

MANDELBAUM **MS** SALSBERG

# 8 Essential Steps to Starting Up Your Veterinary Practice





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The attorneys on the Veterinary Practice team of Mandelbaum Salsburg have represented numerous veterinarians in the start-up of their practices. In our experience, the same issues typically arise for each new practice. We have found that if veterinarians take eight key steps, they are more likely to have a successful start-up.

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## Step 1: Obtain Financing

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The overall debt that a veterinarian will incur upon starting a practice is significant. If you have good credit and a solid team of advisors, a veterinary lending specialist (as opposed to a regular commercial bank) may finance the entire start-up cost of your new practice. A specialty lender may even provide additional working capital. Most lenders will require a personal guarantee of the loan. This means that if a practice defaults on its obligations to the lender, the veterinarian is personally

responsible for the unpaid balance of the loan. The lender may also offer favorable payment options. Interest rates for these types of loans may be higher than from a regular commercial bank; however, specialty lenders will lend money for a start-up when other banks will not. Ask your lender about graduated payments, where a smaller monthly payment is due in the early years of the loan, with gradual increases over time as you develop your practice.

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## Step 2: Find a Location

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A good place to start in finding a location is by affiliating yourself with an experienced commercial real estate broker with expertise in veterinary practices. An experienced broker will streamline your mission, save time and identify suitable locations. Typically, landlords seeking tenants and property owners seeking buyers pay commissions to brokers; therefore, as a tenant or buyer, you will get the benefit of the broker's efforts without incurring the cost of the services. When searching for your broker, be sure to ask how much work they do in placing veterinary

practices, how many potential veterinary locations they have as listing agent and their familiarity with local zoning requirements.

One of the first legal issues you will confront once you have discovered an area or site to locate your practice is whether or not local building and zoning ordinances permit the use that you are intending. Each municipality has its own zoning rules and regulations. You will want to identify the particular "zone" where the site is located and review the zone requirements and prohibitions

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that apply. Even if a particular use is permitted in the zone, there could be issues, such as parking requirements, that may disallow the use or require the granting of a variance to get approval. Recognize that even in the case of an existing practice at the site with the same business or when a doctor buys an existing practice, variances could be required for numerous reasons, including but not limited to a pre-existing non-conforming use that pre-dates the zoning regulations. Such uses can trigger a problem upon the transfer of ownership to another individual or business. If you discover that the use for your practice is not permitted and requires a variance, be aware that this will cause delays of several weeks (or, sometimes, months if the city planning board

agenda is particularly full) and increased costs for professional fees. If you are uncertain as to the requirements or whether or not a use is permitted, many municipalities will allow you to write a request to the zoning officer for a zoning opinion and/or grant you an informal meeting to make your inquiries.

In addition, many municipalities have application requirements for certificates of occupancy and many require a planning board appearance despite the permitted use. This “screening” process is intended to help avoid problems with business hours that disturb other residents, ingress and egress onto busy streets or during certain times of the day, and most frequently, parking problems.

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### Step 3: Plan Your Build-Out with an Architect

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Your next step will be to work closely with your equipment specialist and an experienced architect and/or designer and create your new office design. Retain an architect experienced in designing and building out veterinary offices, who

has the ability to work closely with your equipment specialist. Some equipment specialists and suppliers will have professionals on staff that can create the layout and floor plan of the facility.

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### Step 4: Enter into a Letter of Intent

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Whether you are buying or leasing real estate to locate your practice, business transactions can be complicated and time-consuming. Rather than incurring the expense of negotiating and drafting a contractual agreement for a proposed transaction, consider starting by entering into a letter of intent (LOI) with the other party.

An LOI is a document (it can even be a letter from one party to the other, signed or initialed by the receiving party) outlining the preliminary agreements and understandings between the parties to a transaction. The LOI can be prepared by an attorney, a real estate broker or even by the parties themselves. It is not, nor should it be, a legally

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binding contract. The LOI should simply describe the essential business terms of the deal. These include timing, monetary terms, financing, deal contingencies, risk allocation, form of documentation and which party will prepare the documentation. The LOI allows the parties involved to avoid the investment of greater time, energy and money in negotiating a deal and preparing the final contracts if the

parties cannot even agree on the most basic terms of the deal.

