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Dental Newsbrief

Legal due diligence in dental practice sales and purchases: Why do we bother with it?

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Welcome

Welcome to the latest edition of Hempsons' Dental Newsbrief, a round-up of some of the hot legal topics in the dental sector.

In our first article, Kirsty Odell and Sana Sadiq explain why due diligence is required when a buyer is planning on purchasing a practice. The market for buying and selling practices is very active at present and due diligence is a pivotal part of the process which cannot be taken lightly.

With the spotlight once again on the self-employed status of dentists, Faisal Dhalla discusses the importance of putting in place properly drafted associate agreements and looks at a recent high-profile Employment Tribunal case in this area.

There is an increasing trend in dental practices developing new websites, mobile apps and publishing regular articles and content to promote their brand and services being offered. Matt Donnelly explains all you need to know about some of the key legal issues in this area.

Alison Oliver looks at a recent case concerning whether a pilot service provided by three dentists had been validly brought within the terms of the dentists' GDS contract and therefore whether NHS England could terminate the service arrangements in the absence of default by the dentists.

Finally, David Naughten examines key considerations when taking on leasehold premises for your practice.

We hope you will find something of interest in this Newsbrief. If you want more information or to follow something up, please get in touch.

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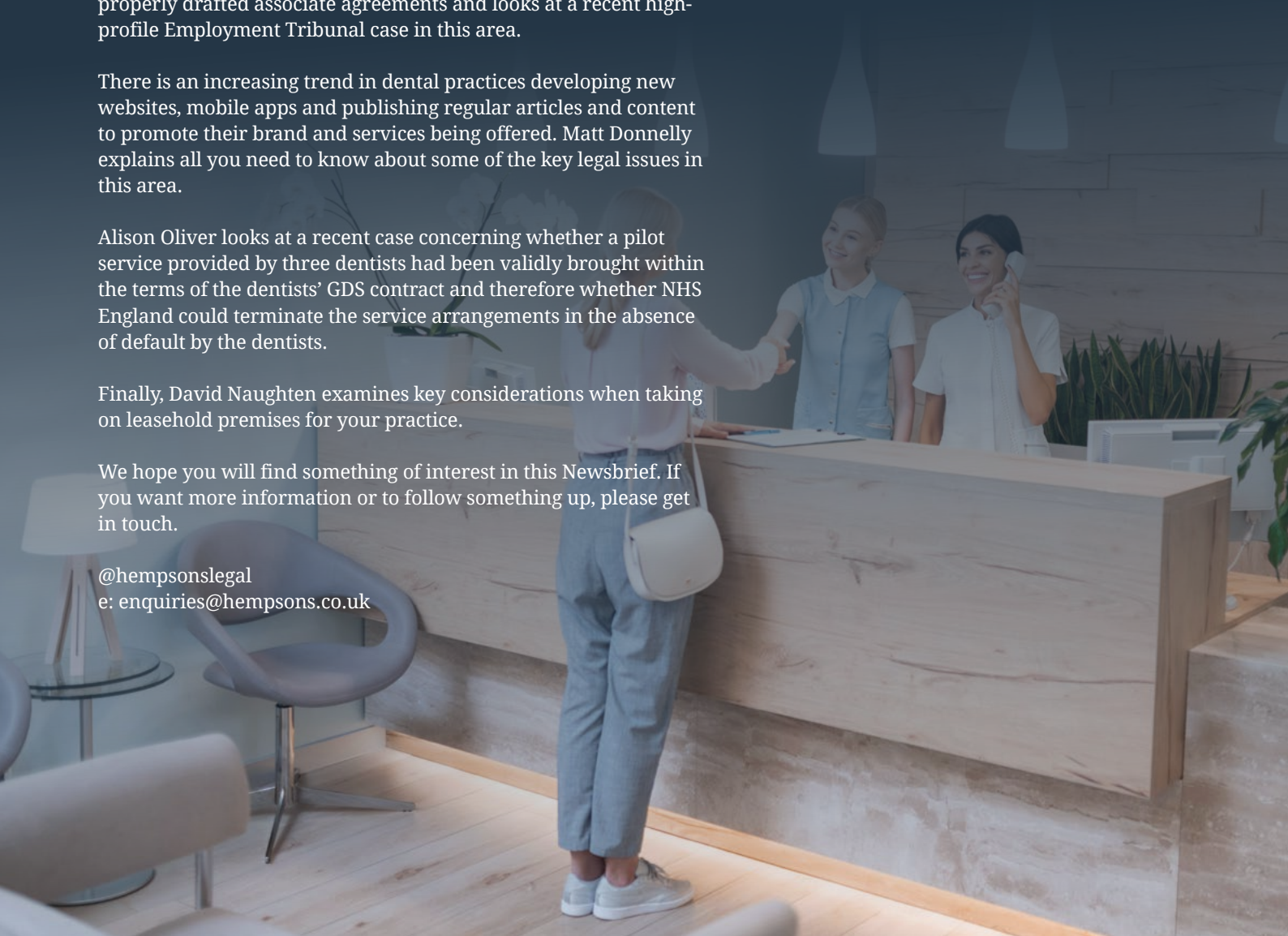

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What is due diligence and why is it required?

Due diligence is the process that a buyer will undertake to obtain information about the dental practice that it is proposing to purchase. It allows the buyer the opportunity to investigate the practice in more detail to ensure that it is a viable practice. It will also highlight any risks of the purchase and seek to draw out any skeletons that may be lurking in the closet!

