NARDONE LIMITED

YOUR BUSINESS, LEGAL, TAX, AND HR ADVISORS

DENTAL PRACTICE ADVISOR – SUMMER 2016

Nardone Limited ▪ 300 E. Broad Street, Suite 490 ▪ Columbus, Ohio 43215 ▪ www.nardonelimited.com ▪ (614) 223-0123

How to Properly Restructure a Dental Practice

By Brian Biglin, Attorney at Nardone Limited

Taxes affect us all and, as small business owners we need to realize the benefits of proper tax planning more than most. Many dentists are restructuring their dental practices to maximize the tax advantages offered by a customized business structure. Restructuring allows them to better manage the flow of their revenue, increase profitability, and enhance the organization of their dental practice. One of the most popular business structure enhancements is to establish a management company to help with the operations side of your dental practice. Of the utmost importance, however, is to enter these new business structures with a holistic view toward fully integrating these changes into your overall dental practice procedures and processes. Attempting to restructure as a half-measure is ultimately not the right path to follow, as evidenced by the recent federal court case of a California dentist and the management company he created.

The Case

In January 2016, the U.S. Court of Appeals for the Ninth Circuit decided against a dentist who had sought to claim fees charged by his management company as expenses to be deducted from his federal income taxes. The Court agreed with the US Tax Court in disallowing the expense deductions in *Wiley M. Elick DDS, INC v. Commissioner of Internal Revenue*, 117 AFTR 2d 2016-457. The U.S. Supreme Court has denied review of this case, finalizing the federal court of appeals ruling.

In the *Elick* case, a dentist from California established a company to manage his Practice's operations. The management agreement stated that the management company would provide various services such as: produce annual budgets; investigate and document in writing customer complaints; develop policies and procedures; recruit, supervise and train employees; perform fiscal services; and ensure regulatory compliance. All of these services are vital and necessary to the operation of a dental practice and must be performed in the ordinary course of the functioning of a dental practice. Management companies can be a great tool to enhance your dental practice's productivity, bottom line and income. But, as the *Elick* case proves, the business structure that puts these entities in place and integrates them into your dental practice operations must be done properly.

This case stated that the Tax Court disallowed the deduction of the management company fees from the dentist's federal income taxes as not being "ordinary and necessary" expenses. As mentioned earlier, the services the management company purported to offer were all matters that are necessary to the operations of a Practice and must be done in the ordinary course of business for a dental practice. What happened? What went wrong and how could it have been avoided?

How Could This Have Been Avoided?

The facts set out by the Court indicate that there were several failures with regard to actually integrating the management company into the overall business structure of the dental practice. The first failure was that the management company had no functioning employees. The dentist was designated as a "co-employee" of the management company and his main dental practice entity, but was then also listed as a full-time employee of the Practice. The dentist employed an office manager who was also the dental practice bookkeeper. However, that person was not an employee of the management company. This failure could have been avoided if the office manager, and other Practice employees, had been properly moved to be employees of the management company, which is a fairly easy matter to handle.

The second failure is related to the fact that there were no records or other indications that the management company actually provided the management services it claimed to offer. Having sound procedures in place to help your office staff keep appropriate records is not only vital to your operational success; it is required under numerous federal laws that impact the dental profession, such as HIPAA.

(Cont'd on Page 2..)

(Cont'd from Page 1..)

The third failure was that the management company never issued monthly invoices. The Court found that it was compensated at the end of the year with a lump sum amount calculated solely by the dentist that owned the Practice. The lump sum amount was not based upon invoices, services performed, or the advice/estimate of his accountant. If you are operating your management company properly, issuing invoices for services rendered will become a very easy and standard process, and allow for successful documentation of the management company expenses without issue. The invoices will track the expenses for the services rendered and allow for appropriate calculation of those expenses at year end without the need to generate numbers to make them fit.

Conclusion

The failures to properly integrate the management company into the dental practice were foreseeable and could have easily been avoided, as mentioned above. The best way for your dental practice to avoid failures of this type, and others like them, is to work with an experienced team of dental professionals that can help you properly and fully integrate your new business structure into your dental practice. It would not make sense to buy a new piece of equipment for your dental practice, planning not to use it or intending to use it improperly.

Entering into a business restructuring to receive all of the benefits the new structure offers, and then not implementing it properly also wouldn't make sense. The new business structures for dental practices can offer enhanced profitability, asset protection and increased organization. The experienced dental attorneys at Nardone Limited can help you create a new business structure that works for your dental practice. We are available to help you make certain that the new structure is properly integrated into your dental practice so that you receive all of its benefits, and avoid any potential pitfalls.

Quote of the Month

"As we learn we always change, and so our perception. This changed perception then becomes a new Teacher inside each of us."

