

Dual Representation Brokers & Conflicts of Interest in Dental Practice Sales

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What is a Dual Representation Broker? A dual representation broker is a broker that represents both the Buyer and Seller in the sale transaction - accompanied by the claim that the broker will look out for the interests of both parties to the transaction. This claim is not entirely accurate or complete. In fact, there are quite a few areas where a dual representation broker has the incentive, conscious or not, to support one party against the other, creating a real (if not legal) conflict of interest.



Commission Based Payment as Conflict of Interest. The source of this conflict stems from the fact that the broker is paid on a commission basis - based on a percentage of the final sale price but only if the sale is completed. This gives the broker an incentive to close each sale, whether or not in the particular case the sale price, structure, and/or timing is in the best interest of either party. While this incentive system exists for any commission based payment, whether or not with dual representation, the claimed benefits of dual representation not only obscure this fact, but also hides a much broader set of conflict of interest problems that need to be recognized.

Problems Related to Conflict of Interest. This is not to say that I believe dual representation brokers generally are acting unethically. On the contrary, I believe the vast majority of dual representation brokers do not intend to mislead anyone. However, I also believe that the brokers are generally unaware that their dual representation business model contains so many substantial risks, preventing the broker from fully disclosing those risks to the clients. Therefore, Buyers and Sellers need to be alert to these possible problems when using a dual representation broker:

1. Broker May Discourage Use of Outside Professionals. One of the supposed benefits of a dual representation broker is the implication (or outright claim) that no attorneys or practice consultants are necessary - that the broker is looking out for the interests of both parties, and therefore the additional cost and time of further professional involvement is unnecessary. I find such an outright claim to be misleading, unethical and possibly illegal (as the unauthorized practice of law when a contract is provided).

A. Professionals Impede Sale? Unfortunately, many brokers see outside professionals (attorneys, CPAs and dental consultants) as impediments to closing a sale, and in one sense they are correct: such professionals educate the client, propose appropriate changes to the contracts or the transition specifics that the other party may not like, and discover previously unknown problems in the transaction that need to be addressed before closing. All these functions can delay or even end the transition, but once crucial facts and issues are brought to light they must be properly addressed. Without examination and discussion, unexpected discoveries or problems after closing can lead to lost Buyer income, Seller refunds, or full blown lawsuits.

B. Why Recommend That Professional? Realizing that outside professional help is necessary, brokers frequently recommend the use of specific professionals to help with a sale transaction. Sellers may need an attorney, and Buyers may need a lender, attorney, CPA and/or consultant. While broker referrals can be helpful in choosing a professional, conflicts of interest may impact the broker's choice of referrals. For example, brokers may receive a commission from lenders for referring Buyers; that commission can increase the overall cost of the loan and make the purchase less affordable to the Buyer. Also, brokers prefer professionals that make the sale run quickly and smoothly - and sometimes the referred attorney provides inexpensive but superficial services. However, the client probably wants a professional that is extremely knowledgeable and will thoroughly review the entire transaction, and who may provide insights that could prevent the sale from closing as quickly or at all. It's hard to know which is which without the client personally investigating the attorney's credentials, experience, approach and other outside recommendations.

2. Broker May Encourage Use of Substandard Broker Contracts. Brokers frequently try to add value to their services (and quietly discourage the use of attorneys) by providing their own version of a practice sale contract. Unfortunately, few brokers are also experienced practice transition attorneys, and these non-attorney brokers simply do not have the training or experience necessary to draft a legally complete and clearly worded practice sale contract.

A. Standard Form Contract? The broker may claim that their "standard form contract" is a starting point for the parties' own attorneys. When a party uses an attorney not familiar with practice sales, this claim is true. However, an inexperienced attorney is likely to accept at face value the dental-specific contract provisions of the contract, leaving the client with a false sense of security that the client's interests are protected. There is *no such thing* as a "standard form contract," only a contract that benefits the person who wrote it. Therefore, even though a broker may truthfully claim that the contract has been reviewed previously by many outside attorneys, the specific contract being presented has not been reviewed by *this* client's attorney, and without that outside review and revision by someone with knowledge of the specific transaction circumstances, that contract will not protect the client properly.