The due diligence process is usually kick-started by the buyer's solicitor issuing a due diligence questionnaire to the seller's solicitor. This generally happens at the outset of the legal work – once the parties have agreed on a deal in principle – but before they sign up to the sale contract. They may have heads of terms in place and are likely to enter into a Confidentiality Agreement (aka Non-Disclosure Agreement) before beginning the due diligence process. This ensures that the buyer keeps confidential any due diligence information disclosed by the seller.

The seller and its advisers will consider the questions and provide responses to the enquiries along with supporting documentation. More often than not, a secure on-line data room is set up so that all of the information can be gathered and accessed by all relevant parties from one place. Based on the information provided, further enquiries are likely to be raised until the buyer is satisfied with the responses received, or, in a worst-case scenario, decides not to proceed with the purchase (either due to a lack of information being provided or of adverse information being disclosed).

Key areas

In terms of legal due diligence, some of the key areas a prudent buyer should cover are as follows:

- **Property** – how is the property owned/occupied, does it have planning consent to be used as a dental practice (D1 use required), is it in a good state of repair and condition? Who actually owns the premises – is it the seller of the practice or is it a third party?
- **Equipment** – an inventory will be requested as well as details of ownership of assets and maintenance of dental equipment (e.g. dental chairs, x-ray machines).
- **Insurance** – copies of all insurances (building, employer's liability, public liability). Also details of any claims made historically under the insurance.
- **Contracts** – details of all commercial contracts in place (e.g. third party supplier contracts), the liabilities thereunder and how/if they can be transferred to the buyer.
- **Regulatory information** – details of CQC inspection reports and CQC registration details.
- **Employees** – copies of contracts and confirmation of key data such as salaries, years of service and working hours.
- **Associates** – copies of contracts, details of licence fee amounts, confirmation of self-employed status.
- **Litigation** – details of any claims or complaints against the practice or employees/associates.

In addition to the above, where the practice is an NHS practice there will be a whole host of further information required in relation to the practice's NHS dental contract. This will include copies of the contract itself and any variations, vital sign reports, pay and activity statements, breach and remedial notices.

Warranties and disclosures
Warranties are statements of fact about the historical running of the practice. They are given by the seller to the buyer in the sale and purchase agreement. If it turns out that a warranty is untrue, the buyer will have a potential claim against the seller for breach of warranty (subject to any limitations of liability that the seller will have added to the sale and purchase agreement). Generally, the buyer will not be able to make a claim against the seller for a breach of warranty where the seller has disclosed against it, i.e. if the buyer is made aware of something through the due diligence process and still proceeds with the sale, it cannot then make a claim against the seller. Disclosures are made by the seller in the "disclosure letter" – a legally binding document which is essentially a side letter to the sale and purchase agreement.

Results of the due diligence exercise
The due diligence process may draw certain matters to a buyer's attention which could have an impact on how it views the commercial viability of the practice. If the due diligence process throws up adverse findings, the buyer will need to decide how it wants to deal with such findings before completion. The buyer may do one or more of the following:

- seek a reduction in the purchase price;
- request a retention – so that some of the purchase price funds are retained for an agreed period in case of certain liabilities arising post completion. These funds will either be used in the event that the liabilities arise, or if no such liabilities arise, the retention will be released to the seller at the agreed time;
- obtain relevant legal protections in the sale documentation – so that the seller is responsible to reimburse the buyer for specific liabilities if they arise post completion;
- in an extreme scenario, where the risks are too large and difficult to mitigate, the buyer may decide to withdraw from the transaction.

Conclusion
The due diligence process may seem like a daunting stage of a dental practice transaction, but it is an essential one. A seller should, so far as possible, seek to get its paperwork in order when looking to sell to try and speed up the process. The more organised and comprehensive the first set of replies are, the less likely a buyer will come back with lots of further questions. Likewise, in order to ensure that the due diligence process is not unnecessarily drawn out, the buyer should consider the number of questions it asks and the scope of those questions – i.e. is the information it is seeking important and what relevance does it have on the buyer's investigations?

