

BUSINESS BRIEFS

Legal Developments Affecting Business



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HOW DO WE SELECT JUDGES? By Hunter Emerick

SUMMER 2013

By all accounts, the Oregon Court of Appeals is one of the busiest intermediate appellate courts in the country. Almost any party aggrieved by a decision issued by an Oregon state jury, trial judge or administrative law judge has an absolute right to appeal the decision to the Oregon Court of Appeals. Over a ten year period, the Oregon Court of Appeals received between 3,200 and 4,100 appeals each year.

Recognition of this workload resulted in passage by the 2012 Oregon Legislature of HB 4026, which increased the number of judicial seats on the Oregon Court of Appeals from ten to thirteen. The positions are to be filled by October 1, 2013. It appears that, despite the fiscal challenges which currently face the State, the 2013 Oregon Legislature will appropriate the funds necessary to staff these three new appellate judicial positions. Curiously, in approving the new appellate positions, the Oregon Legislature specified that the new positions were to be filled initially through appointment by the Governor of the State of Oregon. The newly appointed judges, however, will be required to run for election at the next general statewide election.

Currently, the Oregon Constitution and statutes state that a Court of Appeals judge holds that office for a six year term and until a successor is elected and qualified. If a judge allows his or her term on the appellate court to expire, or if the judge is unsuccessful in running for re-election, the candidate elected in a statewide election will succeed to the office. Only if a judge resigns his or her position midterm, will that position be filled through appointment by the Governor of the State of Oregon. With three new appellate judicial positions being created by the Legislature, the Legislature's decision to allow those positions to be filled initially by appointment, rather than by the ballot box, deserves attention.

Many Oregonians believe that the State's judicial positions are filled by election. Although that is generally true, the appointment process is being used more frequently to fill judicial seats which become vacant midterm. For example, in Marion County, the last 5 trial judge vacancies were all filled by appointment, except for one position. The last 4 vacancies on the Court of Appeals were filled by gubernatorial appointments, except for one position. The American Judicature Society reports that approximately 85 percent of Oregon judges have first been appointed, rather than elected. Once appointed, the new judge running in the next general election is an incumbent and can use the description "Judge" before their name on the ballot. Understandably, the vast majority of these newly appointed judges are successful in keeping their job in the following election.

As currently practiced, the appointment process is triggered by a midterm resignation. Typically, the Governor's office announces the vacancy and requests all interested and qualified candidates to submit an application. The application is then reviewed by the Governor's staff and, in some cases, by a local or state Bar Association. Historically, some of the Bar Associations ranked or expressed preferences between the candidates. More recently, however, the Bar Associations only state whether the candidate is qualified. I have served on both county and state

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Bar committees conducting these reviews. The committee members are drawn from many different practice areas.

The Governor's Office, however, is not required to follow the Bar Associations' recommendations or comments concerning the candidates. In fact, midterm judicial appointments are solely within the sound discretion of the Governor's Office. Although political affiliation is not formally considered in judicial appointments, the fact remains that Oregon has not had a Republican Governor since Vic Atiyeh in 1987. Unlike the federal system, the Oregon Legislature has no formal input into the selection of state appellate or trial judges.

There is a growing unease with Oregon's system of electing judges. Running statewide campaigns is becoming extremely expensive. Federal and state constitutions have not placed any significant limits on the fundraising for or spending in judicial races. Other states have seen their judicial elections inundated with outside money and special interest groups. Recently, incumbent judges in both Wisconsin and Iowa lost elections to opponents funded largely with out-of-state money. These campaigns were focused on special interest issues, not on the judges' qualifications or competency. Although Oregon's judicial elections have not yet experienced similar incursions, many commentators feel as though it is only a matter of time.

Understandably, citizens believe significant campaign contributions to a candidate may affect the judge's impartiality on the bench. An independent judiciary is a critical component of the checks and balances necessary to hold a representative democracy accountable to the rule of law. However, Oregonians have always had an independent streak and are wary of intellectual or political elites. Oregon's rather unique initiative process is a ready example of our State's desire to protect direct democracy from a non-responsive Legislature. Clearly, elections are a very direct manner to hold judges accountable to the electorate.

