MATT DICKSTEIN

Business Attorney

Making legal matters easy and economical for your business

39488 Stevenson Place, Suite 100, Fremont, CA 94539
510-796-9144. mattdickstein@hotmail.com mattdickstein.com

Newsletter, June 2014
Corporate Structure – Levels of Legal Control over a Practice

When the partners in a health care practice argue, usually it comes from one of these problem areas: control, compensation, exit. Today I'll talk about control.

Levels of Legal Control. In brief, a corporation (or partnership) has the following levels of legal control:

	Corporation	Partnership
Level 1	Shareholders – they have baseline control, because they elect the directors	Partners – they have baseline control, because they elect the managing committee
Level 2	Directors – they make high-level decisions and control the executive officers	Managing Committee – makes high-level decisions and controls managing partner
Level 3	Executive Officers – have basic operational control, and direct the rank-and-file employees	Managing Partner – has basic operational control, and directs the rank-and-file employees
Level 4	The employees run the practice day-to-day	

Level #1: Shareholders / Partners. The shareholders elect the directors. The shareholders should meet at least once a year to do so. By controlling the composition of the board of directors, the shareholders can control the corporation. In most other respects, however, the shareholders (in their capacity as shareholders) have no control over the corporation (with exception for a handful of required votes on dissolution and the like).

- In a partnership, the partners are akin to the shareholders. The partners as a group elect the managing committee.

Level #2: Board of Directors / Managing Committee. The board of directors controls over matters of general operating policy. These include, for example, the hiring and firing of officers, setting compensation, declaring bonuses, issuing stock, corporate borrowing and other big decisions. The board should not micro-manage the practice. Directors set the corporation's policies, and they should leave to the officers the implementation of those policies.

- A partnership might have a managing committee, which is akin to a board of directors.

Level #3: Officers / Managing Partner. The officers run the business. In CA, the corporation must have at least the following officers: president/CEO, corporate secretary and treasurer/CFO. One person can serve simultaneously in all 3 positions. The officers oversee the rest of the company's employees.

- A partnership might have a managing partner, who is akin to the CEO, CFO and corporate secretary all rolled into one.

Level #4: Employees. The rank-and-file employees do the day-to-day work. Practice administrators usually are at this level.

CEO / Managing Partner. Many practices have a managing partner, who is akin to the CEO, CFO and corporate secretary all rolled into one. In many practices, the doctors don't want to be bothered with management. Instead they prefer to focus on their individual practices. If that's the case, the practice should provide special compensation to the managing partner, otherwise no one will do the job. It's no fun managing other doctors.

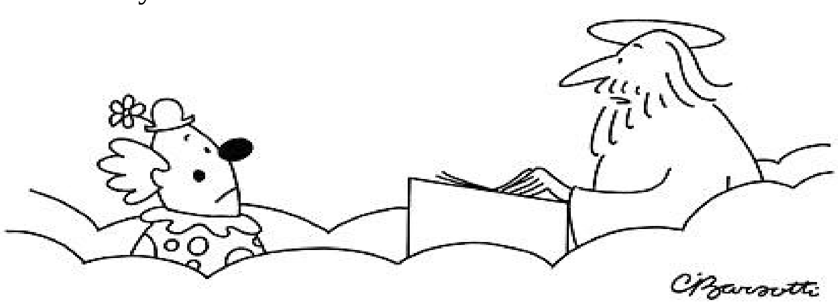
Power. If no one wants to be bothered with management, the managing partner by default has great power. Sometimes the other doctors don't pay attention to management. Over time, management can carve out little fiefdoms for itself. For example, a managing partner can be the sole signer on bank accounts, the sole contact for accountants, bookkeepers and lawyers, the sole person to whom employees report, and more. If the managing partner leaves for any reason, or if the practice develops a split between warring factions, it will take time and effort for the other partners to pick up the pieces and keep the practice running.

We all know the quote "power corrupts; absolute power corrupts absolutely." I think it more accurate to say that power deludes. It's good to put boundaries around the exercise of power, to keep it realistic, transparent, and within the bounds of common sense.

The board or managing committee should actively and regularly examine the management of the practice. The CEO / managing partner should regularly report to the board or other shareholders or partners, including the delivery of quarterly financial statements. Oversight is the best way to keep things under control.

In some practices, the doctors might choose to have the corporate documents set forth in detail the limits on the powers and duties of the CEO / managing partner. For example, the CEO might have the unilateral right to incur expenses only up to $5,000, or enter into contracts with a maximum term of 1 year. To exceed those limits, the CEO would need the approval of the board of directors. In many cases, it's good to rotate the position of CEO every couple of years.

Call me if you need to talk more.



"Well, that was a birthday party the kids won't soon forget."