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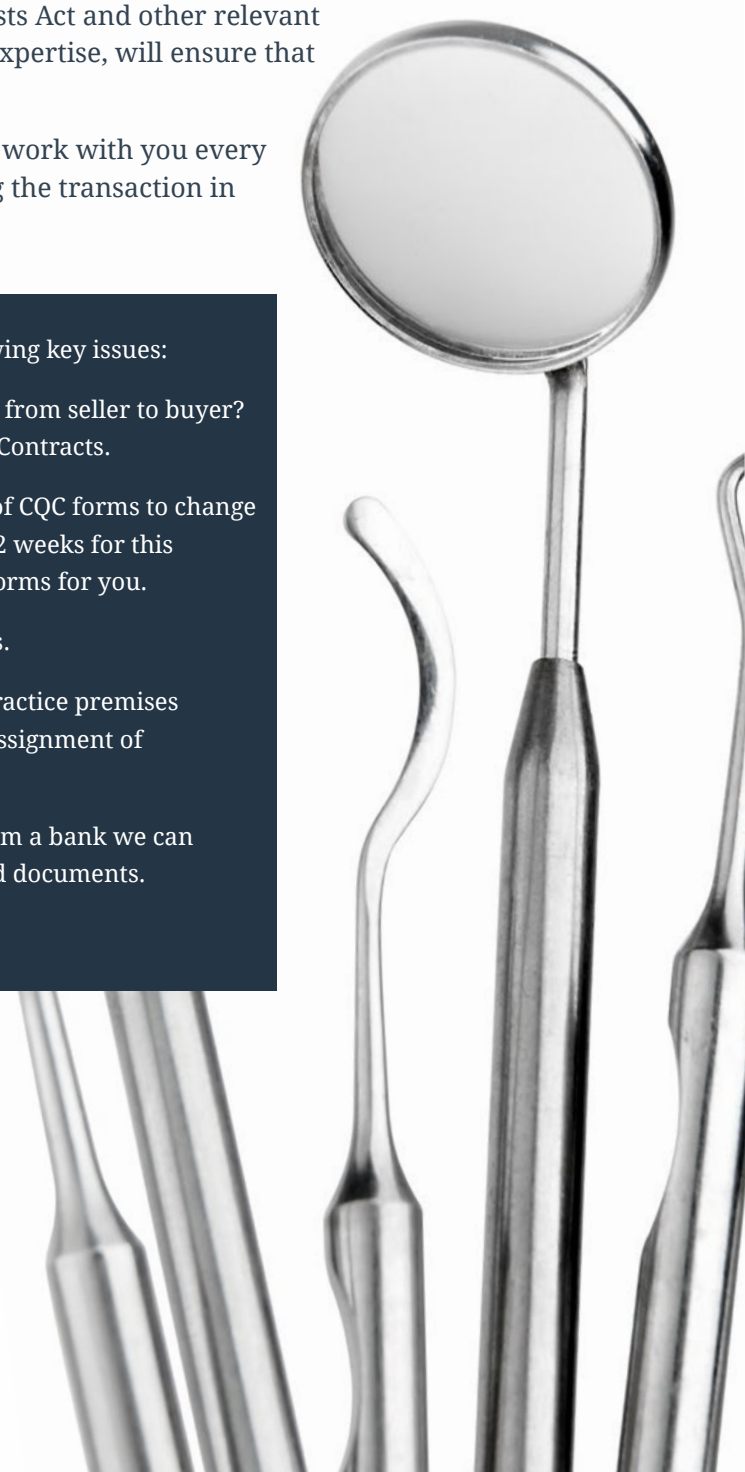
Selling or buying a **dental practice?**

Talk to us...

At Hempsons, we have a dedicated national team which provides expert advice on the sale and purchase of dental practices.

Our expertise in the GDS and PDS Regulations, the Dentists Act and other relevant healthcare legislation, together with our corporate law expertise, will ensure that your sale or purchase is structured in a robust manner.

Regardless of whether you are selling or buying, we will work with you every step of the way, protecting your interests and completing the transaction in a cost effective and timely way.



Amongst other things, we can help you to navigate the following key issues:

- **NHS contract** – how will the NHS contract be transferred from seller to buyer? This is a particularly difficult issue when it comes to PDS Contracts.
- **CQC** – both buyer and seller need to complete a number of CQC forms to change the CQC registration at the practice. It can often take 10-12 weeks for this process to complete. We can draft and submit your CQC forms for you.
- **Employees** – we can advise you on your TUPE obligations.
- **Premises** – we can advise you on the sale / purchase of practice premises as well as putting leases into place and dealing with the assignment of existing leases.
- **Bank funding** – as a buyer, if you are seeking funding from a bank we can advise you on the bank's lending and security process and documents.

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Are your dentists **really self-employed?**

There have been some high-profile cases concerning the status of self-employed individuals, with companies such as Uber and Deliveroo hitting the headlines in recent years.

The issue of the self-employed status of associate dentists is also very much a hot topic at the moment – in particular, with a review HMRC has been conducting in recent times and the Employment Tribunal case of Mr A Lynn v. Damira Dental Studios Ltd. In this case, the associate asserted that he had been employed as a dentist for a considerable number of years and alleged that he had been unfairly dismissed from his employment as a dentist despite having entered a "self-employed licence agreement" with the practice owner. The Employment Tribunal looked at the facts and applied basic legal principles to find that the claimant was not an employee.

In its decision, the Employment Tribunal considered the following significant factors as evidence of self-employment:

1. Lack of mutuality of obligation
Employment contracts contain an obligation on the employer to provide the work and a matching obligation on the employee to perform that work. However, it is important that these obligations do not exist between a practice owner and an associate, i.e. there should not be an obligation on the practice owner to offer the associate dental work on a regular basis and there should not be an obligation on the associate to perform the work. Despite this, associate agreements commonly include clauses that provide that the practice owner will introduce patients to the associate and the associate will perform a certain number of Units of Dental Activity (UDA).

2. Locum cover
Employees are required to personally perform the work that they are employed to do but associates have a right to a appoint a substitute locum to perform the work on their behalf. Even where the associate chooses not to exercise this right of substitution and engage a locum, the fact that the right exists is enough to show that the associate agreement is inconsistent with a contract of employment and it is therefore evidence of self-employment. The right to appoint a substitute locum should be unqualified. Problems may arise where any right to appoint a substitute is subject to the practice owner's approval or where locums may be used only in certain pre-determined circumstances e.g. when the associate is unwell or unable to work, rather than just unwilling or unavailable to work.

3. Clinical freedom
Employees are under the direct control and management of the practice owner, who decides what the employee does and how and when they do it. Whereas for an associate, there should be no line management. An associate should have complete clinical freedom to treat patients as they see fit. Periodic auditing of the associate to ensure compliance with relevant legislations and standards will not amount to a degree of control but compliance with practice policies, such as behaviour and dress code may be an indicator of employment.
Other factors that were considered evidence of self-employment include, the associate:

- being responsible for income tax and national insurance contributions;
- paying for professional indemnity insurance cover;
- not being paid holiday pay;
- sharing responsibility for laboratory costs;
- sharing responsibility for bad debts; and
- indemnifying the practice owner in respect of damage done by him to the practice owner's equipment.

