

Commercial Leases: Overview of Common Terms Covered by a Lease Agreement

Commercial Leases

This guide deals with a situation where you are agreeing a lease of commercial property. You will not own the property but will have the exclusive possession of the premises for a fixed term as a tenant. You can buy an existing lease from another tenant or enter into a brand new lease.

Commercial tenants are not as well protected by legislation as residential tenants, and there are a number of areas to review carefully when taking on a lease. The lease should set out both the rights and obligations of both you the tenant, and also the landlord. A lease should be agreed in writing but in some situations a verbal lease agreement can also be legally binding on both the landlord and tenant.

To help you start to understand what's what, here is an overview of common terms typically covered by a lease agreement:

Security of Tenure: the lease should make it clear if it is protected by the Landlord & Tenant Act 1954, or if it is "contracted out" of that Act. This is sometimes called "security of tenure", or a "protected lease", or a "renewal lease". In short, if you have security then you have the right to a new lease when the existing lease ends, or potentially to compensation if you do not get a new lease. If you are contracted out, when the lease ends you are a trespasser and can be evicted immediately. Apart from the rent, your status as a tenant is probably the single most important thing to consider. Please see our How To Guide "The Landlord and Tenant Relationship" for more information.

Rent: the lease will set out when rent is to be paid, and sometimes how ie by direct debit or standing order. Rent might be payable monthly but is usually payable "quarterly". That means three months' rent is payable in advance on the "quarter days". These are 25 March, 24 June, 29 September, and 25 December. This clause will usually specify that rent is payable whether the landlord formally demands it or not. So you are probably not entitled to any invoice before you pay. The lease will also have in it, probably in a different paragraph, a condition that you have to pay interest on late payments of rent and specify the interest rate.

Rent Reviews: most leases have a "rent review clause" where the rent is 'adjusted' or 'reviewed' after a set period of time. The lease will set out when and how this is to be done. The idea is that the landlord keeps on getting the "market rent" for the property. As you would expect, these are unpopular with tenants. Usually, rent reviews take place every three to five years. The lease will say how often. The lease will say how the new rent is to be worked out, and the legal process involved. In practice, upwards only open market rent reviews are the most common. That means that even if the market rent has gone down, the rent payable will stay the same. Please see our How To Guide "Lease length, break clauses and rent reviews" for more information.

User: Critically, the lease should also stipulate what the property can be used for. This is called the "user" clause. You should check whether there are any restrictions on use in the lease. You should also check separately that the correct planning consents are in place before you sign the lease.

Repairing Obligations: The majority of new commercial leases are fully repairing and insuring leases (or "FRI Leases.") This means it is your responsibility as the tenant to repair and pay for the insurance of the premises. Exactly what 'repair' is will depend on the wording of your lease. Repair clauses are one of the most commonly litigated aspects of commercial leases. The repair clauses will also contain the tenant's responsibility and liability for "Dilapidations" (see next item).

Dilapidations and reinstatement and fittings and fixtures: You will have to return the premises back into the standard of repair set out in the lease. That usually means the condition in which you took the premises on. This could mean a substantial cost if work you have carried out to meet your needs limit the market for finding a new tenant. You could also find that ownership of any equipment installed on the property at the end of the lease stays with the

landlord. You need to be aware of the degree of your responsibility before signing. See our How To Guide "Dilapidations" for more details.

Lease Term: The "Term" is the length of the lease. Make sure these fit in with your short term and long term commercial objectives. Typically, this may be between three and five years but can be longer and even up to 25 years. See our How To Guide "Lease Length, Break Clauses and Rent Reviews" for more details.

Sub-letting and Assigning the lease: Sub-letting is granting a lease to another party so they become your tenant in the property. You might sub-let all or only part of the property. Assigning is selling the lease itself to someone else. Look carefully at any restrictions on your ability to assign or underlet the lease. Even if you can transfer the lease, you may still be responsible for the rent and other commitments if the incoming tenant does not honour them. This is a complicated area and you should seek legal advice before doing this. See our How To Guide "Assignment and Sub-Letting" for more details.

Alterations: Does the lease allow the tenant to carry out alterations? If so, what kind? Will the tenant need the landlord's permission? What does the tenant need to do to get that permission? There may also be limits on what signs and decorations a tenant can put up. Sometimes the lease will allow the tenant to make non-structural alterations without consent. Some issues with alterations are:

- What a "non-structural" alteration may be debatable!
- If landlord's consent is needed, the landlord will usually have their surveyor check that what is being proposed is acceptable to them, and will also want a contract drawn up called a "licence to alter". You will usually have to pay the landlord's costs of all this, but these costs must be reasonable.
- Landlords are however not usually allowed to charge a premium (ie a capital lump sum) for their consent. The landlord usually cannot get any rent increases in a rent review for alterations that have consent.
- On the other hand, if alterations are "unlawful" (ie without consent where consent is needed) then the landlord CAN charge extra rent if they increase the value at rent review.
- Finally, the landlord can usually insist that alterations are removed and put back at the end of the lease. The law around consent for alterations is complicated and you should get specialist legal advice.

Notice Period and Break Clause: Leases can include rights to "break" (terminate) them before the term has ended, under certain conditions. Either the landlord or tenant must give written notice of their intention to trigger any break clause. If the landlord has a right to break early this creates uncertainty for your business and your staff. Not every commercial lease has a break clause so you or your advisors should check this. See our How To Guide "Lease length, break clauses and rent reviews" for more details.

Service charges: Will you be liable for additional charges such as the maintenance of any shared spaces or grounds around the premises? Service charges may also include:

Common Area Maintenance ("CAM"): Most leases are "triple net" (meaning you pay rent, plus your proportionate share of CAM, and property taxes for the property). Maintenance charges will usually appear in the service charge clauses in the lease. The percentage of the CAM you are responsible for should be based on the percentage of the building you are renting

Capital Expenditure: In a commercial lease this typically refers to major structural expenditures, i.e. roof, foundation, HVAC (heating, ventilation, air conditioning) and other major repairs/replacements. Again, this is likely to appear in the service charge clauses. It is generally recommended that you should try to strike out the term "replacement" from any proposed lease. If at all possible, try to limit your repair obligation to a maintenance contract and for general repairs up to a certain annual maximum amount

Personal Guarantee: Many landlords insist that the directors or owners of a business personally guarantee the lease alongside their company. Guarantees are negotiable. If possible, try to avoid giving personal guarantees. If you have to give a guarantee, try to limit it, if possible, to only a portion of the lease term, say half. Before giving any form of guarantee you should always take independent legal advice.

Security measures: Check who is responsible for any security of the premises, and whether extra CCTV or other measures can be installed if needed, and who is responsible for those costs.

Get It Checked!

Finally, however straightforward a lease or rental agreement looks, always have it checked over by a lawyer. There will be a cost for this, of course, but getting it wrong can be disastrous, and far more costly.

More Information

Please see our How to Guides “Guide to Renting Business Premises” and “Choosing Commercial Premises.”

Further support

The London Growth Hub has published this series of ‘how-to’ guides to help businesses rent or buy commercial property. [This flowchart](#) will help you identify the most relevant ‘how-to’ guides for your business.



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