What is included in an LOI comes down to what is important to each party. At a minimum, key business considerations (things impacting dollars and cents) should be included. The remaining provisions in an LOI should cover all areas identified by the parties as important matters, and that unless agreed to, could be “deal killers.”

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## Step 5: Negotiate and Enter Into a Lease

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With financing lined up, an office design that will work for you, a capable contractor, a location selected and an LOI for the salient terms to lease your space, you are ready to finalize the lease agreement. The commercial lease for your practice may be the largest financial obligation you will undertake. It is important to remember that as a tenant, you do not have the same statutory rights in a commercial setting as you might have in a residential setting. As a result, the lease agreement only contains those rights that a tenant has contractually negotiated with the landlord. Thus, if the lease does not specifically contain a provision in writing, then it is not so under the lease. Before determining the provisions that you need in your lease, you must first understand the different types of lease agreements that are available.

- A Gross Lease is a lease with a set rental obligation each month. The landlord is responsible for paying all expenses for the operation of the building,

including but not limited to: taxes, insurance, upkeep, repairs, replacements, cleaning and landscaping. In exchange for the useful enjoyment of the premises, the tenant pays a set amount of rent each month.

- A Net Lease is a lease with a set base rent per month, plus an additional rent to cover specific costs for the operation of the premises. You may have heard the terms “single net,” “double net” and “triple net” to describe types of leases. A single net lease is where the tenant pays a monthly base rent, as well as its share of the real estate taxes for the premises. A double net lease is where the tenant pays a monthly base rent, as well as its share of the taxes on, and the insurance for, the premises. A triple net lease is a lease where the tenant pays a monthly base rent, as well as its share of the taxes on, and the insurance for, the premises, in addition to its share of the operating

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and/or maintenance costs of the premises. With a triple net lease, if the cost of snow removal increases because of a snowy winter, the tenant pays. If the

cleaning company raises its rates, the tenant pays. If the town does a tax reassessment, the tenant pays the increase, and so on.

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## Step 6: Complete the Construction and Build-Out of Your Practice

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You will need to retain a contractor to complete the construction and build-out the facility. It is critical that the contractor have experience in building out veterinary offices; seek multiple references. In many cases, the equipment supplier can make recommendations. You should seek multiple bids to establish the price and the timing of the construction schedule. Remember, stick to what you do best and don't try to be your own contractor. Instead, get a "turn-key," fixed-price bid based on the architect's plans and specifications. In addition to getting references, you should visit practices previously built out by the contractor, and confirm that the contractor is fully insured for liability, workers' compensation and builders' risk.

Once you select your contractor, you should agree to a contract for

a set price, including all necessary aspects of the project, from receipt of permits through issuance of a certificate of occupancy. Payment under the contract should be linked to completion of various phases of the project, not based on time elapsed. Avoid a contract where the fees associated with milestones are too front-loaded. There should always be a large enough amount of money held until completion to incentivize the contractor. You may want to consider penalties to the contractor, or discounts, if the contractor runs significantly behind their construction schedule.

With a qualified, skilled and insured contractor providing a fixed fee, "turn-key" build-out with a set timetable, you will be positioned for a successful project.

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## Step 7: Choose a Business Entity

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The choice of business entity is one of the first building blocks to the foundation of your new practice, so it is vital to figure out what kind of business entity is right for your practice. There are numerous business entity options from which to choose, and the selection may vary from state to state. The

formation of any business entity will present different legal and tax consequences, depending upon the type of entity selected. Each business entity has different advantages and disadvantages. Among the many factors that you should consider with your accountant and attorney when selecting a business entity are your

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personal goals and intentions as a business owner and operator.