Do your associate agreements reflect the above principles? Have you had them checked in recent times? Whilst model associate agreements are readily available and come with easy to follow guidance notes, they may need to be adapted to suit individual circumstances. It is important that legal advice is sought before adapting model agreements that are available. To avoid issues regarding self-employment status, a well drafted associate agreement should include:

- **Limited control** – the associate should be given clinical freedom, and whilst the agreement can indicate UDA targets, it should avoid placing obligations on the associate to carry out specific work and dictating how that work is performed. Complete integration, line management and compliance with practice polices (e.g. relating to behaviour and dress code) can be an indicator of employee status.
- **Use of facilities** – the practice owner will need to determine when the associate can access the dental practice and what facilities the associate is entitled to use. Providing the associate with equipment required to carry out the work could be an indicator of employee status but to get around this, the practice owner should charge the associate a licence fee for use of the equipment.
- **The financial arrangements** – the associate should not be paid a fixed amount each month and should not receive benefits from the practice, such as pensions (not including superannuation) or bonuses, or they may be at risk of being considered an employee. The associate's pay should be linked to the actual work carried out by the associate and should take into account laboratory bills.
- **Taxation** – to demonstrate self-employed status, the associate should be responsible for payment of their own income tax and national insurance contributions on their gross earnings.
- **Financial risk** – given that the associate will have clinical freedom, they too should be responsible when things go wrong and remedy defective treatment in their own time, at their own expense and should share responsibility for bad debts. The associate should also indemnify the practice owner for any damage caused under their watch to the facilities, including the equipment. This is in contrast to employees, who do not assume any such financial risks.
- **Working hours** – the agreement should give the associate flexibility in the days and hours worked. Obviously, a practice owner may wish to stipulate a minimum number of hours per week. However, a rigid approach in this area runs the risk of the associate being deemed an employee.
- **Substitution** – if the associate is unwilling or unavailable to work, they should have the right to appoint a locum to provide cover. The practice owner should exercise as little control over this exercise as possible. In other words, the associate should organise the locum cover, retain the locum's revenue and pay the locum out of that revenue.
- **Restrictive covenants** – when the associate leaves, the agreement should include restrictions on the associate's future activities to prevent the associate from competing with the interests of the practice. Restrictive covenants can be an indicator of employee status. However, it is a plausible argument that restrictive covenants are necessary to protect the goodwill of the practice.

The associate agreement itself is not enough to determine self-employed status. Once you have gone to the effort of ensuring that the associate agreement is consistent with self-employment, it is important that you ensure that the terms are followed in every day practice to avoid the courts looking beyond the associate agreement to determine whether an associate should actually be considered an employee.

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Faisal specialises in the sale and purchase of dental practices and also advises dentists on commercial matters such as 24 hour NHS retirement, associate agreements and the incorporation of dental practices.

Taking control – knowing the value of your intellectual property

We live in an increasingly digital age where innovation and new technologies are at the forefront of everything we do, with new apps, websites and content being released daily, helping practices to stay in touch with patients. There is an increasing trend in dental practices developing new websites, mobile apps and publishing regular articles and content to promote their brand and the services being offered. However, consideration is often not given to ownership of intellectual property in this content or 'IP' as it will be referred to throughout this article.

One key error that dental practices make is failing to realise where ownership of IP lies and the importance of ensuring you own, or have the rights to use, any IP that has been created for you. In recent dental practice transactions, we have seen examples where practices have commissioned new websites or mobile apps but have not obtained the correct IP rights. This can often be fundamental to a sale and the buyer of a practice will often ask for "warranties" as to ownership of your IP, which you would not be able to give without ensuring that the correct rights have been obtained.

IP is the term that is used to describe things that can be owned but are not physical in nature; examples of this would include copyright in articles written for publication, the code forming part of a website or even the design behind a logo. The owner of IP does not own something that is tangible but instead has the right to control how that intangible thing is used, hence the phrase 'intellectual property rights'.

You could have joint ownership of IP, it could belong to individuals as well as organisations and you can also sell and grant rights in IP in a similar way to a tangible object. It is important for organisations to be aware that IP is an asset, which in business can potentially carry a significant value.

It is therefore fundamental that you own or have the rights to use the IP that forms part of your website by considering where the IP comes from and who owns each aspect of it. For example, if a company built a website for you and registered a domain, a friend designed your practice logo or a consultant wrote an article for your website, then in the absence of an agreement granting rights or an employment contract, the IP in those aspects will likely automatically lie with their creator and not necessarily with you or your practice. Therefore, you will need the owner of this IP to give you rights to use the IP that they have created on your behalf.

There are two common ways in which rights can be granted in IP. Firstly, an organisation can be given permanent ownership rights through what is known as an 'IP assignment', whereby ownership of that IP is 'assigned' to you. Alternatively, where an owner of IP wishes to retain that ownership, then you can be granted the right to use the IP by way of an 'IP licence'. Licensing is common with photography and you will often see images being licensed by an owner to multiple users through websites such as Getty Images. If you are using someone else's IP that you don't have the rights to use, then the owner will be able to take legal action against you which may leave you financially exposed. In general, if someone is employed by an organisation then the law states that any IP created during the course of their employment will automatically lie with the employer, unless there is an agreement to the contrary. However, for non-employees such as locums or consultants, the IP will typically remain with that individual.

You should always carefully consider if you have the actual rights to use IP and if not, how you can go about obtaining such rights. If you have an image on your website, have you been granted the rights to display it? If a consultant has written an article for you, have they given you the rights to use this online or in print? If you are developing a website, has the web developer granted you full rights to utilise this as you wish in the future? Don't let simple mistakes like this potentially affect your practice further down the line and cause complications for you.

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Matt provides advice on a range of commercial issues with his expertise lying in intellectual property, data protection law and commercial contracting. Matt is a member of the Hempsons Digital team, helping to drive and enable new technologies and innovations for clients throughout the NHS and the wider health and social care sectors.

