

COMMERCIAL LEASES IN THE CURRENT CLIMATE

The current financial climate is not the time to be a tenant or is it? You may feel that everything is against you - rising costs, falling income and an unsympathetic landlord!

However, you may not be aware that we are currently in the strongest tenant's market for many years. Landlords are nervous of empty spaces, and if your lease contains any bargaining power at all there are a number of steps you can take.

HOW CAN YOU MAKE YOUR LEASE WORK FOR YOU?

1. Although it may provide for quarterly payments of rent, it is always worth trying to do a deal to pay monthly or even weekly. If, in the short term, cash flow is a real problem, try to negotiate a short rental holiday even if you have to accept some form of small interest charge for the delay. Interest rates are ridiculously low at the moment so the landlord will not be earning vast amounts on its investment.
2. If your business is really in trouble the landlord may be prepared (although it is not obliged) to accept a surrender, albeit possibly at a premium, if he has another prospective tenant whose covenant is much stronger and who is likely to flourish in the particular location.
3. If your lease contains a right to terminate sometime in the future you may be able to use it to your advantage in one or more ways. For example:
 - (a) You might be able to trade the right to break against an immediate reduction in the rent, which could be done by way of a Deed of Variation.
 - (b) If you are keen to stay in the premises and your lease (even with the break) has only a few years left, a further reduction in rent may be achieved if you trade the right to break against a longer lease. This would be done by an immediate surrender and re-grant. Note that in this scenario you would need to pay further Stamp Duty Land Tax (SDLT) on the grant of the new lease.
4. Even if you have no right to break but only a few years left to run at a high rent, you could offer your landlord a reversionary lease (one that starts when your current lease ends) in return for an immediate rent reduction.
5. If none of the above appeals to you but you do have the right to break and wish to exercise it, you must seek legal advice to ensure that it is exercised properly. Landlords are attacking the validity of such notices more than ever at the present time, as they are clearly anxious, if at all possible, not to lose quality tenants and have potentially unlettable space.

Therefore, if your right to break is conditional upon various matters, e.g. no material breach of covenant, you must ensure that each condition is fully met and, where breaches of repairing covenants could be involved, be sure you ask your landlord in good time to carry out his dilapidations inspection so that you have enough time to do any necessary works before the break date is reached.

ADVICE NOTE

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6. If, notwithstanding the current climate, you are a prospective tenant seeking new space, be aware of the following points of negotiation:
 - DO NOT agree to pay the landlord's costs, either on the new lease or in connection with any consent which you require for fit out works.
 - DO try to agree a rolling break, i.e. a right to determine at any time after a certain date. Ensure that such a right is unconditional or, at most, conditional upon payment of the rent and vacant possession.
 - DO try to negotiate a substantial rent free period or contribution to fit out, although there are potential VAT issues so you would need to seek your accountant's advice in this respect.
 - DO avoid a long term if you can. A short lease with an option to renew will spread the SDLT burden as this is assessed on the level of rent as against the number of years. Therefore, the shorter the lease the less the tax. However, note that if the lease is renewed, a further payment of SDLT will be due on such renewal unless both leases are under the threshold for payment.
 - DO NOT agree to quarterly rent if you can avoid it. Monthly is better.
 - DO NOT agree to a full repairing obligation if you have a short lease. Agree a schedule of current condition with your landlord and limit your obligation to keeping the premises to that standard and no more.
 - DO try to negotiate a rent review which can go down as well as up.
7. If you are a larger operator and need some short term space, many of the larger landlords will actually agree to a tenancy at will, i.e. a right to use the space subject to payment of rent but with no commitment on either side to stay or be allowed to stay. Landlords may agree to this if the space would otherwise be unused.

Above all, if you are in trouble speak to your landlord sooner rather than later. It may be possible for new arrangements to be worked out.

If you would like any further information relating to any of the above, please contact Susan Scott on 01306 502960 or s.scott@downslaw.co.uk.