



COMMERCIAL LEASES

GENERAL

A lease is an agreement between landlord and tenant setting out the terms and conditions under which a property is let. The landlord owns the property and most commercial leases contain standard clauses which govern the relationship between Landlord and Tenant. In the current climate it is possible to negotiate terms with a Landlord which may be favourable to the tenant. The principal terms relate to rent, rent reviews, obligations to maintain and repair, insurance, payment of outgoings, guarantees, the term of the lease, option to terminate and user of the premises.

There is no completely standard common form of lease of commercial property. Each lease of property needs to be examined to identify potentially difficult clauses and to adapt to the requirements of the Tenant. A Lease may be new in which case it is negotiated directly with the Landlord, or a prospective tenant may take an assignment of an old lease from an existing tenant. Sometimes a sum of money called 'key money' is paid if the property is in a desirable location. There is little or no scope for negotiation of terms with the Landlord if the Lease is an assignment of an old lease as the landlord is not a party to the assignment (other than to give consent to the transaction proceeding if satisfied with the commercial standing of the new tenant). Older leases or poorly drafted leases may not contain all the clauses typically found in more modern leases and may impair the value of the investment by exposing the landlord or the tenant to hidden risks or by failing to give him the rights he would expect.

1. RENT REVIEWS - UPWARDS ONLY RENT REVIEWS.

The form of commercial lease found over the last 25 years is almost invariably an upwards only market rent lease, with five yearly rent reviews. Section 132 of the Land and Conveyancing Law Reform Act, 2009 (the "2009 Act") prohibits the long established practice of rent review clauses in commercial leases containing provisions for static or upwards only rent reviews. It applies to all new commercial leases granted on and after 28th February, 2010. Therefore as and from 28th

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February, 2010, all new commercial leases which provide for a rent review allow the rent on review to be greater, less or equal to the then passing rent, notwithstanding any wording in the lease to the contrary.

However, existing commercial leases (i.e. those in place prior to 28th February, 2010) are not subject to this legislation and, as such, the legal rights and obligations of landlords and tenants of these older leases remain unaffected. Tenant's of older leases containing upwards only rent reviews will find it difficult to assign these leases as such leases could be viewed as less attractive by potential incoming tenants in the market.

In Leases of ten years or more, five year rent reviews are standard. The standard rent review clause involves resetting the rent based on market value at the review date. However, other forms of increase may be offered as an alternative. A rent based on percentage of turnover of the tenant's business may be found in leases of shops in premium locations. Another more unusual rent review clause is one that links rent increase to the increase in a specified index such as the consumer price index.

The most common provision in a Lease is for "open market rent" reviews.

The process is that the parties endeavour to negotiate and if they are unable to agree the rent, it is referred to an independent valuer or surveyor who will decide the rent and his decision is binding on the parties. The property is valued on an open market rent basis on the assumption of a hypothetical new lease between a willing landlord and tenant with no premium. The wording of the rent review clause is critical. In the case of older leases, it may be that the wording has hidden traps for landlord and tenant on rent reviews.

2. TERM OF THE LEASE.

Over the last few years terms have fallen from the classic 25 year terms of the past to 10 or 15 years or even less. Even then, tenants are insisting on break clauses being included. Therefore short flexible lease terms are becoming more common. If the term is less than 5 years the tenant will be obliged to vacate at the end of the term unless the landlord negotiates a new term. If the term exceeds 5 years then the tenant acquires 'Landlord and Tenant rights to renew the Lease indefinitely. However it is common for Landlords to require the tenant, before commencement of a lease term, to waive these rights.

3. OBLIGATION TO REPAIR AND RENEW - THE MAINTAINING AND REPAIRING TRAP.

In a Lease with a term exceeding 5 years, there is usually a full repairing and insuring responsibility on the tenant so that repairing and insuring costs are paid or reimbursed by the tenant over and above the rent. Care has to be taken at the outset to do a survey of the property and to agree with the landlord that this duty to repair and renew will not go beyond the condition

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of the building as it stands at the commencement of the Lease. Otherwise the tenant may find himself having to carry out improvements such as replacement of a roof, floors, windows etc that have become dilapidated. A photographic survey will prove the state of the building when the Lease commenced. A tenant taking on an assignment of an existing Lease does not have this option open to him and should never take on a Lease of a building in poor condition unless the Landlord agrees to vary the repairing and insuring obligation in the Lease. However there is no incentive for the Landlord to do this where an old Lease is being assigned to a new tenant.

4. LANDLORD AND TENANT ACT RIGHT TO RENEW -THE RENUNCIATION OF TENANT RIGHTS.

A tenant who remains in possession with the consent of the Landlord for in excess of 5 years may renew the Lease upon expiry of the term even if the Landlord is not in favour of that tenant remaining in possession.

Since 2004 it has been considerably easier for parties to “contract out” of Landlord and Tenant Act rights. Accordingly contracting out now or ‘Renunciation’, happens in most cases. When the renewal right is contracted out or renounced, the tenant will not have the right to a new lease at the end of the lease term or period.

5. BEWARE THE PERSONAL GUARANTEE.

Guarantors are very commonly required by landlords in leases. This is because the original or incoming tenant may not have the financial strength by itself to perform the obligations in the lease. Frequently, a group company takes a lease but a “head” company, with more financial strength and depth will guarantee the performance of the tenant’s lease obligations. In the case of smaller companies it would be common that the directors or principal shareholders are required to guarantee the performance of the tenant’s lease obligations. A tenant should always restrict the terms of a guarantee. A Landlord may agree that the guarantee will last of only the first few years of the term only. Alternatively a deposit may be accepted by the Landlord instead of a guarantee. Another form of limitation is to agree a rolling guarantee for the term of the lease but with exposure at any one time to one years rent and outgoings.

6. INSURANCE FOR THE UNWARY.

The tenant is usually responsible for the cost of insurance to cover:

- Normal perils such as damage by flood and fire etc;
- Tenants public liability and employers risks;
- Damage to plate glass windows;

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- Loss of rent for three years.

The tenant will be obliged to take out his own policy to cover the tenant's risks and will reimburse to the Landlord the cost of the landlord's policy covering his risks. It is therefore important to ascertain the cost of insurance before taking on the Lease and if possible to get all the risks insured with the one company to avoid duplication or overlapping of the policies and to make the job of processing a claim easier if there is a problem.

7. OPTION TO TERMINATE.

The term or duration of a lease is a matter for negotiation between the landlord and tenant and their agent. Because of the ease at which landlord and tenant rights can now be waived by the tenant (that is the right of the tenant to remain in possession after a period of five years occupancy has elapsed), the term or duration of the lease is commercially significant. The term will be relevant to both landlord and tenant, in that the tenant will be obliged to quit the premises unless he negotiates a longer term. Break options are a matter of agreement. They can allow for either the landlord or tenant to terminate the lease on particular dates. They usually kick in after an agreed period of time has elapsed such a one yeat, three years etc. Some are expressed to be personal and can only be exercised by the original tenant. Some will be free options or some may require an payment of a sum of money to the landlord representing for example three months or six months rent. Generally they can only be exercised if the tenant is compliant with its obligations under the lease and the rent is paid up to date. A variation on a break is an option to renew. They are not often found in leases because there may already be a statutory right of renewal. A tenant starting up a new business will seek to agree a short term of say three years along with an option to extend the term if the business is successful.

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