To terminate or not to terminate?

Key points

The Court of Appeal recently considered a case which is of interest to all NHS primary care contractors, and particularly those who provide services under pilot contracts or other temporary contracts which are ancillary to their core NHS contracts, as well as being of general interest from a contract law perspective. The case[1] related to a General Dental Services Contract ("GDS contract") but the key principles established by the case could apply just as easily to any NHS primary care contract – or, indeed, any contract for the provision of services in any field.

[1] NHS Commissioning Board (known as NHS England) v (1) Dr Manjul Vasant (t/a MK Vasant & Associates), (2) Dr Angelica Khera (t/a The Family Dental Practice) and (3) Dr Gursharan Kalsi (t/a Lancaster House Dental Practice, 16 July 2019

The case was concerned with whether a pilot service provided by three dentists ("the dentists") had been validly brought within the terms of the dentists' GDS contract and therefore whether NHS England could terminate the service arrangements in the absence of default by the dentists.

NHS England had brought the appeal following a High Court decision in favour of the dentists delivering services under the GDS contract.

The circumstances

In 2007, the dentists started to supply intermediate minor oral surgery services ("minor surgery") under an NHS pilot scheme designed to transfer minor surgery from hospital into primary care. The pilot scheme contract was for a fixed term which expired in November 2008, but the dentists continued to provide the service and the NHS (then Croydon PCT) continued to pay them. The parties to the dispute all agreed that this amounted to the terms of the pilot contract being "continued by conduct".

In 2009, the PCT and the dentists signed a GDS contract variation, the purpose of which was to add the minor surgery services as an "Advanced Mandatory Service" under the GDS contract. This was a simple, single-page contract variation containing no detail about the minor surgery services to be provided or the payment arrangements for those services (which differed from the framework for payment for other services under the GDS contract). The contract variation simply stated that the dentists were to provide "an Advanced Mandatory Service in the form of an Intermediate Minor Oral Surgery (IMOS) service".

The dentists continued to provide the services and to be paid for them as they had been prior to the contract variation for a number of years without any issues arising.

In 2016, NHS England (which was now responsible for the GDS contract following the abolition of PCTs) sought to terminate the minor surgery arrangements by notice, without default on the part of the dentists.

Relevant law
This case is concerned with the law of contract. For a legally binding contract to be formed, certain conditions have to be present:

There has to be an offer of terms and an acceptance of those terms: in the circumstances, this would have involved either the NHS offering the pilot contract terms to the dentists and the dentists accepting those terms, or the NHS inviting the dentists to tender for those terms and the dentists submitting a bid which was accepted.

There has to be "consideration" passing between the parties: this would usually be payment of money in exchange for goods or services, but payment could be in kind. In this case, the NHS paid fees in return for the services.

There has to be an intention to create legal relations: an offer and acceptance of terms between family members (for example) might not always satisfy this test whereas between arms' length commercial organisations the test is more likely to be satisfied.

There has to be certainty of terms: in order to be legally binding, the rights and obligations of the parties must be clear. The terms do not necessarily have to be in writing, and terms can be implied into a contract by law (such as the law relating to the sale of goods which implies a term into contracts that the goods supplied will be of satisfactory quality) or by the conduct of the parties. When courts are considering the terms of a contract, courts will generally only imply terms where they consider it necessary to reflect the intentions of the parties at the time the contract was formed.

The issues
In this case, it was common ground that a legally binding contract existed for the dentists to provide the minor surgery service.

The parties were not in dispute about the nature of the minor surgery service, nor about the payment terms. Terms relating to the nature of the service, arrangements for referral and triage and arrangements for payment were set out in the pilot contract or had been confirmed or varied by conduct and in subsequent correspondence between the parties. The service had been provided for some time without any argument about those terms. The dispute was over whether NHS England had a right to terminate the minor surgery service without default on the party of the dentists.

A GDS contract continues until terminated in accordance with its terms; NHS England has no general right to terminate without default by the dentists. The same applies to personal dental services agreements.

In this case, no default was cited as the reason for the termination. The dispute boiled down to whether the applicable termination provisions were those in the pilot contract or those in the GDS contract. This in turn depended on whether:

1. the GDS contract had been validly varied so that the minor surgery services were provided under the GDS contract, in which case the GDS contract termination provisions applied and the minor surgery service could not be terminated on notice; or

2. the GDS contract had not been validly varied so that the minor surgery services continued to be provided under the pilot scheme contract, in which case the termination provisions in the pilot contract applied and the minor surgery service could be terminated on notice.

Much of the legal argument focused around two main provisions in the GDS contract:

- an "entire agreement" clause which provides that the GDS contract constitutes the entire agreement between the parties in respect to its subject matter and that it supersedes any prior agreements; and
- a "written variation" clause which provides that any variation to the GDS contract must be in writing and signed by the parties.

The arguments and discussion

NHS England argued that the written variation to the GDS contract contained insufficient detail about the nature of the minor surgery service and the payment arrangements to be legally binding and that the entire agreement clause and the requirement for GDS contract variations to be in writing and signed by the parties prevented clarification of the terms by reference to the pilot contract and subsequent conduct and correspondence of the parties. NHS England's conclusion was that the minor surgery service was not provided under the GDS contract and could therefore be terminated on notice. Rather, in the absence of a legally binding variation to the GDS contract, it followed (argued NHS England) that the minor surgery services continued to be supplied on the terms of the pilot contract, which could be terminated by notice without cause.