- **Sole Proprietorship.** The sole proprietorship (“Sole Proprietorship”) is an unincorporated practice. This means that the doctor/business owner is operating as an individual and is personally responsible for any and all actions of the business. It is true that as a licensed doctor you are always responsible for your own acts of negligence in performing the professional services for which you have been licensed; however, in a Sole Proprietorship, you are also personally liable for all other claims against the business, including claims by vendors, creditors, employees and other claimants, or even personal injury claims, such as a slip and fall accident on your premises.
- **General Partnership.** A general partnership (“General Partnership”), much like the Sole Proprietorship, is an unincorporated entity, which is not registered with a state. A General Partnership comes into existence as soon as two or more persons join together to own and operate a business. Ownership of a General Partnership is usually discussed in terms of units or percentages of partnership interests. Although a General Partnership must have at least two owners, there is no limit to the number of partners, nor are there restrictions on the kinds of owners that can be partners. The “owners” of a General Partnership are personally

responsible for all acts and omissions of the partnership, and the business entity does not provide any liability protection. Although the partners can act in the name of the business and borrow money in the name of the business, the general partners are always personally and jointly and severally responsible for all liabilities and debts of the business.

- **Corporation.** A corporation (“Corporation”) is a business entity where ownership interests are evidenced by shares of stock (a percentage ownership) in the Corporation. Unless special elections are made in accordance with federal tax law (such as a subchapter S election, which will be discussed below), all corporations are considered to be “C” corporations (“C Corporation”). A Corporation owns its assets and is liable for its acts and debts. Shareholders are not individually liable for corporate debt (unless they sign a personal guaranty). This limited liability is the primary advantage of the Corporation as a form of business.
- **S Corporation.** An “S” corporation (“S Corporation”) is a Corporation that elects to be taxed as an S Corporation by filing an election to do so with the IRS. Laypersons often mistakenly believe that the S Corporation is a different type of corporation. This is not true. An S Corporation is simply a “regular” Corporation formed under a state’s laws as described in the section on C Corporations above. The only difference is that the Corporation makes

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an IRS election to be treated differently for tax purposes to avoid the corporate level taxation. This election generally provides tax advantages for some Corporations that have a small number of shareholders. Foreign citizens may not be shareholders in an S Corporation. S Corporations have the same liability protections and shareholder liability insulation as C Corporations outlined above.

With some limited exceptions, income earned by an S Corporation as a business entity is not taxable at the entity level. Shareholders are taxed personally on income regardless of whether that income is distributed to shareholders in the form of cash or property.

The “pass through” taxation that is created by an S Corporation results in another advantage to the veterinarian in that losses that result from the startup of a practice are passed along directly to the shareholders, which offsets the doctor’s taxable income from other sources. For example, if you are associating during the early stages of starting your practice in order to have a steady stream of income, within the first year or two of establishing the practice, you can deduct the losses from your startup directly against your income. With a C Corporation, the losses inure to the benefit of the corporation and will be of no benefit to the owner until there are profits in the practice to offset the losses.

- **Professional Service Corporation.** The professional service corporation (“PC”) is a corporation established to provide personal professional services, such as medical or legal services. PCs limit the liability of the owners for business debts, but do not limit the liability of the owners for their personal professional malpractice. The Internal Revenue Code taxes PCs at the corporate level so income is usually distributed to its shareholders in the form of bonuses prior to year end.
- **Limited Liability Company.** When reviewing the various forms of business entities above, one immediately gets the sense that each entity evolved to provide certain liability and/or tax benefits as a vehicle to run a business. The limited liability company (“LLC”) was the next step in that continued evolution toward a business entity that gave us “the best of both worlds.” LLCs were developed in the early 1990’s and were intended to combine the best liability protections and tax attributes of the numerous entities illustrated above. An LLC is a hybrid entity that is treated like a Corporation for limited liability purposes, but can choose to be taxed either as a Corporation, partnership or disregarded entity (single-member LLC) for tax purposes. An LLC is created under state law by registering under a state LLC statute, which involves the filing of what is known as a certificate of formation or articles

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of organization. Like corporate shareholders, LLC members are not personally liable for the obligations of the LLC; instead, their liability is limited to their financial investment in the enterprise. Unlike a partnership, where general partners remain liable for partnership debt, all members of an LLC have limited liability, with the exception of malpractice liability, which always attaches personally to the licensed professional.

