

## Do's and Don'ts of Facility Leasing: Special Considerations for the Physician Tenant

In leasing space for any business, the landlord and tenant must negotiate several basic terms, which include lease duration, rental amounts and respective obligations for maintenance and repairs. However, physician tenants have unique concerns beyond the basic provisions generally applicable to tenants. A physician tenant must navigate regulatory and non-regulatory issues particular to the practice of medicine in order to successfully negotiate a lease.

**Do:** Tenants must address regulatory issues.

If a physician tenant is renting space in a facility owned by either a hospital, ambulatory surgery center, medical practice, or other entity with whom the tenant has a referral relationship, the parties must comply with the Federal Stark and Anti-Kickback rules and regulations. In simplified terms, the leasing arrangement must meet certain criteria, including the following:

- The agreement must be set in writing and signed by the parties.
- The term of the agreement must be for at least one year.
- The rental charge must be set in advance, must be consistent with fair market value, and must not be determined in a manner that takes into account the volume or value of any referrals.
- The space leased does not exceed the amount needed for the tenant.

To safeguard against violations, an appraisal of the fair market value of the space or other defensible justification for the rental amount should be obtained. Also, the tenant must be careful not to structure the lease arrangement with too high of a tenant allowance or rental abatement period. In general, the arrangement must be commercially reasonable or it will not be permissible.

In addition to the regulatory issues outlined above, HIPAA rules must be considered in drafting a lease. The tenant is required by HIPAA to ensure the safety and confidentiality of patient medical records. To do so, the lease should restrict a landlord's access to the portions of the premises where patient medical records are kept or stored. This is likely to arise in connection with a landlord's right to enter the space and/or to retake the space following a default by the tenant.

**Don't:** Tenants should not assume that every general contractor will be capable of properly handling a medical facility build-out.

If the tenant will be responsible for the build-out of the space, the tenant may be tempted to use a contractor that will perform for the lowest price. However, price is but one of many factors that should be considered. The contractor must be familiar with the specialized needs for the operation of the equipment and systems in a medical space build-out. For example, wheelchair and gurney access may be necessary. Secure space may be required for medicine and patient records. Additional capacity for electrical, water use and waste disposal may be needed. Not all contractors are capable of providing

the specialized services needed for a proper build-out, and they should be interviewed appropriately to ensure their qualifications.

**Do:** Tenants should consider exclusivity clauses tailored to their practices.

In many cases, it is beneficial for a physician tenant to negotiate an “exclusivity” clause with the landlord. This clause prohibits the landlord from renting other space in a building to a tenant with the same type of medical practice. This is of particular concern for practices with more specialized areas of medicine. For example, an imaging center in a multi-tenant building will likely want to prohibit the landlord from leasing space to another imaging center located in the same building, or even prohibit other tenants from maintaining their own sophisticated imaging equipment within their space.

**Don’t:** Tenants should not delay in starting the lease process.

Ideally, physician tenants should start the process of identifying and moving into a new facility at least one year in advance of the anticipated move-in date. Once space is identified, there is still much work to be done. If the current configuration is not suitable for the tenant, an architect must be hired to develop a floor plan. Bids for build-out work must be obtained from contractors. Permits must be obtained. The process for a health care facility can often take longer, given the specialized nature of the work. Article 28 space may also require inspections to ensure code compliance.

**Do:** Physician tenants should anticipate future business structures and transactions.

In today’s business climate, many practices are presented with opportunities that would change their existing legal structure. A practice could be sold to a hospital, making physicians direct employees of the hospital. In that scenario, the applicable space lease must be assigned (or the space subleased) to the acquiring hospital as the new tenant. A properly drafted lease will permit such assignment or sublease without the consent of the landlord. If the landlord has the ability to prohibit assignment or sublease, it could become a difficult obstacle to overcome in the tenant’s negotiation of the sale of its practice.

Leases are often long term commitments that have a significant impact on the operation of a practice. Careful consideration during the early stages of the leasing process could pay dividends in the long run.

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