Hyemeyohsts Storm, taken from
"The E-Myth Dentist" by Michael E. Gerber

Upcoming Events

July 4, 2016
Nardone Limited offices will be closed in observance of Independence Day.

July 22, 2016
KiDDS Cup Charity Golf Tournament at the Little Turtle Golf Club. See below for details.

September 16, 2016
Paragon's Indiana Excelleration Seminar at the Sheraton Indianapolis Hotel at Keystone Crossing.

October 14, 2016
Paragon's Ohio Excelleration Seminar at the Sheraton Hotel in Downtown Columbus.

SAVE THE DATE

You won't want to miss this year's golf outing! Save the date and join us in helping to change the lives and smiles of children all around the world. Submit your registration today!

Please call Zimmerman, Boltz & Co. at (614) 939-4700 with any questions regarding your entry.

Moving Artwork to an Irrevocable Trust

By Ashley Privett, Attorney at Nardone Limited

As a dentist, you are likely aware that the atmosphere of your dental practice is a key factor in making your clients feel comfortable. Because of this, many dentists feature a variety of artwork in their dental office, not to mention their home. A recent trend in estate planning has been transferring the ownership of artwork to an irrevocable trust as a way to benefit from tax savings. We have provided an overview of this process below.

What is an Irrevocable Trust?

A trust is a relationship created at the direction of an individual, in which one or more persons hold the individual's property subject to certain duties to use and protect the property for the benefit of others. One specific type of trust is an irrevocable trust. An irrevocable trust is a trust that cannot be changed or cancelled once it is set up without the consent of the trust's beneficiaries. Irrevocable trusts offer tax advantages that revocable trusts do not. Further, the transfer of assets to an irrevocable trust is a taxable event resulting in gift tax liability, as discussed further throughout this article.

Benefits of Transferring Art to an Irrevocable Trust

If you transfer the ownership of your artwork to your irrevocable trust, then the artwork will no longer be legally part of your estate. As a result, there will be a reduction in value of your estate for tax purposes. An irrevocable trust includes property that no longer belongs to you, and so the assets will not be subject to estate tax after your death. Further, you would be gifting the artwork to your irrevocable trust and the artwork would be appraised at the time of the gift for tax purposes. If the appraised amount is higher than the current $14,000 annual exemption from gift taxes, then any excess amount will be deducted from your lifetime combined federal gift-tax and estate-tax exemption, which is currently $5.45 million. If that exemption has already been used, you will pay tax on the gift. Ultimately, if you, as the owner, retain ownership of the artwork instead of gifting it to your irrevocable trust, then it is very likely that the artwork will be appraised at a much higher value when you pass away, which would result in a higher tax liability for your estate. Irrevocable trusts are taxed on income similar to the way individuals are taxed on income. Transferring assets to an irrevocable trust can also save on annual income tax. The grantor of the irrevocable trust is not personally liable for income taxes on trust income because the tax liability belongs to the trust itself. Ultimately, transferring the artwork to your irrevocable trust shifts the tax responsibility to your beneficiaries.

Renting the Artwork Back from Your Trust

Once the artwork is gifted to your irrevocable trust, the trust will be responsible for storing and caring for the art. If you want to continue to enjoy your artwork in your home or your dental practice, you would simply rent the artwork back from the trust. It is important to remember that you must pay fair market rent for the artwork, which can be difficult to determine since it is a more limited market. If you do not pay fair market rent to the trust, then it would likely be a violation of the trustee's duties and responsibilities. Further, if you are ever audited by the Internal Revenue Service ("IRS"), then you will want to be in a position to provide documentation to the IRS regarding the fair market rent. The IRS has not provided set standards for determining fair market value for art rentals. Thus, hiring an art leasing firm to set the rental price and keeping documentation of the firm's findings is your best defense in the event that you are ever audited by a taxing authority or someone questions the trustee's decisions or actions.

Beneficiaries

Do the beneficiaries of your trust have any input regarding your artwork once it is placed in a trust? Any property placed in your trust, including any artwork, belongs to the trust and would not belong to the beneficiaries. Thus, the beneficiaries may enjoy the artwork; however, they cannot sell the artwork. Only the trustee can sell the artwork. Ultimately, if the beneficiaries do gain ownership of the artwork, and it is sold, they would pay capital-gains taxes at the appreciated value of the artwork. If the trustee sells the artwork, then the trust would pay the same taxes that the beneficiaries would. The taxable amount would be the difference between the value at the time of the sale and the tax basis, which is generally the amount paid for the art by you.