The dentists argued that, as the entire agreement clause was "subject to" the written variation clause, there was nothing to prevent reference to the terms of the pilot contract to clarify the terms of the GDS contract variation. The appeal judge (Lord Justice Lewison) rejected this argument. He said that once the GDS contract was varied, the entire agreement clause continued to apply to the GDS contract as varied. The varied GDS contract consisted of the GDS contract plus the written variation signed by the parties; it was not possible to incorporate some or all

the provisions of the pilot contract into the GDS contract in the absence of this being specifically recorded in a written variation. He further noted that the dentists would not want all the pilot terms incorporated in any event as this would mean incorporating the provisions enabling termination on notice: this raised a further problem of determining which of the pilot contract provisions should be incorporated, if such incorporation was permitted at all.

The dentists also argued that the words used in the written contract variation to describe the minor surgery service had a meaning which was well-known to the parties and that the variation was therefore sufficiently clear to be legally binding. This argument succeeded. The appeal judge pointed out that "extrinsic evidence is admissible to explain the meaning of unconventional expressions in a contract, especially where the expression in question is used in a particular sector of economic activity".

The written variation said that the dentists were to provide "an Intermediate Minor Oral Surgery (IMOS) service" and the key question to answer was therefore "what do those words mean?". The appeal judge did not consider that it was possible to give meaning to that phrase without extrinsic evidence. This extrinsic evidence was (in the appeal judge's words) "close at hand" in specific provisions of the pilot contract that described the service but did not incorporate the termination provisions of the pilot contract.

One of NHS England's arguments was that the payment arrangements for the minor surgery service were not sufficiently clear and that existing payment arrangements could not be incorporated into the GDS contract without a written variation signed by the parties. However, the appeal judge was of the view that the provisions describing the service in the pilot contract which were admissible as extrinsic evidence also stated that the PCT and the dentists would negotiate fees for the services. He considered that the entire agreement clause did not preclude the implication of a term that is intrinsic to the agreement and noted that "in the case of a continuing contract for services in the course of performance the court will readily imply a term that a fair price will be paid for the services rendered". Additionally, legislation[2] implies such a term into a contract where not expressly excluded in the contract (which it was not in this case). He was therefore of the view that the agreement of a price by negotiation as contemplated by the provisions of the pilot contract which were admissible as extrinsic evidence to interpret the meaning of "an Intermediate Minor Oral Surgery (IMOS) service" did not constitute a variation of the GDS contract requiring a written variation signed by the parties. The pilot contract and subsequent negotiations and conduct of the parties in relation to the payment arrangements were therefore sufficient to clarify the payment terms for the service.

The judgment

NHS England's appeal was dismissed. Admissible extrinsic evidence and implied terms clarified the meaning of the words "an Intermediate Minor Oral Surgery (IMOS) service" (used in the written variation to the GDS contract) sufficiently for the variation to be valid without incorporating the termination provisions from the pilot contract. NHS England was therefore unable to terminate the service on notice without cause.

[2] Section 15 of the Supply of Goods and Services Act 1982.

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Alison is a partner in the corporate team focusing mainly on the GP and dental sectors. She helps dentists and dental bodies corporate buy and sell practices, advises on partnership and expense sharing arrangements and dental associate contracts and assists with dental practice incorporations. She also has an in-depth understanding of the NHS dental contract regulations.

Securing the right lease for your dental practice:

key considerations when taking on leasehold premises

The premises out of which a dental practice is run are one of the most important elements of a dental practice sale/purchase. It is important that time and care is taken to ensure that the terms on which the practice occupies the premises are appropriate for the continued requirements of the business.

There are three common scenarios that exist in the acquisition of a dental practice:

- the seller owns the freehold of the premises and grants a lease to the buyer;
- the seller has an existing lease of the premises and assigns its interest to the buyer;
- the buyer takes a new lease from a third-party landlord.

All the above scenarios provide opportunity for negotiation of the lease terms and it is important that a buyer considers carefully whether the terms are appropriate for its plans for the business, and also ensures that it is not opening itself up to undesired liabilities and/or obligations in respect of the premises.
We set out below some of the main terms of a lease and what a buyer needs to consider before it commits to taking on or entering into a lease arrangement.

Term length
A buyer will want to ensure that it can occupy the premises for a considerable period. Ordinarily, a lease term of at least 15 years is sought on a purchase of a dental practice.

