

Your dentistry questions answered

Practice Plan's **NIGEL JONES** looks for answers to the questions you're asking...

When buying a practice, should I take a lease or buy the freehold?

BUYING a dental practice is one of the biggest decisions you are likely to face in your career. It is not just a significant investment monetarily but also in terms of your time, effort and responsibility.

The decision of whether to become a practice owner or not brings with it several other questions, one of which is whether to take a lease or buy the freehold. It is not straightforward and can be a confusing time especially for those unfamiliar with the legalese and the process. To gain more clarity on this aspect of buying a practice, I asked specialist solicitor Thomas Coates: **When buying a practice, should I take a lease or buy the freehold?**

Thomas: 'There is no one-size-fits-all answer to this and much depends on certain key variables, in particular, the financial position of the buyer, the location of the practice and the future expansion plans for the practice. Here, I will touch upon some of the things to think about when faced with this choice.

Where a practice is for sale and the seller owns the freehold, the seller has the option to either sell the freehold to the buyer along with the business assets or the seller may choose to retain the freehold premises and instead grant a lease to the buyer.

We tend to find that a sale of the freehold is preferable to sellers as it provides a clean break from the practice and removes the sometimes-onerous

responsibility of acting as a landlord post-sale. Although, occasionally we encounter a seller who sees the income from the rent payable under the lease as a key aspect of their retirement planning and – assuming they have no ready need of the proceeds of the property sale – prefers to hang on to the freehold.

From the perspective of a buyer, there are once again benefits and disadvantages to both options. It is very often the possibility of acquiring the freehold which is most attractive to buyers (although not usually the corporate buyers who tend to prefer taking a lease), with the view that paying rent under a lease is essentially 'dead money' which could be put to better use in acquiring the bricks and mortar outright.

Whilst that is a logical and attractive conclusion, financial reality can ultimately prove a barrier to proceeding in that way. Practices in the south of England and particularly in London can often occupy premises which are worth significantly in excess of the value of the business assets of the dental practice.

Under those circumstances, a buyer wanting to acquire both business assets and freehold with the assistance of bank lending is going to find it difficult to raise the level of deposit required. This is often when we see the 'bank of mum and dad' riding to the rescue with the injection of a significant cash deposit to allow the acquisition of both freehold and goodwill/equipment.

Where finances do not stretch to the acquisition of the freehold and a lease is the chosen option, a buyer will need to be aware of the usual obligations under a commercial lease that they will be expected to sign up to, as well as the likely requirements of any bank who is financing the purchase.

If they are to support an acquisition of a practice without the freehold also being acquired, a bank would typically expect to see a lease of 10 to 15 years' duration put in place and they would structure their lending over that term. The shorter the term, the higher the repayments will be.

The lease will typically contain repairing obligations on the tenant and may also provide for service charges and insurance rent to be paid in addition to the monthly rent and the tenant will be required to maintain the premises at their own expense up to a specified standard. The rent agreed at the outset will normally be reviewed periodically on what is known as an upwards-only basis meaning that it will only ever stay the same or be increased – it will never reduce. These 'rent reviews' typically take place every three to five years during the term of a lease and adjust the rent to current market value or against some other pre-determined criteria.

Where acquisition of the freehold proves impossible at the time the practice is purchased, a buyer may wish to consider asking the seller for either a right of first refusal (sometimes called a pre-emption) or alternatively an option to purchase, in respect of the freehold.

A pre-emption basically means that if at any point in the future the seller wants to dispose of the freehold, they must offer it to the buyer (who will by that point be the tenant under the lease) who has first refusal to acquire the freehold. Criteria for valuation and timescales for completion of the purchase will all be pre-determined and set out under the pre-emption agreement.

Alternatively, an even more attractive option for a buyer with one eye on a future freehold purchase would be to negotiate an option to purchase with the seller. This differs to a pre-emption in that it confers on the buyer the right that the freehold is sold to them at some point in the future, usually within a specific time period or subject to a trigger event. It can be drafted however the buyer and the seller agree and would provide for a mutually agreed point in time where it can be exercised by the buyer/tenant and at what price the seller must sell it to them.

Whilst freehold ownership is without question the more attractive proposition to the majority of buyers, where financial limitations make it an impossibility at the time of purchase, a pre-emption or an

option to purchase should be explored. This ensures that acquisition of the freehold remains something that can be achieved further down the line once the initial expense of purchasing the business has passed.'

Thanks to Thomas for that thorough explanation of the options when it comes to considering buying a practice freehold or taking a lease. As is so often the case, your decision will be influenced by your personal circumstances, your future plans and your financial situation, but it was enlightening to hear from Thomas about the paths available to buyers, particularly when it comes to taking a lease but with clauses to obtain the freehold at a later date.

These days, practice ownership is not necessarily the traditional career path – with BDA research showing that only 16 per cent of young dentists estimate they'll be owning a practice in the next five years – but for those considering it, this has been a full exploration of the lease vs freehold debate. ■

About the authors

Thomas is the Managing Director of FTA Law and a corporate solicitor specialising in the sale and acquisition of dental practices, practice incorporations, commercial advice and drafting the full range of commercial agreements applicable to practice ownership, including expense share, shareholders agreements and partnership agreements. If you're thinking of buying a dental practice and need some advice, you can contact the FTA Law commercial property team for a no obligation consultation on: 0330 0882275.



Nigel Jones is Sales and Marketing Director at Practice Plan, the UK's leading provider of practice-branded dental plans and has spent the majority of his 27-year career supporting the development of successful private practice. Through this regular column, he offers YOU the chance to ask any questions you may have about dentistry and running a practice today. Simply email hello@practiceplan.co.uk with your question alongside your job title and location and let us do the rest!