Partially in response to these concerns, former Chief Justice Paul De Muniz is leading a Work Group on Appellate Judicial Selection and Retention in Oregon. The Work Group is supported by the Oregon Law Commission. The Commission is housed at the Willamette University College of Law located in Salem, Oregon. The purpose of the Work Group is to make recommendations to the Oregon Legislature as to the judicial selection process. Many formulations are being considered by the Work Group. Among them is a judicial nominations commission comprised of diverse and bipartisan members of the public and the Bar that would review the candidates' backgrounds and qualifications, interview the candidates and recommend the best candidates to the Governor. However, the Governor would make the selection, presumably from the list submitted by the commission, in his or her sole discretion. After appointment, the Judge would later run in a retention election or, in the alternative, be reconsidered by the commission for retention as a judge. This group is doing important work which could very well change the Oregon judiciary for years to come. If you are interested in following this Work Group, more information can be found at www.willamette.edu/wucl/centers/olc/groups/2011-2013/js/index.html.

YOUR OFFICE LEASE – NOT AN AFTERTHOUGHT WHEN BUYING A PRACTICE

By Mark Shipman & Doug Alexander

You just started the initial negotiations on purchasing a dental practice. In addition to discussing the purchase price of the practice, the goodwill, and the equipment, there is a single line on the letter of intent that says you will assume the existing lease agreement or that you will agree to enter a new lease agreement. Oftentimes, leases mistakenly take a back seat to the sale documents in a dental practice purchase. This is a mistake that should be avoided. Your lease is an important business asset that you need to keep pace with, no different than maintaining and expanding your patient list, or upgrading your dental equipment.

The initial negotiation for the practice purchase is the best time to negotiate lease terms that will enable you to grow your new practice. Below is an overview of some key elements regarding a lease that you should consider at the time of a practice purchase.

Term (Length) of The Lease

There are many questions to consider regarding the term of the lease. If there is an existing lease in place, when does the current term end, and are there options to extend or renew the term? Taking over a lease mid-term with 3 years remaining and no option to renew could put you in a difficult position in 30 months. Better to build in an option to renew for 3 – 5 years, with additional renewal terms to ensure you won't have to engage in a costly move. In most cases, if you are financing the purchase of the practice, your lender will insist on a lease term that is at least as long as the term of your loan. If you want to consider relocating your practice before your loan is paid off, then you should negotiate a shorter initial lease term with options to renew. That option will enable you to stay at the current location for the term of your loan, but be sure to get approval from your lender.

If you are entering into a new lease, you may not want to start out with a 10 year term unless you are certain that you will be content with the location for a long period of time. Instead, consider starting out with a 5 year term with multiple 5 year renewal options. Building in this type of flexibility will enable you to evaluate whether this location is the one that will allow you to grow your business, or time to prepare a more suitable permanent location, if needed. On the other hand, if you know at the outset that the current location is the best for your practice, then consider requesting an option to purchase the property up front.

Rent and Rent Increases

When assuming the current lease, are the current and proposed rent rates commensurate with the market? If not, now is your time to negotiate a change in the rate, and possibly change the escalator provisions as well. Almost all leases have rent escalator provisions. Some are tied to the

Consumer Price Index (CPI), others can be a lock step increase by a certain percentage each year. What does the existing lease require under the escalation clause? Are rents tied to the Consumer Price Index (CPI), and if so, which index? Does the clause have a ceiling on the CPI increases? At the end of each term, does it allow for an evaluation of rents and rent increases going forward?

With the downturn in the Oregon economy, rents in many areas have not increased but remained flat. If the selling dentist/landlord has an aggressive rent structure and escalator provisions in the current lease, then the current contracted rental rate may not be in tune with the market. This is the time to recalibrate both the rent and escalator provisions.

Maintenance & Conditions of the Premises

What does the existing lease require for maintenance of the leased premises? Are the premises a standalone building and parking area for which the landlord expects the tenant to be responsible for all maintenance; or, is it a part of a larger building or complex, where the maintenance is shared between the tenant and landlord?

Likewise, what are the conditions of the leased premises? Is it newer space that is well maintained? Is it an older building where the current tenant and landlord let things slide, failed to keep up on repairing or replacing worn items, or failed to keep track of maintenance? The landlord can often provide you with a file with the maintenance schedule and items that have been completed during the current lease.

