and potentially increasing income.

Because of the complexity of planning for many contingencies, today's physicians need plans to protect both their business interests and their retire-

ment nest eggs. By using the expertise of financial, legal, and tax advisers, you can avoid potential pitfalls and ensure the smooth transition of a practice that took years to build. Small steps now can give you peace of mind and allow you to shift your focus from healthcare to wealth care. ■

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