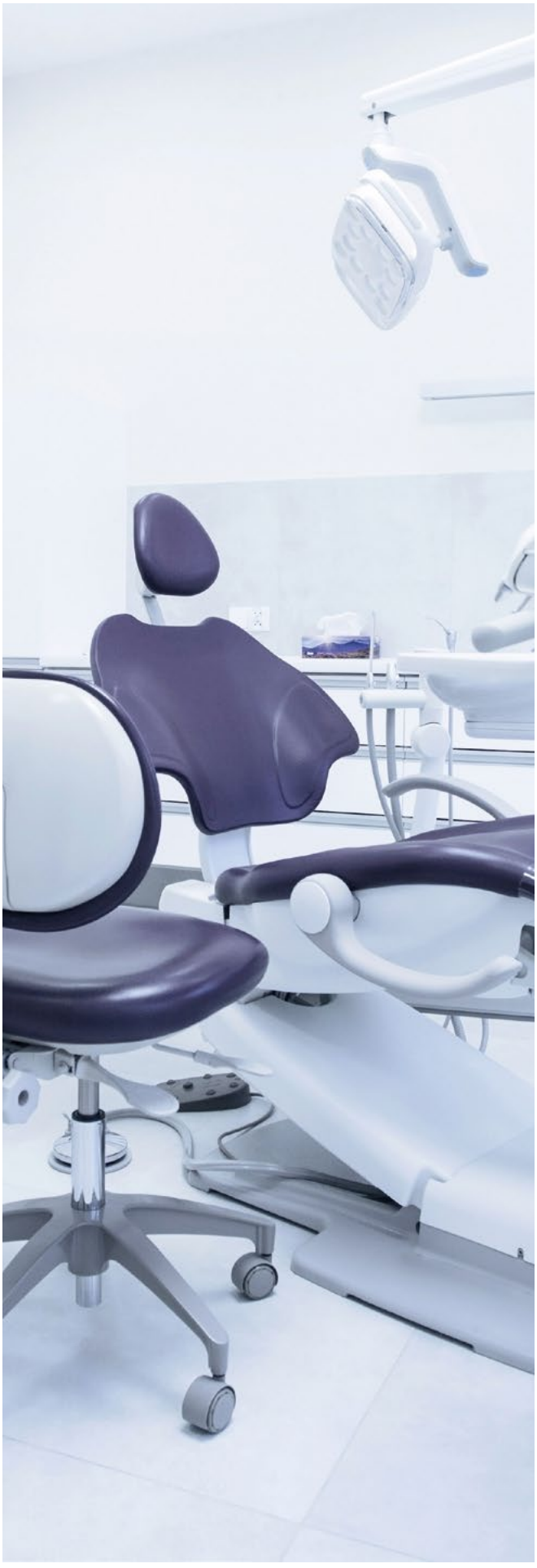
Consideration needs to be given to the funding arrangements of the buyer. The "starting position" for an institutional high street lender is often that they require the lease to be in excess of 15 years, however, there is normally flexibility where dealing with dental practices (where the value sits within the business itself). Where there is a lender involved, a buyer should look to engage with the lender early in the process, to ensure that the lease arrangements meet its requirements.

Break rights
Whilst ensuring that the term of a lease is adequate for a buyer's business plans, equally, a buyer may wish to look at ensuring that it has the flexibility to relocate in the future (whether that may be in a situation where more attractive premises become available, or to mitigate against future rent increases) or to protect against unforeseen circumstances.

Conversely, a lease may include break rights in favour of a landlord, to allow the landlord to take back the premises. Break rights can take the form of specific dates e.g. the 5th and 10th anniversaries or arise as a result of a trigger event, e.g. the tenant's NHS contract being terminated.

When dealing with a new lease arrangement, break rights are very much a commercial negotiation between the parties. The buyer's desire for break rights to ensure flexibility in the longer term may come at a price, typically, in the form of paying a higher headline rent.
Incorporating break rights into an existing lease is rarer, as it does not make commercial sense for a landlord to accept such a concession unless they are being offered something in return (again, an increase in the passing rent being the obvious incentive that a buyer can offer, or a premium being payable if the break right is actually exercised in the future).

It is always prudent to ensure that the terms of a break right are reviewed by the buyer's solicitors. There are many instances where break rights have been incapable of being exercised by a tenant due to the way that they have been drafted (and the preconditions to be satisfied before the break can be exercised).



Rent and rent reviews
The headline rent payable under a lease will be readily apparent to a buyer on undertaking its due diligence and taken into consideration in reaching a proposed purchase price for the dental practice. A buyer should agree at the outset with a landlord, the basis of any rent reviews during the term of the lease, together with the frequency of the reviews. Where the buyer is taking over an existing lease, it should ensure that its solicitors have reviewed the rent review provisions of the lease to check that there are no unexpected "surprises".

Most leases will include rent reviews that are either carried out on an upwards only open market basis or are index linked to the Retail Prices Index.

Both methods of review have their advantages for a buyer. An open market rent review will likely lead to low or minimal rent increases in a market where rental values are depressed (i.e. during an economic downturn), whilst an RPI review can provide a buyer with some level of assurance as to the likely level of rent increases throughout the term (additional security can be obtained by "capping" the potential percentage increase from one review to another).

Conversely, where the demand for commercial premises increases and/or availability of premises is limited, an open market rent review can lead to more dramatic rental uplifts. A buyer also needs to take care to check that the initial rent is not artificially inflated e.g. to reflect works the tenant has undertaken, as that could lead to an unexpected uplift when the rent is next reviewed. The main disadvantage of an RPI rent review is that the index is unlikely to decrease and therefore the rent is always going to go up over the term, irrespective of the wider state of the commercial property market.

Repairing obligations
The single greatest cost or liability to a tenant under a lease (excluding the rent) is the cost of complying with the repairing obligations under the lease, including any obligations placed on a tenant at the end of the term. Where a lease includes a "full repairing obligation" on the tenant, the tenant will be in a position where it must attend to all wants of repair, regardless of whether they were pre-existing when the lease was granted.

A buyer should always ensure that it carries out a survey to identify any items of disrepair; even if the buyer will not be under a direct obligation to the landlord to deal with such items; it could be that they have a fundamental impact on the operation of the business, e.g. a serious leak in the roof.

Where a buyer is entering into a new lease and there are items of disrepair, the buyer would be prudent to look to agree with the landlord that either i) the landlord carries out repairs before the buyer becomes responsible for the premises or ii) the buyer's repairing obligations are limited by reference to a "schedule of condition" (which normally takes the form of a series of photographs

evidencing the existing disrepair, with the tenant having no obligation to attend to such items either during the term or at the point at which the premises are handed back to the landlord).

Where a buyer is taking over an existing lease, it will need to ensure that it understands what its obligations will be to the landlord and the likely cost of complying with the same. In some instances, a buyer may take over a lease on the basis that the seller either carries out certain works before completion, or there is a deduction in the purchase price of the practice to reflect future outlay by the buyer to attend to the items of disrepair.