Knowing the specifics of the condition of the premises and the status of maintenance can be very important. We cannot stress enough how many times a tenant has come to us and said, "The landlord verbally told me that we were not responsible for that element when we entered the lease." Yet, the lease language is clear and unambiguous—it is the tenant's responsibility. Or worse, the lease is ambiguous and the landlord is now taking the position that the tenant is responsible for the costly maintenance and improvements to the premises. Taking the time to

fully understand the condition of the premises and your obligations for maintenance is important at the front end, so you can minimize a costly repair or avoid a costly dispute over a needed repair.

Assignment

What does the existing lease require for an assignment of the lease? Does it freely allow assignment, or is the assignment restricted, perhaps requiring the landlord to consent. May the landlord withhold consent in its discretion, or perhaps if the new tenant does not have a credit rating and net worth similar to the current tenant? May the landlord charge a fee for the assignment? If so, are the terms of the fee established in the lease, or are they ambiguous? Is there a personal guarantee in the lease and will the landlord release the underlying tenant upon an assignment?

While it seems odd that you would be thinking about a future assignment at the beginning of the new relationship, building flexibility into your lease agreement is important with respect to a business purchase, expansion, sale, or upon your unforeseen disability or death. You do not want to be in a situation where you want to bring in a new dentist to take over your practice, but the lease assignment provisions require the landlord's consent and the landlord has decided to be less than cooperative in approving an assignment. This can be avoided if you effectively negotiate the terms for a future assignment at the time you enter into a new lease or assume an existing lease.

These are just a few of the key provisions that you should consider before committing to a lease or an assignment. Putting off the lease negotiations or treating them as unimportant can put you in a bind both in the short term and in the future. During your purchase negotiations, be sure to meet with your financial and legal advisors in order to carefully consider all the consequences of a current or new lease on your practice. If you would like assistance in reviewing and analyzing these and other lease related issues, please contact a member of our Dental Team 503-399-1070.

PREPARING FOR RETIREMENT

By Freeman Green

Hoping to retire in the near future? Here is an overview of seven things to consider.

Plan for Health Insurance

Affordable health insurance is one of the biggest obstacles to retiring prior to age 65. Group coverage is typically less expensive than purchasing individual coverage. Look for group coverage through professional associations, a spouse's employer or even churches. Maintaining health insurance through part-time employment is also an option.

Though traditionally more expensive, purchasing an individual policy is also a coverage option. Individual coverage may become more attractive in 2014 when provisions of Obamacare go into effect. These provisions forbid insurers from denying coverage based on preexisting conditions, limit the degree to which insurers can differentiate based on age and simplify shopping through online exchanges.

At age 65, you will be eligible to enroll in the federal government's health insurance program, known as Medicare. Evaluate whether to enroll in traditional Medicare or Medicare Advantage, which is a Medicare alternative designed to give Medicare beneficiaries access to a broad array of private health plans. In addition, consider purchasing a "Medigap" policy. Private insurers offer these supplemental policies to cover the coinsurance, deductibles and services not covered by Medicare.

Plan for Long Term Care

Long term care costs are a commonly overlooked matter in retirement planning. Health insurance policies do not cover the costs of caring for chronic disabilities, illness or infirmities (i.e. nursing home and assisted living expenses). This type of care is commonly referred to as "long term care." Long term care can cost as much as \$80,000 per year, and the odds of needing such care are high. According to the U.S. Census Bureau, individuals age 75 and older have a 53% chance of having some kind of disability.

Most individuals prepare for potential long term care costs using some combination of long term care insurance and self-insurance. Like most insurance products, the cost of long term care insurance will vary with your age, your health and the quality of policy purchased.

Transition Your Business

Transitioning your business takes planning. Plan on at least 3 to 5 years to implement an effective exit strategy. Begin by valuing your business and establishing a fair asking price. Involve your accountant and attorney in the process early on—they will help you minimize income tax, and protect your interests. Your buyer may be a fresh young entrepreneur, so be prepared to give mentorship as a part of the transition.