If you have artwork that has high value or you believe will appreciate over time, then you may want to consider establishing an irrevocable trust to place your artwork in simply for tax savings purposes. Even if you transfer ownership of the artwork to an irrevocable trust, as long as you or your dental practice pays fair market rent to the trust, the artwork can hang in your dental practice and everyone in your dental office can still enjoy the piece.

If you would like more information on estate planning or would like to discuss preparing your estate plan with one of our estate planning attorneys, please contact Nardone Limited at (614) 223-0123 or visit our website at www.nardonelimited.com.

The Necessity of a Written Employment Agreement

By Blair Browning, Law Clerk at Nardone Limited

One of the first discussions to occur when a practice hires a new associate dentist is about the parties' expectations, understandings, and goals. Oftentimes, these verbal agreements regarding the employment relationship between a Practice and an associate dentist are not memorialized in writing. Memorializing the employment agreement is necessary to protect both parties' interests. Four key reasons it is important to have a written employment agreement with your associate dentist(s) are as follows:

1. Issues The Parties May Not Have Considered

Drafting and preparing a written employment agreement forces the parties to focus on and address the issues they may not have considered. This is even more effective when the parties seek experienced dental attorneys, who are able to highlight legal issues that are unique to the dental field. For example, practices may not be aware of the various ways to compensate associates. Other terms or issues the parties might not discuss or address include: (i) definitions, such as the definition of net collections or production, remake, rework, etc.; (ii) required administrative duties that the associate dentist will be required to perform during their employment; (iii) fringe benefits, such as malpractice insurance, payment for continuing education, and professional associations or organizations, etc.

2. Resolves Uncertainty and Eliminates the Possibility of Confusion

In any business relationship, clearly expressing the terms in writing will eliminate ambiguity and any uncertainty the parties may have. This is especially true if the attorney drafting the written agreement has experience and knowledge regarding the particular profession. For example, the employment agreement may address the nature of the associate's compensation, the associate's duties and responsibilities, and any benefits the associate will receive as part of their employment. Because there is no "one-size-fits-all" employment agreement, the written agreement can and should be customized in each situation. An attorney can be an invaluable tool to ensure that your written agreement is customized, unambiguous, and detailed.

3. People Often Forget the Terms of the Agreement

It is foolish to assume that both parties will remember each and every business term and related details previously discussed and negotiated. Even if both parties do recall all terms and details discussed, the parties' interpretation of their discussions might differ. If the parties forget the terms and details discussed and if their interpretations of such differ, it will inevitably lead to conflicts unless the agreement is in writing.

For these reasons, it is important that the Practice memorializes these business terms involved in an employment relationship with an associate. Even more seriously, when parties recall the negotiated terms differently, it oftentimes leads to litigation. As a result, the parties end up spending time and money to assert their rights, both which could have been avoided had the parties put their agreement in writing.

4. Helps Parties Avoid Being Taken Advantage Of

Finally, in the unfortunate event that you are in a business relationship with someone who is attempting to take advantage of you, a written employment agreement serves to support your claim better than making the argument that there was a verbal agreement addressing it. Without a written employment agreement, your attorney is less equipped to represent your position. Further, in the event of trial, without a written agreement, a judge is forced to determine who is more credible and who is telling the truth. Additionally, a written employment agreement gives your attorney the resources to threaten litigation if the other party breaches the agreement. Written employment agreements, therefore, can also serve as a litigation tool for you and your attorney to defend against a dishonest business partner or associate.

Vince Nardone Comment: From my perspective, the three most important provisions of an employment agreement are: (i) the compensation, (ii) restrictive covenants, including non-compete and non-solicitation, and (iii) the term and exit strategy, both for the employing Practice and the associate dentist. If you do not have a written agreement documenting the compensation, issues will arise. If it is not clear how long the relationship will last, or how one may end the relationship, issues will arise. Most importantly, if the parties do not protect their interest as it relates to a non-compete or non-solicitation, that Practice or that associate, at some point, will incur much more significant expenses than the initial expenses of having a well-drafted employment agreement negotiated and finalized. Take the time and make the investment on the front side. Or, risk taking more time and incurring much more expense on the back side.

Contact Nardone Limited

If you have any concerns about employment or business matters at your dental practice, specifically regarding written employment agreements, you should contact one of the dental attorneys at Nardone Limited. Nardone Limited represents dental practices in many different areas such as: (i) employment contracts; (ii) labor and employment representation; (iii) buying and selling dental practices; and (iv) human resource representation. If you would like more information regarding your dental practice, contact Nardone Limited.

