



10 PITFALLS TO TAKING A COMMERCIAL LEASE

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If you have never taken a commercial lease before - and even if you have – you may find that the process is not as straightforward as you expected.

In this guide, we have summarised the key issues that you may wish to consider before committing to a commercial lease as a tenant. Being aware of the pitfalls and knowing how to address them should enable you to both save money, and speed up the process of signing up to your lease. Ideally, you should send the Heads of Terms which have been agreed for the letting to us and to a surveyor for approval - there may be points

which ought to be included or removed, and these can then be dealt with at an early stage, preventing unwanted delays later.

Bear in mind that in some situations, particularly where you only need a property for a short time, a standard lease may not be your best option. We can advise you on your options at an early stage so that you can make the right decision for your business.

1 UNDERESTIMATING THE TIME REQUIRED

The legal process when a lease is prepared and negotiated can take a number of weeks before it is in a form that we are happy to recommend to you. Typically, finalising Heads of Terms is only the start of the negotiation process rather than the end. Even a relatively simple lease will typically take 3 to 4 weeks to finalise. You should allow longer if the terms agreed are unusual or if there are other parties involved, such as the landlord's bank, as its consent may be required.

Ensure that you begin lease negotiations and instruct solicitors well in advance of the date you intend to start business at the property.

OUR TIP

Retailers should consider how timings may affect your plans for starting trade from a new property. You may want to try and avoid completing just before holiday periods or during very busy trading periods. Factor in the time needed to prepare the property for trade, and bear in mind any lead times required for orders.



2 TAKING THE WRONG PROPERTY FOR YOU

It is vital you ensure that your property is fit for your intended use. Make sure you check:

- **THE NATURE OF THE PROPERTY**

Will your budget be adequate to make the property fit for your purpose? Does the property have enough space to meet your intended requirements and do you need to leave room for expansion?

- **THE RIGHTS YOU WILL BE GRANTED**

Will these cover everywhere and everything that you need? For example, if you need the use of communal parking spaces, or the right to load or unload lorries in a loading bay, ensure these points are in the Heads of Terms from the outset.

- **PLANNING ISSUES**

You should check that the use as designated by the planning authority complies with your intended use. For instance, if you are taking over a property that was previously a private house with the intention of turning it into an office, you may need to apply for planning permission before you can use the property.

- **IF THERE'S ANYTHING YOU DON'T NEED**

The likelihood is that you will be responsible for the upkeep of the property. If, for example, you are granted a basement which you do not need, consider whether the increased responsibility in terms of your obligation to repair (and possibly business rates and utilities) makes it worthwhile to take on.

OUR TIP

Check with your local planning authority, or ask your solicitor to check if the property is (or forms part of) a listed building or lies within a conservation area. Either of these designations can affect your ability to alter the property and even put up signs.



3 MISJUDGING THE LENGTH OF THE LEASE

The term of the lease should be considered carefully. On the one hand, you need to ensure that you will have long enough to build your business and recoup the cost of any initial fitting out or moving costs. On the other hand, you want to avoid the risk of being burdened with the responsibility of a long lease which you cannot afford. You may be able to agree the inclusion of an early exit (known as a, “break option” – see below), but regardless, the length of the term should be considered carefully.

WARNING – Watch out for anything in your lease which states that your rights under the Landlord and Tenant Act 1954 are excluded. An exclusion of these rights could prevent you from having a right to renew your lease or receive compensation when your current lease expires. This is a risk; especially if you have invested a great deal into the property, or if your business is dependent on the particular location.

4 HIDDEN RENT TRAPS

It is very important that you understand the rent obligations which are contained within your lease. If you are late paying your rent, you run the risk of being liable for interest as well as other costs. More significantly, there is a risk that the landlord could end your lease early. This is known as “forfeiture”.

The law allows a landlord to take the property back without even applying to Court for situations where rent is unpaid after the period of time stipulated within the lease, often as short as 7 days.

Landlords can also invoke the ‘CRAR’ (Commercial Recovery of Arrears of Rent) which allow them to seize a tenant’s goods from the property if rent remains unpaid.

