

DENTAL LEGAL UPDATE

Your Dental Office Lease – Watch the Terms

by Jeanine Lehman and Jan Gillia

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Special points of interest:

- Rent often consists of base rental and pass-throughs.
- Determine utilities, services and maintenance and who pays for them.
- Specify signage.
- Check parking.
- Investigate Landlord's track record.

Your dental office lease is one of the single most important contracts you sign when establishing, moving, or expanding your practice. Many dentists are exposed to great risk and expense when they sign the "standard lease form." In leasing, there is no such thing as a standard lease, and dentists should negotiate leases to meet their needs. All the terms of the lease should be in writing.

The office space glut in some metropolitan areas has produced a tenant's market, resulting in dental practices and other businesses moving up to higher grade space and paying lower rents than in boom times. You should watch the overall lease terms and not just the base rental you pay. Since the lease is akin to a marriage between the tenant and landlord, the time for negotiation and discussion between them is before the lease is signed.

Tenant: If your practice is operated through an entity, such as a Texas professional association, professional corporation, professional limited liability company, or partnership, the entity should be the tenant on the lease, not you.

Rent: For dental office leases, rent often consists of both the base rental and certain pass throughs, such as utilities, common area maintenance, repairs, insurance and taxes. The lease may have a rent escalation clause, for example, tied to the Consumer Price Index. You should evaluate the lease on the combination of all of the elements of the rent including anticipated increases. The pass-through expenses and their method of allocation should be carefully defined. You should request the right to audit the expenses. You should not sign a lease to pay a

percentage of your "sales" to your landlord, as this could put you at odds with "fee-splitting" prohibitions.

Services: Before signing the lease, you should determine what utilities, services and maintenance are provided. These include, but are not limited to:

- Electricity
- Gas, Water, Sewage
- Maintenance
- Garbage Removal
- Security
- Utilities and Maintenance for Common Areas
- Elevators, Lavatories, Parking Lots, and Garages
- Phone service to the building and your office
- Repairs
- Snow and ice removal

After hours use of utilities is essential for many dentists and should be addressed in the lease. Seeing your patient on a summer Saturday without air conditioning is possible, unless provision is made in the lease at the outset for after hours utilities. Having after hours access to the building and elevators is also critical.

Shared heating and cooling systems can result in cigarette smoke and other fumes being pumped into your office much to the distress of patients and staff. Therefore, if HVAC systems are shared with other offices, you should be certain that you will share air with non-smoking, nonpolluting offices.

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Your Dental Office Lease (cont.) --

**MAKE SURE
YOUR CURRENT
LEASE DOES
NOT EXPIRE
BEFORE YOU
MOVE OR RENEW
OR YOU FACE
“PENALTY”
HOLD-OVER
RENT INCREASE
AND EVICTION
RISK.**

Signage: Signage is critical to your practice because it advertises your practice location, presents an image, and is an element of cost. You should discuss with the landlord the type of signage provided and allowed, and the cost of the signage. Signage may include, but not be limited to, listing in the building directory, names on or adjoining the office suite, window signs, an exterior freestanding sign listing tenants, and signs or banners affixed to the building. The lease should carefully specify what signage is allowed; placement of, restrictions on, and size and dimensions of signage; illumination of signage for 24 hour exposure; cost of signage; deadlines for placement; who bears the original cost and cost of modifications; ownership of the signs. You may also want to reserve the right to add additional listings or modify listings, for example, to add practice members or a corporate name on the building directory. Additionally, if drive-by business forms a significant portion of your practice, you may want to require a provision to ensure visibility and placement. For example, if tree limbs block your sign, your landlord might need to trim the limbs for visibility. Signage cost is typically paid in full at the beginning of the lease. Signage, if removable, usually has no value at another site, because of that new site's building conformity standards. Finally, particularly, for free standing signs, you will want to check that the sign conforms with the city sign ordinance.

Parking: Your lease should specify the location and cost of parking and if possible, the lighting. Additionally, adequate parking spaces should be provided. If available at the building, covered and reserved parking should be addressed in your lease. Other questions to ask:

- Is there a high parking use neighboring tenant or potential tenant?
- Will other tenants have spaces reserved in front of your office?

- Will future construction reduce parking?

You will also want spaces reserved for handicapped patients close to a convenient entrance.

Your Neighbors: While more common in retail leases, in some situations, you may be able to negotiate a restriction to prevent competing or objectionable businesses from leasing in the building, and if you are a major tenant, you may be able to negotiate an approval right, within reason, for new tenants.

Alterations & Fixtures: If remodeling work will be done before your occupancy (“finish out”), the type, grade, time-frame, and inspection rights for such work should be specified in your lease, as well as who will pay for the remodeling. Wheel chair access and patient flow should be considered. Similarly, if alterations are desired, provision should be made for these. It is important to note that once property is affixed to the office, it becomes a fixture and consequently, the landlord's property. Therefore, specific provision should be made for certain fixtures to remain the dentist's property, for example, x-ray machines.

Insurance: One of the least understood and potentially most expensive clauses in a lease is the indemnification clause. A disturbing trend in leases is a shifting of almost all costs of litigation, including the landlord's damages and attorneys fees, to the tenant regardless of fault. Under these clauses, a dentist may be liable for millions of dollars of damages and attorneys fees. These clauses need to be reviewed with your attorney.

