

What Can I Do to Protect the Value of My Medical Practice If Something Happens to Me?

Every year, hundreds (perhaps thousands) of California physicians die or become incapacitated, leaving their families or survivors to sort out the disposition of their medical practices. Unlike other classes of assets, medical practices have a short “shelf-life”; they will almost instantaneously become worthless if there is no physician to address the needs of the practice’s patients. Once a physician is incapacitated or deceased, time is truly of the essence to effectuate a transfer of the practice to another physician.

Employing a revocable living trust as part of a structure to hold an ownership interest in a medical practice offers significant protection for physicians and their heirs. Revocable living trusts are used in most estate plans to avoid probate and potentially achieve certain tax advantages. This result is accomplished only if assets, including a physician’s interest in his or her medical practice, are transferred to a revocable living trust during the physician’s lifetime.

The legal basis upon which a physician may transfer an interest in a medical practice to a revocable living trust is a 1979 legal opinion from the California Attorney General. The Attorney General, in an opinion regarding the transfer of an interest in another type of professional corporation, specifically a public accountancy firm, sanctioned the ability to transfer a stock interest in a professional corporation to a revocable living trust under certain circumstances. Office of the Attorney General, State of California, 79-5, Feb. 16, 1979 (hereinafter “Legal Opinion 79-5”)

This issue of the transfer of an interest in a professional corporation into a revocable living trust — from an accountancy firm perspective — was further analyzed in an August, 2001 article in California CPA (“Passing the Baton – Succession Planning,” Andrew Katzenstein & David Schwartz) (hereinafter “Katzenstein & Schwartz”)

In pertinent part, Katzenstein & Schwartz argue that Legal Opinion 79-5 provides the mechanism whereby an interest in a professional corporation can be transferred in a revocable living trust. They put forth that to maintain its professional corporation status, both the trustees and beneficiaries of the trust must be licensed individuals. Thus, when spouses jointly enter into a trust agreement and only one spouse is licensed, the trust instrument must specifically provide that the licensee spouse has exclusive control of the interest in the practice. However, importantly, the non-licensed spouse may nonetheless retain equitable title in the proceeds of the medical corporation.

Another step that is integral to the integrity and survival of the medical practice in those moments following the incapacitation or demise of the physician is the appointment of a trusted advisor in the role of successor trustee. The trust should provide for the sale of assets and should name as successor trustee a trusted adviser who is capable of having the assets quickly valued and sold with the least disruption to the medical practice.

In our law practice, we have seen a number of end-of-life situations in which physicians have held their ownership interest in a revocable living trust, as well as the unfortunate circumstance where physicians have not set up such a structure. Without question, those medical practices, as well as the physician’s heirs, have fared much better following the demise of the owning physician wherein the physician appropriately held his or her interest in the medical practice in a revocable living trust.

Failing to maintain the ownership interest in a trust and relying upon the slow moving process of probate will at a minimum significantly impact the value of the practice, and in fact might result in the end of the practice in total.

Physicians must give careful thought to how their medical practice will pass at their incapacity or death. Careful planning by a trusted advisor who has an understanding of both trust and estate issues as well as the specific legal issues surrounding a medical practice makes it possible for a physician to provide for his or her heirs, maximize the medical practice’s value and avoid the dreaded pitfalls of probate.



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