Service charge

Where premises form part of a larger building, the lease arrangements will ordinarily include a service charge arrangement with the landlord. The landlord will be under an obligation to provide certain services in return for the tenant paying a proportion of the overall costs.

The services to be provided by a landlord will depend on the nature of the building, but will typically include things such as the landlord repairing the structural and common parts of the building, ensuring that any common parts are kept clean, maintaining any shared service media etc.

A buyer should look to ensure that the services to be provided by a landlord are adequate for the continued running of the business from the premises and look to get a firm understanding of the likely service charge payable. Whilst information as to the historical service charge/service charge for the next accounting year should be readily available from the landlord, care should be taken to fully understand the terms of the lease and exactly what can be charged back to the tenant.

Service charge arrangements are one of the main areas of dispute between landlords and tenants and it is not uncommon to discover lease terms that offer little by way of “safeguards” to tenants and/or allow the landlord to recover costs that a tenant would not envisage as being recoverable.

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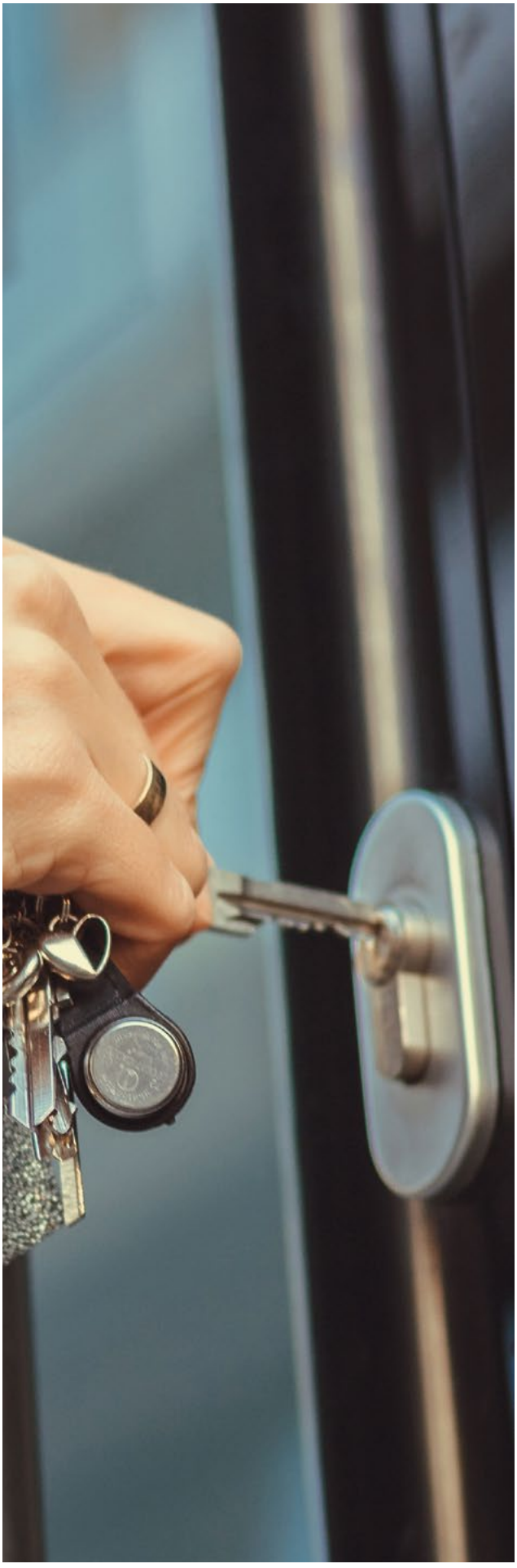
David provides advice to a variety of real estate clients, including dentists, GPs, NHS Trusts and private companies. David regularly acts on behalf of dental clients in relation to the property elements of both the sale and purchase of dental practices. He has extensive experience at negotiating sale contracts, lease arrangements and advising clients on any issues arising from due diligence.



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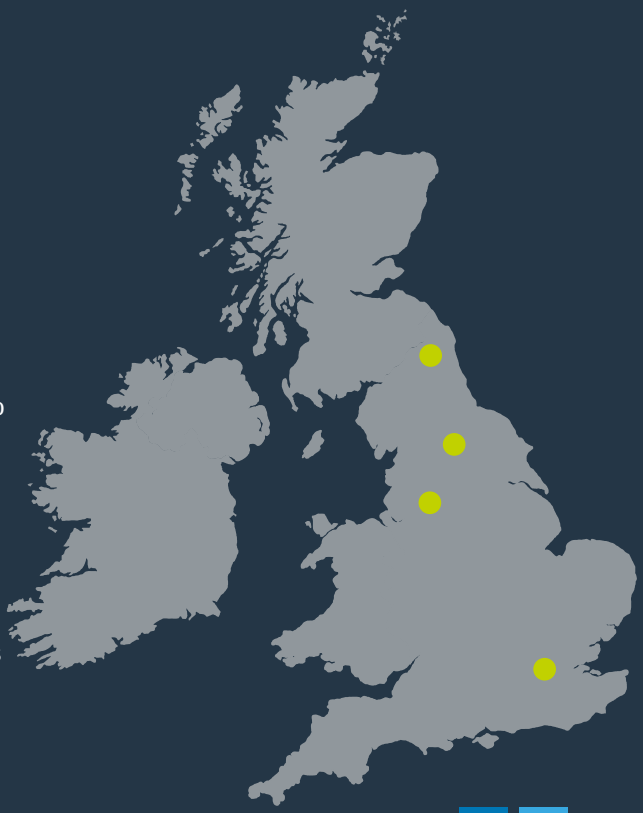

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