Update Your Estate Plan

Remember those old documents at the bottom of your safe deposit box? It's time to dust them off and take them in to your estate planning attorney for an update. At a minimum, you should have a current power of attorney, an advance health care directive and a will. These documents will provide financial continuity in the event of your incapacity, express your wishes regarding medical and end-of-life decisions, and direct the division of your property after your death. You may also choose to create a living trust in order to circumvent the expense, delay and publicity of a court-supervised probate. A proper estate plan can also reduce the impact of state and federal death taxes, which currently affects individuals with property and life insurance totaling more than \$1 million.

Meet With Your Financial Adviser and Accountant

Your financial adviser and accountant have tools to help you evaluate and plan for retirement. Learn which investments would be best to draw from first, and specifically ask for advice on when to begin drawing on Social Security benefits.

Most retirement decisions have hidden tax and financial impacts. Your accountant and financial advisor can help identify these impacts and use them to your benefit. For example, some items discussed in this article, such as health and long term care insurance premiums and estate planning costs, can be tax deductible.

Figure Out How to Coexist With Your Spouse 24/7

The emotional and financial strain of a divorce can pour a great deal of lead into the golden years. Many couples are surprised to find that retirement tests their relationship in new ways. Work with your spouse to develop and maintain mutual hobbies and interests. Balance your shared interests with individual interests, and respect the personal time and hobbies of your spouse. Remember, your spouse will now bear an additional 40 to 50 hours per week of your quirks and oddities, and vice versa. Work together to anticipate and solve potential problems through open and tactful communication.

Develop a Plan for Your Free Time

Get involved in a community or charitable program. Learn a musical instrument. Write that book you've been visualizing for the past 20 years. Spoil your grandkids. Join a book club. Become a Mentor. Write a personal memoir to pass on to your descendants. Create a long, ambitious bucket list and start checking it off. Cheat death for as long as you can—and when you die, die from exhaustion, not boredom.

AVOIDING THE 3.8% MEDICARE TAX ON SELF-RENTAL INCOME

By David Myers

For those of you who don't have the opportunity to read the tax code like I do, you may not know that the federal government has imposed a new 3.8% Medicare tax on certain investment income. Absent some up-front planning, this tax can apply to rental income that is generated when a business rents property from its owner. Many business owners set up a separate entity to own a building or other real estate and then have the operating business rent that property back from the new entity. Businesses use this strategy to help protect the property from potential liability and for tax planning purposes.

Although we still don't have all the details about this new Medicare tax — more technically called the Net Investment Income Tax — it seems likely

that businesses answering “yes” to the following questions may have an unpleasant surprise waiting for them on tax day:

- a) Does your business pay rent for the use of property that you either own personally or in a separate entity?
- b) Is the lease for that rental a “triple-net” lease? In other words, is the tenant responsible for paying taxes, utilities, and insurance on the property?

If you’ve answered “yes” to these questions, then it’s time for some changes. In order to avoid application of the additional 3.8% tax to this “self-rental” income, business owners should work with their professional advisors to ensure that the following actions are taken. These recommendations are based on the general rule that rental income is not subject to the additional 3.8% tax when it is “derived in the ordinary course of a trade or business” that is not a “passive activity.”

Make the Grouping Election for Section 469 Purposes

Business owners engaging in self-renting should make the election to group the rental activity with the active business activity for Section 469 purposes (assuming they are eligible to make such election). The election is made by filing a statement with the applicable tax return, although the rules differ depending on the type of entity. Once made, the election is generally irrevocable. Making the election will cause the rental activity to be considered active rather than passive (assuming the business owner materially participates in the business). However, the U.S. Treasury has taken the position that taking the election may, by itself, be insufficient to avoid the tax because the rents still must be “derived in the ordinary course of a trade or business.” In order to address that position, we recommend also taking the second action, described below.

Do Not Use a Triple Net Lease

Lease agreements for self-rented property should not be structured as triple net leases in order to ensure that there is enough activity on the part of the landlord to characterize the rents as “derived

in the ordinary course of a trade or business.” The landlord’s leasing activities should be as active as practical. Such active activities include snow removal, landscaping services, and similar included services. However, the removal of any triple net lease provisions would appear to be adequate as a minimum threshold.