When you take on your lease set up a Standing Order – as explained, late payment of rent can result in interest being due, or even forfeiture. Avoid agreeing to direct debits which give the landlord more control over withdrawing money from your account.

OUR TIP

Traditionally, rent is payable 3 months in advance on the standard quarter days (25th March, 24th June, 29th September and 25th December. However, many tenants negotiate for rent to be paid monthly in advance, which tends to be better from a cash-flow point of view.

5 RENT CHANGES

Many leases (particularly leases of three years or more) contain rent review provisions. You should be aware of the most common types of rent review:

- **UPWARDS ONLY REVIEWS**

Typically, rent reviews will be on an upwards only basis, which means that on the review date the rent will either stay the same or go up. An upwards only review means that the rent will never come down.

The rent will be based on the prevailing market rent at the time of the rent review date, which leaves a degree of uncertainty as to what the rent will be increased to in the future. With this arrangement there is sometimes scope for dispute as to what the appropriate rental uplift should be and you may have to budget for a surveyor to assist with any negotiation. Try and have surveyor check the rent review clauses in the lease before you agree to them.

- **INDEX-LINKED REVIEWS**

Rent reviews can also be index-linked to inflation. This does not entirely remove the element of uncertainty as to what the rental increase might be in the future, but there is less room for dispute as to what the correct figure should be.

- **STEPPED RENT INCREASES**

Some leases state from the outset what the rent will increase to on certain dates. This removes any element of surprise as to what your future rent will increase to, but there is always the potential that the market value for leasing your property and inflation do not increase as much as anticipated, leaving you in a comparably worse position than if one of the alternative methods had been adopted.

OUR TIP

If your lease contains an open market rent review, you should ensure that the landlord cannot value improvements which have paid for when determining the rent at the review. Check the wording in the lease carefully.

A large, stylized logo for 'bbs law' is positioned in the bottom right corner. The letters 'bbs' are in a dark green, serif font, while 'law' is in a white, serif font. The logo is set against a light blue background that is part of a larger graphic element.

6 TRANSFERRING YOUR LEASE – IT'S NOT AS EASY AS IT SOUNDS

• WHY DO I NEED TO WORRY?

You may wish to reorganise or sell your business; your property might become surplus to requirements; or you might need to downsize.

• WHAT DOES IT HAVE TO DO WITH THE LANDLORD?

There are two main ways of parting with leased property: assignment, where you transfer the lease, and underletting, where you essentially grant a lease to someone on similar terms to your lease, so that you become the landlord for your new tenant. You will almost certainly require the landlord's consent to do either and there will be conditions attached to any consent. Normally the landlord will have a duty to act reasonably in these situations but bear in mind that some leases do prohibit passing on your interest altogether.

• IS IT ALL OR NOTHING?

It is unlikely that you will be permitted to split up the property unless the property is easily divisible, and you have agreed this concession with the landlord from the outset. Sharing the property is also likely to be forbidden by the lease.

• WHAT OTHER COSTS WILL I HAVE?

Any application for permission to assign or underlet will almost certainly involve paying the landlord's legal and survey costs for considering and providing a licence to consent to your application. These costs are likely to be payable whether or not your application is successful, so consider carefully before making an application to transfer your interest in your lease.

WARNING – *Whether you assign or underlet you are unlikely to be released completely of your responsibilities as the tenant when you transfer your lease. The landlord on any assignment is likely to be able to request that you remain as a guarantor – known as an Authorised Guarantee Agreement – and you will still remain the tenant.*

7 REPAIR OBLIGATIONS

Standard commercial leases will usually require you keep the property fully repaired and in a suitable state of decoration. This obligation will apply even if you did not receive the property that way, meaning that you could be required to put the property into a better state of repair than it was in when you took the lease.

You should always thoroughly inspect the property and ideally have a surveyor examine the property before entering the lease. Raise any concerns with the landlord well in advance of committing to the lease. You may be able to negotiate a longer rent-free period to compensate for the state of the property, or alternatively ensure that any necessary repairs are undertaken before you sign the lease.

Ask the landlord to limit your repairing obligations through a schedule of condition. The schedule of condition should be prepared by a surveyor, and should show the condition of the property on the date that you take the lease. The schedule of condition should be attached to the lease so that you are not liable to put the property into a better state than that in which you received it.