B. Loss of Seller's Negotiating Position. If the Seller's attorney has not reviewed and revised the document *before* the Buyer gets the document, that attorney has no opportunity to eliminate or modify contract provisions that hurt the Seller. Most broker contracts are Buyer-oriented, because (1) most Sellers assume they are adequately protected by their broker and won't hire an attorney to have the broker's contract reviewed, and (2) the broker would prefer the Buyer or its attorney to not ask for changes that could delay or prevent the sale from closing. It is near impossible to remove or change contract provisions that impose inappropriate risk and/or cost on the Seller if that contract has already been reviewed by the Buyer.

3. Broker May Not Keep Confidences. Anyone who represents both sides of a transaction is not allowed to keep the parties' secrets from one another - full disclosure is required. This may lead the broker to disclose information that was thought to be given in confidence. While I believe it is (legally) important to fully disclose any problem areas the transaction may have, nobody can be open with a dual representation broker concerning "deal point" issues. Sellers

and Buyers lose all their negotiating power, since the broker can drive the agreement to the lowest common denominator in order to make the sale.

4. Broker May Negotiate Against One Party on Price. The lack of confidentiality is particularly harmful when it comes to pricing the practice fairly - one of the three main functions a broker provides (the other two are finding a Buyer for the practice and helping the Seller collect the documents and information required by the Buyer's lender). The broker's incentive will find the subjective middle ground between what the Seller can tolerate and the Buyer is able to pay - and that middle ground is not necessarily an objective one. If a party discloses their "best price" to the broker, that information easily can be used against that party to bring the purchase price up or down to that number.

5. Broker May Require the Buyer to Pay a Commission. Since the dual representation broker claims to provide services to the Buyer, the broker may ask the Buyer to pay its own sale commission. The broker is legally required to disclose this arrangement to the Seller before the listing agreement is signed (and it should be disclosed IN the listing agreement).

A. Seller Loses Potential Buyers. Charging the Buyer ends up discouraging many Buyers from even considering the Seller's practice, which limits the likelihood of finding an appropriate Buyer. Sellers hardly ever realize this detrimental effect, and if this effect was fully explained many Sellers would not consider using that broker at all. I strongly discourage Sellers against listing their practices with brokers who charge the Buyer an additional sale commission.

B. Buyer Receives Little Benefit. I don't see any significant value provided by dual representation brokers that justify the Buyer paying a sale commission. There are many independent fee-for-service dental transition professionals available (attorneys, CPAs and consultants) that will serve the Buyer's transition needs far more competently and without a conflict of interest, and also can refer the Buyer to available lenders and other professionals. The only "benefit" I see is the apparent cost savings available by not hiring outside professionals to protect the Buyer's interests, but I believe this supposed benefit is a false economy. I strongly discourage Buyers against agreeing to pay any broker an additional sale commission.

6. Broker May Encourage Completion of a Poorly Structured Sale. Even if the particular practice sale doesn't make sense from the Seller's or Buyer's point of view, the broker may still try to force the sale to close to receive the commission. Fee-for-service professionals generally don't have this incentive; instead, their goal is to give the client the best advise possible, and that advise may be that this particular transaction should not proceed as currently structured, for any number of reasons.

Conclusion. Brokers are very good at what they are supposed to do for Sellers - practice valuations, educating the Seller on the sale and transition process, marketing the practice to potential Buyers, and coordinating all the moving parts of the sale through closing. However, once a broker steps outside these specific roles into dual representation, I believe that the broker is doing a disservice to its Seller by dividing its loyalties, and to both Buyer and Seller by discouraging proper contract drafting and review, limiting deeper outside inquiry, and interfering with confidentiality in negotiations. Buyers and Sellers would both benefit by considering these issues before working with a dual representation broker.