BETTER Employment AGREEMENTS

A WELL-PREPARED EMPLOYMENT AGREEMENT ensures that physicians and their groups understand what each expects of the other. Here are 10 key considerations.

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This is the second article in a two-part series examining key medical group contracts. The first article, which appeared in the August 2007 edition, focused on medical group buy-sell agreements.

A physician's employment agreement with his or her medical group is the bedrock document defining their relationship. The employment agreement should clearly reflect the physician's and the group's expectations, rights and obligations with respect to each other. Failing to do so can lead to misunderstandings, suboptimal performance, termination of the relationship and a lawsuit.

This article discusses the key terms and conditions that every physician employment agreement should address. Keep in mind that employment agreements are not only for physicians just out of training. They are equally important for owners of professional medical corporations who are also employees of their groups.

Employee vs. Independent Contractor

Full-time physicians need to be hired as "W-2" employees and not "1099" independent contractors. Even if a physician wants to be hired as an independent contractor to "save on taxes," it is generally a bad idea for both parties. The group runs the risk that the Internal Revenue Service and California Franchise Tax Board will impose fines and penalties if the physician is improperly treated as an independent contractor. There are also potential kickback and fraud and abuse risks for independent contractors that are not present for employed physicians.

From the physician's standpoint, an independent contractor has to pay the 15.3 percent self-employment tax and does not have the employee protections provided by federal and California labor laws.

Employment Duties

The agreement should address issues such as the physician's work hours and on-call obligations, the specialty in which the physician will practice, whether moonlighting will be permitted, and whether the physician will be expected to assist in practice administration and promotion.

Term and Termination

The term of the agreement (e.g., one or two years) and whether it will automatically renew should be specified. Equally important are provisions for early termination. Typically, three categories of termination should be addressed:

- Termination with or without cause upon a specified number of days notice (e.g., 30-90 days).
- Termination for breach of the agreement. The physician is generally given a period of time (such as 15-30 days) to attempt to "cure" the breach.
- Immediate termination in the event of certain very serious problems, such as loss of medical license or medical staff privileges, exclusion from the Medicare or Medi-Cal programs, conviction of a felony, uninsurability, endangerment of patients, or acts of dishonesty.

Compensation

Compensation provisions vary widely from straight salary to complex production formulas. Development of a compensation formula that incentivizes desired physician behavior is obviously essential to the success of any group. If a production-based formula will be used (such as a percentage of the physician's collections or profits), the formula needs to be clearly described. For very complex formulas, examples should be included. It should be noted that under the so-called "Stark" law, a physician cannot be compensated directly for ordering certain ancillary services (such as laboratory, physical therapy and imaging) for Medicare patients.

If some or all of the physician's compensation will be based on a production formula, the employment agreement should describe how both revenue and expenses will be determined and allocated. If not handled carefully, the allocation of expenses can be complicated and lead to disputes. For example, some groups allocate certain expenses equally (such as rent), other expenses based on production (such as supplies), and some 100 percent to the physi-

cian (such as continuing medical education tuition).

In any production-based formula, it is also important to agree upon how post-termination collections will be handled. Will a departing physician be credited with collections that he or she generated before leaving? If so, for how long? What post-termination liabilities and expenses will be charged to the departing physician? Finally, as noted in the first article in this series, groups need to ensure that post-termination payments qualify under the IRS' new rules for non-qualified deferred compensation plans. Otherwise, the deferred compensation may be taxable to the physician before he or she actually receives the money and also subject to penalty taxes.

Fringe Benefits

The employment agreement should describe the fringe benefits that will be provided, such as paid time off; CME tuition; health, life and disability insurance; automobile allowances; medical staff and professional society dues; license fees; and cell phones. Malpractice insurance should be addressed, including the amount of coverage and who will pay for a "tail" policy in the event of termination.

The agreement should also include a reasonable policy setting a limit on the amount of paid time off a physician can accrue. Otherwise, upon termination, the group runs the risk of owing the physician an enormous amount of money for unused paid time off.

Credentials and Staff Privileges

The employment agreement should specify whether the physician is expected to be board certified and on the staff at certain hospitals, and how long the physician has to obtain board certification and staff privileges.

Sickness and Disability

The employment agreement should provide that if the physician is unable to work for a specified number of consecutive or *non-consecutive* days, the physician can be considered disabled, and the employment agreement terminated. Depending on the size of the group, disability provisions may need to comply with federal and California laws, such as the Americans With Disabilities Act and the Family and Medical Leave Act. The employment agreement should also address what compensation, if any, the physician will be entitled to while on disability leave.

Finally, the agreement should provide that if there is a question as to whether the physician is or remains disabled, the matter will be decided by an independent physician selected by the group.

Restrictive Covenants

Typical restrictive covenants include prohibitions against using the group's confidential information and trade secrets and against soliciting the group's patients, referral sources and employees. The enforceability of such provisions, however, is not guaranteed if they are overbroad. Restrictions on a physician's right to practice medicine after leaving the group will not be enforceable for nonowner physician employees. But such provisions may be enforceable in the case of physician owners who are selling back their stock in the group for a fair market value amount that includes a payment for goodwill.

Review and Amendment

Groups should review their employment agreements periodically to ensure they comply with current law and still reflect the goals and understandings of the parties. If an amendment to a physician's employment agreement is necessary, it typically cannot be made unless both the group and the physician employee agree in writing.

A problem can arise when a group with multiple physician employees wants to adopt an employment agreement amendment that will apply equally to all of the physicians who are shareholders, but one or two physicians refuse to sign the amendment. To prevent this, each shareholder physician's employment agreement should provide that the group can amend it unilaterally in order to adopt groupwide amendments that do not unfairly discriminate against any of the affected physicians.

Disputes

It is an unfortunate reality that many physicians who are terminated threaten to or actually sue their former groups. Therefore, employment agreements should include a provision requiring that the parties attempt to resolve any dispute through mediation. In mediation, a retired judge or experienced attorney attempts to help the parties reach a voluntary settlement of their dispute. Mediation frequently enables the parties to save considerable time and attorneys' fees.

If the parties are unable to resolve the dispute through mediation, then the employment agreement should specify whether the parties must submit the dispute to binding arbitration, rather than having the right to sue in court. Traditionally, arbitration has been viewed as a faster and cheaper way to resolve disputes, when compared with litigation. But this is not always the case.

Further, except in very limited circumstances, the losing party in a binding arbitration will not be able to appeal the arbitrator's decision. Obviously, that is good for the winning side and bad for the loser. Finally, if an arbitration provision will be included in the employment agreement, the group needs to ensure that it complies with California law. There have been a number of cases in California over the past five years invalidating arbitration provisions in employment agreements on the grounds that certain terms were unfair to the employee.

A well-planned and well-prepared employment agreement helps ensure that physicians and their groups understand what each expects of the other, encourages the right behaviors and discourages the wrong ones, and provides a mechanism for resolving disputes. ■

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