Although the law in this area is still unclear because the additional 3.8% tax is so new, unofficial IRS commentary suggests that the above changes will most likely protect businesses with self-rental income from the new tax. It is expected that the U.S. Treasury will provide additional guidance on this issue before the grouping election needs to be made with a taxpayer’s 2013 tax return. This election can be dated back to the beginning of the tax year. However, the decision to modify a triple net lease should be made immediately, in order to avoid the additional 3.8% tax for as much of 2013 as possible. It is expected that this requirement will be mandated under the official IRS interpretation.

In sum, in order to avoid application of the new 3.8% Medicare tax to self-rental income, we recommend immediately amending lease agreements to remove triple-net provisions, and making the section 469 grouping election with the 2013 tax return filing, subject to any additional guidance provided by the Treasury.

Saalfeld Griggs Blog

The firm recently re-vamped and re-launched its website. Check us out at www.sglaw.com. In addition to our newly re-designed website, we have added the SG Blog. Check out the website homepage for recent SG Blog posts, including:

- Senate Bill 558A: Changes to Oregon’s Foreclosure Laws
- Construction Contracts: Using Price Escalation Clauses to Address Rising Costs
- Banking Law Alert: Foreclosure Practices Violated WA Consumer Protection Act
- Employer Update: 2013 Payroll Taxes

FIRM SEMINARS AND ANNOUNCEMENTS

Thank you to everyone who voted for **Saalfeld Griggs PC** in the **Statesman Journal's "Best of the Mid-Valley"** competition. We are excited to announce that Saalfeld Griggs received the Gold Medal for best mid-valley law firm for the third year in a row. This is a great honor and we appreciate the community's support.

Jeffrey Moore and **Robert Saalfeld** were recently selected by Martindale-Hubbell and the American Lawyer Media, a leading provider of news and information to the legal industry, as 2013 Top Rated Lawyers in **Trusts and Estates**. Congratulations Jeff and Bob!

Dorothy Bean, a lawyer in the **Saalfeld Griggs' Construction Industry Practice Group**, was honored as the Future Leader of the Year for 2012-2013 by the Salem Chapter of the National Association of Women in Construction ("**NAWIC**"), a national nonprofit organization that promotes and supports the advancement and employment of women in all aspects of the construction industry. The Future Leader of the Year Award recognizes an individual who has made significant contributions to the Salem NAWIC chapter in the past year, and who has taken on a leadership role within the organization. Congratulations, Dorothy!

The Saalfeld Griggs **Employment Law Team** is tracking employment-related legislation and sending out monthly updates with status reports and analysis of possible impact. If you would like to be included on our email distribution list, please email **Randall Sutton** at rsutton@sglaw.com.

Saalfeld Griggs' Dental Industry Team has posted a selection of white papers for use by dental professionals in managing the legal aspects of their practices. Check out the Dental Team and the whitepapers at our website at sglaw.com.

On January 29, 2013, **Jennifer Paul** was named the 2012-2013 National Catholic Educational Association ("**NCEA**") Distinguished Graduate for Queen of Peace Elementary School. The NCEA Distinguished Graduate Award recognizes an alumni member who has made a significant contribution to his or her community. Jennifer graduated from Queen of Peace Elementary in 1997. Jennifer was honored for her volunteer work, including her involvement with Catholic Community Services, the Boys and Girls Club, and Mothers Against Drunk Driving.

Erich Paetsch and **Shannon Martinez**, lawyers in the **Creditors' Rights & Bankruptcy Practice Group**, recently made a presentation to the Oregon Banking Association Lending Committee. The presentation was entitled "What's in a Name? Transitioning to Perfection Under the UCC." The presentation covered the 2013 changes to the Uniform Commercial Code ("**UCC**") and other hot topics in commercial lending.

Mark Shipman, **Alan Sorem**, and **Nate Boderman** recently presented four sessions on COMMERCIAL LEASING: LANDLORD BOOT CAMP AND TENANT BOOT CAMP. If you would like to attend future sessions, please email jmarshall@sglaw.com.

Randy Cook and **Christine Moehl** recently spoke at the National Institute of Pension Administrators ("**NIPA**") Annual Conference in Las Vegas, Nevada. The topic of their presentation was "ADVANCED PLAN DESIGN TECHNIQUES FOR DEFINED CONTRIBUTION PLANS." If you would like more information on retirement or health plans, contact Randy or Christine.