For an LLC that chooses to be taxed as a partnership, the tax rules differ from those of General Partnerships only in minor ways. Similarly, an LLC that elects to be taxed as a Corporation will be taxed in the same way as a Corporation. Many single-owner veterinary practices are formed as single-member LLCs, which are considered disregarded entities for IRS tax purposes. In essence, this means that the single practitioner enjoys the liability protection afforded by the LLC, but for tax purposes, he or she only need file a Schedule C Form 1040 in the same manner as a Sole Proprietorship.

Setting up an LLC makes the burden on the business owner less cumbersome. Although observance of the corporate formalities such

as meetings, minute keeping and company resolutions is prudent, an advantage of the LLC over the Corporation is that the statutory obligations for such formalities are not as stringent.

In addition, profits in an LLC may be distributed disproportionately compared to actual percentages of ownership. This would allow the practice to disproportionately distribute profits to a powerhouse producer or the senior doctor or managing partner. Further, if two practices or multiple doctors were to merge and contribute significant equipment or advanced technology products to the new venture, the business deal may provide that the contributing doctors would receive a larger portion of the profits for a period of time.

With an understanding of various business entities and evaluation of the various business entity options, you should not be surprised that veterinary practices today are generally organized as either an LLC or a professional corporation with an S Corporation election. You should consult with your attorney and accountant to decide if an LLC or S Corporation election is best for you.

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## Step 8: Hire Your First Employees

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One of the final steps in launching your practice is hiring your first employees. There are many factors to consider concerning staff selection, recruiting, hiring and management, personnel considerations, and legal and employment law compliance matters that come into play.

- **The Application For Employment**  
The application is the first chance you have to gather information about a potential employee. During this process, you should learn about the employee's qualifications, background, experience and licensing.

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The employment application should pose key questions to the employee in order to avoid potential problems after hiring.

- **Job Descriptions**

A properly composed job description is a very important tool in clearly communicating and outlining the expectations and requirements of the job, without unwittingly entering into an employment contract. The job description should articulate the substantive requirements of the job, including the proposed employee's role in the practice and the minimum requirements to be eligible for the position, as well as the essential functions or duties of the position.

- **Restrictive Covenants**

A condition of employment for all of your employees should be that they enter into a Confidentiality, Non-Solicitation and Non-Competition Agreement. This agreement should be signed by the employee on or before his or her first day of employment. The standard in most states for whether or not a restrictive covenant is enforceable against an employee in a court of law hinges on whether the restriction as drafted is reasonably limited in both time and geography to protect the legitimate interests of the employer.

- **Employee Handbooks and Procedure Manuals**

An employer that operates without a clear understanding of the labor and employment laws or without a proper employee handbook is taking a serious risk. Employment lawsuits can destroy a business and often result in large verdicts or awards for the plaintiff and extremely high legal fees for the defendant business owner. The employee handbook offers the employer a way to publish required policies necessary under the law, set forth operational procedures and describe benefits. Upon accepting employment with the practice, every employee should be provided with an employee handbook and should immediately sign the acknowledgement contained therein. The original executed acknowledgement should be maintained in the employee's personnel file. You do not want the handbook to be interpreted as an employment contract because you want to maintain "at will" employment, and as such, the handbook should be clear and concise and in plain language.

*Once you decide to build your own practice, these steps, with the guidance of experienced professionals, should help make that time in your career an exciting and positive journey.*





Attorneys at Law

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**Mandelbaum Salsburg Lazris & Discenza, P.C.**

155 Prospect Avenue, West Orange, NJ 07052 • Tel: 973.736.4600 • Fax: 973.325.7467  
Edison, NJ • Elizabeth, NJ • Port St. Lucie, FL • New York, NY

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[www.MSGLD.com](http://www.MSGLD.com)