8 UNEXPECTED COSTS

• UP FRONT COSTS

On top of budgeted initial repairs and fit-out costs, depending on the amount of rent and the length of your lease, you may need to pay Stamp Duty Land Tax (SDLT) and Land Registry fees. We will advise you very early on if these will be payable.

• INSURANCE, UTILITIES AND BUSINESS RATES

Unless you have agreed an all-inclusive rent you will be required to pay these on top of your rent. For insurance, normally the landlord will take out buildings insurance for the property and charge the cost back to you. You will need to arrange your own contents and public liability insurance cover.

• SERVICE CHARGE

There will often be a separate service charge payable under the lease to cover the costs of maintaining and repairing communal areas, and possibly structural parts of a multi-let building or other shared development. You should enquire as to what these costs are likely to be, what services are provided, whether a managing agent will be providing the services (and their charges) and if there are historical details going back at least three years and budgets for future years. Additionally, do check there is no significant expenditure contemplated.

The service charge may look reasonable, but check to ensure that the landlord does not have a major capital expenditure planned, which is something that may be recovered from you via the service charge. Additionally, ensure that the service charge is limited to maintenance and repair, and does not allow the landlord to improve their property at your expense.

Do not be afraid to ask!

OUR TIP

It is often worth trying to negotiate a maximum figure (cap) on your annual service charge payments to ensure that the service charge cannot exceed a certain sum. A cap will ensure that you are able to budget better by knowing the maximum you can be required to pay for the service charge in any year.

9 DIFFICULTIES WITH ENDING YOUR LEASE EARLY

“Break clauses” allow tenants to bring their leases to an end early, offering you more flexibility. Landlords often stipulate conditions which need to be fulfilled before the tenant can operate (known as exercising) the break clause. Common conditions include all or some of the following:

- A minimum period of notice (often six months) prior to exercising the break,
- Written notice notifying the landlord that you intend to exercise the break – often in a precise form set out in the lease,
- All monies due under the lease to be paid up to date on the date of service of the break notice and/or the break date,
- That there are no breaches of the lease on the date of service of the break notice and/or the break date,
- A requirement that the property is returned empty.

If you intend to exercise your break, let us know a few months in advance so that we can advise you how to correctly bring the lease to an early end.

The law generally requires very precise compliance by the tenant of any conditions for it to be able to exercise the break. If the requirements relating to breaks are not dealt with correctly, the likelihood is that the exercise of the break will be invalid, meaning that you will be obliged to continue with the lease. Try, if possible, to have the landlord agree to a break clause with no conditions or limited conditions, which will make the break clause easier to understand and operate correctly.

OUR TIP

Avoid mutual break clauses, where either the landlord or the tenant can end the lease early. These can be a real problem in creating uncertainty as to how long you will be able to occupy the property. This is especially true if business is going well, as the landlord could use his break to end your lease early, potentially resulting in significant disruption to your business.




TO AN UNHAPPY ENDING

Depending on the extent of your repairing obligations, the landlord will want to ensure that you give the property back at the end of the term in the condition required by the lease. Try to agree at least 6 months in advance of the end of the term with the landlord the extent of the works that will be required, so that you have adequate time to carry out the necessary repairs.

If you do not deal with the necessary repairs before the end of the lease, the landlord is likely to serve a schedule of dilapidations on you, setting out what repairs you are liable for, and the costs in respect of those works. They are likely to then charge these repairs back to you, as well as a sum to account for the property being unavailable for leasing to other parties whilst the repairs are being undertaken. It might be possible to negotiate the costs with the help of a surveyor, but we would always recommend that you deal with the issue well in advance of the end of the term.

Alterations you have made also need to be removed at the end of the term. If your lease requires it, always obtain consent from the landlord before undertaking alterations to the property and try to agree in writing with the landlord as to what the reinstatement obligations will be for the alterations at the end of the term. If you are undertaking major alterations, it could be very costly to have to remove all these when you vacate the property.



For further assistance with your lease requirements, or for any further information contact a member of our property team.

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