

Leasing Commercial Premises – some ‘ins’ and ‘outs’

Introduction

1. Like many legal matters most people underestimate the issues involved in taking on a commercial lease of a premises.
2. Likewise terminating or extracting yourself from a lease can also be fraught with difficulties and needs to be managed carefully.

Entering into a new lease

Here are some of the issues you need to consider when entering into a new lease:

1. **Defining the premises/Carparks**

It is surprising how many agreements to lease arrive without the exact outline of the premises and carparks delineated. The best way to achieve this is to attach a floor plan/carpark plan and highlight the exact areas/carparks that the tenant has “exclusive use” of.

2. **Parties to the lease**

The tenant will more often than not be a company in which case the question arises as to who (if any) will be personally guaranteeing the tenant’s obligations.

3. **Guarantees**

What guarantees are given is open to negotiation and depends very much on how strong a bargaining position both parties are in.

If directors and/or shareholders are to be included as guarantors their liability can be limited in several ways. For example:

- As to quantum eg. a sum equivalent to six months of the then current rental;
- As to time eg. the guarantee will terminate after one year after the lease commences and/or upon assignment of the lease (to a third party).

Otherwise the guarantors **will continue to remain personally liable** in the event that the third party to whom you have assigned the lease defaults (unless the lease has been renewed after you have assigned it).

4. **Term/Rights of renewal**

Generally the landlord wants the tenant to sign up for the longest term possible. However the tenant prefers shorter terms with several rights of renewal to keep some flexibility in case the tenants business is faltering and/or the tenant needs to exit the lease to find a more suitable premises.

5. **Annual rent/rent review**

A tenant needs to be wary of an artificially low rent offered by a landlord in order to “induce” the tenant to enter into the lease. What usually happens then is that upon the first

rent review the rent jumps up significantly to the "current market value" and this impacts upon the tenant's budget/cash flow.

This can be avoided by linking the rent reviews to the CPI.

6. **Alterations/Improvements/Reinstatement**

The typical lease provides that if the landlord agrees to the tenant completing alterations to the premises then the landlord is entitled to require the premises to be "reinstated" back to its original condition at the commencement of the lease. If the tenant wishes to modify or exclude this requirement then this needs to be done up front.

7. **Outgoings/Maintenance**

The payment of outgoings (also often referred to as "operating expenses" or "opex") can add significantly to the overall costs the tenant has to pay under the lease and needs to be examined carefully by the tenant at the outset to ensure the tenant understands the true costs payable pursuant to the lease.

A typical lease also provides that the tenant has to repaint the interior of the premises and replace floor coverings when "reasonably required" by the landlord. It is therefore important to negotiate any modifications to this arrangement up front.

Exiting the Lease

Some points to note when a tenant wishes to exit/terminate a lease are:

1. **Term**

The tenant will typically be liable for all obligations under the lease through to the expiry of the then current term. The nearer the lease is to expiry of the current term the better for the tenant in negotiating the exit.

2. **Reinstatement**

As set out above the tenant may be liable under the lease for the cost of reinstating the premises to its original condition and this is a cost to be taken into account when exiting a lease.

3. **Assignment**

Usually the best option is to assign the lease to a third party. While the tenant may still be liable for any defaults by that third party, hopefully that third party will be able to comply with the tenants obligations under the lease for at least a certain period of time which should bring the lease closer to the end of the then current term.

These are some of the issues that arise when a tenant is looking at entering a new lease or exiting/terminating an existing lease and legal advice should always be taken prior to entering into these arrangements.

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