

Business Leases - Guidance to Tenants

Business leases come in many shapes and sizes. Some are short and some are long. Some carry heavy responsibilities for the tenant while others are intended to be “easy come/easy go”. These notes are intended to answer some common questions for anyone thinking of taking on business premises.

Repairing obligations in Leases

FRI Lease

The lease will regulate the responsibility for undertaking repairs as between landlord and tenant. The ideal scenario for a landlord is to grant a “fully repairing and insuring lease” under which all responsibilities to undertake repairs are passed to the tenant.

Where the tenant agrees to take a full repairing lease it would normally be appropriate for the tenant to have a report from a building surveyor who will be able to advise the tenant of the likely liability that may be to undertake repairs during the life of the lease and as to any existing defects.

What is disrepair?

Under English law the obligation to “repair” extends not only to keeping the property in the condition it was in when the lease was taken but also to making good any existing disrepair so that the landlord can require the tenant to hand over the premises in full repair when the lease comes to an end. The landlord is entitled to exercise his right to serve a schedule of dilapidations when the lease ends. This can prove to be an expensive exercise for the tenant who may have to bear not only the cost of the repairs but the landlords surveyors and legal fees as well.

Internal repairing leases

Some leases –typically of shops - are granted as “an internal repairing lease”. In this case the tenant is responsible for undertaking internal non-structural repairs and for repair and maintenance of the shop front but will not be responsible for the structure of the building. However, the tenant may be obliged to contribute towards the maintenance of the structure via a service charge formally set out in the lease or the informal obligation to contribute towards the maintenance and repair of items shared in common with the landlord or other tenants.

Schedule of condition

Where the tenant agrees to be responsible for repairs but not to put the property into any better state than it was in when the premises were first leased then it would normally be necessary for a schedule of condition to be prepared. For small properties it may be appropriate for the tenant to take a set of photographs recording existing defects and to prepare an accompanying note listing those defects. A duplicate set of photographs and notes is then incorporated in the landlord’s part of the lease so that both parties agree the condition of the building when the lease was taken. For more substantial accommodation it would normally be appropriate to employ a building surveyor to prepare a detailed schedule with photographs to be agreed by the landlord’s surveyor.

Asbestos – effect on tenant’s responsibility

The Control of Asbestos at Work Regulations 2002 came into force in 2004 and requires every person who has any obligation to maintain non-domestic premises to determine the nature and extent of asbestos present within that building.

In order to comply with the requirement the tenant will need to commission a report and to act upon its recommendations. The report might indicate that although there is asbestos present within the building it needs merely to be managed rather than removed. Alternatively, the report may state that the asbestos is hazardous and should be removed by specialist contractors at considerable expense.

These regulations apply to existing leases and to new leases. Where a new lease is being taken it would normally be appropriate to enquire whether a report has been undertaken previously and, if not, to attempt to limit the tenant’s responsibility to deal with asbestos. If this is not done the lease will normally contain provisions requiring the tenant to comply with statutory obligations leaving the landlord free to require the tenant to obtain a report shortly after moving in.

Failure to comply with the regulations is a criminal offence.

Other issues**Inclusive rents**

These are usually only found in a short lease of part of larger premises. The rent may include the cost of maintaining the building as a whole, the cost of heating and lighting, insurance and rates. Where the rent is “exclusive” the landlord will collect these expenses in addition to the rent.

Break clauses

Break clauses are often negotiated before the lease is granted to enable the tenant or the landlord (or sometimes both) to have the right to end the lease on the giving of notice in writing. Typically 6 months notice is to be given. Where a shorter period of notice is required the tenant is often obliged to pay a penalty of additional rent on top. Time limits for service of notice to end the lease are strictly construed by the courts and the mechanism for serving notice should be carefully considered when the lease is granted to ensure that the tenant is fully aware of what will be required if the tenant wishes to serve the notice at the appropriate time.

The right to break is sometimes linked to rent review but there is no automatic right to end the lease when the rent is due for review and any break clause must be individually negotiated.

Rent review

Most business leases will incorporate a rent review if they are granted for more than, say, five years. The landlord will be entitled to an uplift in the rent if market rents generally have increased. Occasionally there is an automatic uplift in line with RPI but the usual rent review clause requires a comparison to be made with other similar properties and recent lettings in order to establish if there has been a rise in the market. Rents of some types of accommodation have been fairly static for some years and sometimes the market goes down. It would be unusual for a tenant to be able to secure the right to a downward review if this should happen. When the parties are unable to agree on the rent to be paid there is normally a mechanism to refer the decision to an independent surveyor.

Stamp Duty Land Tax

This tax is payable when a new lease is granted. The tax is paid by the tenant and is due within 30 days of completing the lease or having occupation under an agreement for lease if this is earlier.

The tax is due if the Net Present Value of the leased property exceeds £150,000. Tax is then payable at 1% of the excess. Unfortunately the calculation is complex and requires adding all the rent and VAT payable for the term together and then applying a discount for each year. The formula is so complex that a calculator is provided by the Inland Revenue website to enable the NPV to be calculated. The longer the lease the more the tax will be.

Protection available to tenant of a lease of premises used for business purposes

The Landlord and Tenant Act 1954 protects tenant of business premises as it provides that a tenancy of business premises can only be ended by not less than 6 nor more than 12 months notice either by landlord or by tenant regardless of what is written in the lease.

When the landlord serves notice to end the lease he must state whether or not he is willing to grant the tenant a new lease. If the landlord is not willing he must state one of the statutory grounds available to him. Provided that the tenant has observed his obligations under the lease the landlord will need to be able to show that he intends to demolish or reconstruct the premises in some way or occupy himself. Where this ground is shown the tenant is entitled to compensation equivalent to the rateable value of the premises or more where the tenant has occupied for a lengthy period.

“Contracted out” leases

Where the landlord is not willing to grant a lease having the protection of the 1954 Act the landlord may give the tenant notice that the lease will not be protected. The notice must be given before the lease is granted and the tenant must acknowledge the notice by making a declaration in a specified form. Once this has been done the lease will not be protected and the tenant will be required to vacate the premises when the lease ends.

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Note: The contents of this fact sheet are true to the best of our knowledge. We hope you find them useful. However, they do not constitute legal advice and you should consult a qualified lawyer before proceeding further.