Preventing the Unauthorized Use of a Dental Practice Patient List

By Vince Nardone, Attorney at Nardone Limited

It is important to remember that dentistry is business. As an essential component of the business side of dentistry, dentists work hard to develop a Practice patient base. Patients are the lifeblood of a successful dental practice, as patients are the source of the business's revenue. A dental practice's patient lists are a very valuable asset to any Practice. Thus, it is imperative that dental practices take appropriate steps to prevent any unauthorized use of their Practices' patient lists. Fortunately, there are a number of steps that a dental practice owner should take to prevent employees or former employees from improperly removing or misusing the Practice's valuable patient lists. Unless a Practice owner takes appropriate steps to prevent the unauthorized use of patient information, he or she may unnecessarily lose patients.

Preventative Measures to Protect Patient Lists

To prevent a current or former employee from steering business away from a Practice, a dental practice owner should take steps to ensure the confidentiality of patient lists. Ohio law provides protection for a business owner with valuable confidential information. Ohio's Uniform Trade Secrets Act prohibits the improper disclosure or use of a "trade secret," which has a specific meaning under Ohio law. A trade secret includes a listing of names, addresses, or telephone numbers, that (i) has independent economic value from not being generally known to others, and that (ii) is the subject of reasonable efforts to maintain the secrecy of the information. Thus, certain confidential business information, such as a patient list, may constitute a trade secret. As a result of being a trade secret, Ohio law prevents improper use or disclosure of this information.

There are a number of steps that a Practice should take to ensure that these protections would be deemed to apply to your Practice's patient list. As described below, a Practice should ensure that it has a confidentiality policy in its employee handbook and contracts. Such a policy should state, among other things, that the Practice's patient lists and other proprietary information is confidential. A dental practice should also ensure that it takes steps to protect its confidential information, such as password protecting files and locking file cabinets.

The exclusion against improperly disclosing or using trade secret information applies to information in tangible form. But, it may also apply to information that employee memorizes, such as patient identities. The Ohio Supreme Court has ruled that patient lists are protected trade secret, and remain a trade secret even when the list is memorized. *See Al Minor & Assocs. v. Martin*, 117 Ohio St. 3d 58, 881 N.E.2d 850 (2008).

Thus, an employee cannot memorize trade secret information, and then attempt to disclose or use that information for their own benefit without being authorized by the owner of the trade secret. Despite these protections, the specific contours of what is a trade secret are not well-settled under Ohio law. For example, in *Al Minor & Assocs.*, the Ohio Supreme Court acknowledged that employees will have memories "casually retained from the ordinary course of employment." Thus, the Court suggested that information casually acquired in the ordinary course of employment, such as learning the names of patients through day-to-day interactions, does not constitute a trade secret. Additionally, an intermediate appellate court in Ohio has expressed skepticism over whether a list of patient names by itself will constitute a trade secret. *See Columbus Bookkeeping & Bus. Servs., Inc. v. Ohio State Bookkeeping, LLC*, 10th Dist.No. 11AP-227, 2011-Ohio-6877.

Confidentiality and Non-Solicitation Provisions

To limit the potential unauthorized use of a patient list, a dental practice owner should limit employee access to that patient list. Furthermore, the owner should mandate that employees with access to a patient list sign a carefully drafted confidentiality agreement relating to the information contained in the patient list.

But, if information is known to an employee, such as a patient's name, it may not be considered a trade secret or otherwise treated as confidential. In this instance, an employee could potentially contact that patient to solicit business away from the Practice. To prevent this scenario of patient theft, a Practice owner should limit their employee's ability to solicit the Practice's patients by including a non-solicitation provision in employment agreements. A carefully drafted non-solicitation provision can prohibit employees from inducing a patient to discontinue his relationship with the dental practice for a specified and reasonable period of time during and after their employment. The effect of these non-solicitations provisions is to prevent a current or former employee from contacting your Practice's patients to induce them to leave the Practice. With a non-solicitation provision in place, the Practice is able to deter any solicitations and is granted a legal claim against former employees if they violate their agreed duties not to solicit the dental practice's patient. Although a non-solicitation provision is advisable, a dental practice owner should remember that Ohio State Dental Board policy indicates that patients should be timely informed of changes that could impact their dental care and the continuity of that care. Thus, if applicable, the Practice itself should provide a dental patient notice that the patient's treating dentist has left the Practice to ensure compliance with that provision.

Nardone Dental Practice Advisor

Would you like to receive our electronic email newsletter?

Sign up on our dental blog at:
www.nardonelimited.com/dental-blog

Nardone Limited
300 E. Broad Street
Suite 490
Columbus, Ohio 43215

Phone:
614-223-0123

Fax:
614-223-0115

information@nardonelimited.com

Website:
www.nardonelimited.com

Dental Blog:
http://nardonelimited.com/dental-blog

Nardone Limited
300 East Broad Street
Suite 490
Columbus, Ohio 43215