You should check that there is insurance coverage on the remodeling work and items added to the office prior to signing the lease. You and your landlord need to agree who will pay for the insurance. You

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Your Dental Office Lease (cont.) --

also should be sure that you have adequate liability coverage.

In all cases, your insurance agent should review the insurance provisions of the lease before you sign it.

Equipment Financing: Most banks and finance companies require that they have a first lien on office equipment or furnishings, to secure equipment or furnishings loans and certain working capital loans. Under Texas law, the landlord also has landlord's liens on property in the leased space. The mere presence of the landlord's lien in certain circumstances could result in you being in violation of your practice's loan agreements. Therefore, your office lease should contain a clause to subordinate the landlord's liens to liens due to these other types of financing.

Sublease or Buyout/Cure: You will want to include a right to sublease the premises or pay a lump sum settlement to "buyout" the lease and relieve you and your estate of further liability. These terms are subject to negotiation and are dependent on current market conditions. Your lease should specify how you and your landlord notify each other of problems and a method to remedy such problems.

Foreclosure: Generally, when real estate goes through foreclosure, leases are voided in the foreclosure process, and the tenant no longer has the protection of the lease and may be evicted. Further, the tenant may not be able to recoup his security deposit from his former landlord. Therefore, before signing your lease, you should investigate the financial strength and track record of your landlord. In response to the foreclosure trend which has occurred in recent years, some lenders will enter into attornment agreements whereby they agree to be bound to the lease if the lender is the new owner of the office building as a result of foreclosure or acceptance of a deed in lieu of foreclosure. In return, under these attornment agreements, the tenant agrees to also remain bound under the lease to the new owner of the building. The attornment agreement provides some protection to both the lender and the tenant, because the lender does not lose the income stream of the lease on foreclosure, and the tenant has potential continuity of use of his office. Such attornment agreements should be reviewed by your attorney.

Expansion & Renewal: If you think your practice will expand, you will want to have an option in the lease on adjacent or convenient space and parking, possibly in the form of a right of first refusal. Also, depending on market

conditions, you may desire to negotiate options to renew the lease for additional periods.

Special Situations: Your lease should comply with all state and federal regulations. Healthcare providers are subject to certain Occupational Safety and Health Administration requirements which do not apply to other businesses. Specifically, medical and hazardous materials waste disposal costs and x-ray shielding remodeling costs should be considered.

Buying/Selling Practice; Adding Partners: When buying or selling a dental practice or bringing in additional owners of the dental practice, the dental office lease terms need to be evaluated again, including liabilities under personal guarantees and for pass through expenses for prior periods. Additionally, the landlord's written consent may be required for changes in ownership or transfer of the lease. Your attorney needs to assist with these transition agreements.

Conclusion: In the dental office leasing arena, dentists should be informed consumers. There is no such thing as the "standard lease form." The lease contract is a true marriage consisting of many more terms than the base rental. Your lease should be evaluated on the basis of the aggregate of all terms, the track record of the landlord and building management, and the long term prospects and qualities of the building. You should be represented by your own attorney who is knowledgeable in commercial leasing. With the assistance of the attorneys and commercial leasing agents, a fair and workable agreement that makes sense to both the landlord and you should be reached before the "knot is tied". © 2010 Jeanine Lehman & Jan Gillia.

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Texas Law Changes

Franchise Tax – For the 2010 and 2011 tax years, business entities with \$1 million or less in total revenue do not pay the Texas franchise tax (changed from \$300,000 threshold). This change helps small businesses and is anticipated to take 40,000 off the tax rolls. After 2011, the threshold amount drops to \$600,000. Dental practice entities that benefit from this change include professional associations, professional corporations, and professional limited liability companies, which are below the revenue threshold.

Registered Agents – Effective 1/1/2010, registered agents need to

consent in writing or electronically to serve as registered agents and to continue in such capacity after the sale of a majority interest in the entity. Registered agents receive lawsuit and other notices on behalf of professional associations, professional corporations, professional limited liability companies, limited partnerships, and other entities and have a duty to provide such notices to the represented entity.

Identity Theft/Driver's License Number - Effective 1/1/2010, it is illegal to include an individual's driver's license number on a receipt or document evidencing payment for goods or

services that is given to an individual. Civil penalties can be up to \$500 per month.

Dental Assistants – Due to the shortage of dental hygienists in areas of Texas, Senate Bill 455 was passed to allow dental assistants in Texas to perform additional procedures, including coronal polishing and certain interim treatments of a minor emergency dental condition. For details on this new law including the requirements and certification for dental assistants to perform such procedures, see: <http://www.capitol.state.tx.us/tlodocs/81R/billtext/doc/SB00455F.doc>

About Our Firm ...

Law Offices of Jeanine Lehman P.C. is a Texas law firm headquartered in Austin with a state-wide health law practice. Our health law practice is focused on business law, transactional aspects of individual and group practices, such as contracts and incorporations, office/facility leases, building purchases/condos, and build-to-suits, practice sales/purchases/buy-ins, employment agreements, financing, and consultation concerning the day-to-day legal concerns of running a health care practice. The firm is owned by Texas Attorney **Jeanine Lehman**. Jeanine has over 25 years experience as an attorney. She has had one book and over 70 articles published. She speaks to professional and business groups concerning legal topics. Jeanine is blessed to have one dentist and three dental hygienists in her family. Contact us at (512) 918-3435, jeanine@jeanine.com or PO Box 202211, Austin, TX 78720, and visit our website at www.jeanine.com.