

Commercial Leases – A Landlord’s Guide

Introduction

This guidance sheet has been prepared to assist you in understanding the stages involved in letting commercial property. A flowchart showing the steps in the process is attached.

Heads of terms

Heads of terms setting out the main terms of your agreement with the tenant should normally be agreed at the outset. Once these have been agreed it is usually difficult to change anything later in the process. For this reason we recommend you involve us at an early stage and ask us to comment on them before they are finally agreed. Heads of Terms must always be marked “subject to contract”. They should deal with:

- the extent of the property included in the lease and any additional rights the tenant may need over other property e.g. for parking or for access
- the tenant’s proposed use
- the amount of rent and whether it will be changed at any time during the lease (known as a rent review)
- the length of the lease
- any rent free period or incentive for a tenant to take the lease
- whether the lease will be protected by the Landlord and Tenant Act 1954 (see **Landlord and Tenant Act 1954**)
- any rights to end the lease early (known as break clauses)
- whether you require any rent deposit from the tenant as security for payment of the rent and compliance with other conditions and the terms on which it will be held
- the tenant’s repairing obligations. These may be limited to a schedule of condition (see **Condition of Property**)
- any alterations the tenant may wish to make to the property or signs the tenant want to put up
- whether the tenant may transfer the lease to another person or may sublet
- whether the tenant will have to pay any of your costs

Landlord and Tenant Act 1954 (“1954 Act”)

The 1954 Act gives certain tenants the right to a new lease once the originally agreed term comes to an end. You may not want the Tenant to have this right and should consider whether the operation of the 1954 Act should be excluded from applying to the lease.

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Service charges

If you are letting part of a property, there are likely to be shared facilities which will need to be maintained by you or someone on your behalf. In order to recover your costs, you should require the tenant to pay a service charge. The tenant will almost certainly ask what the likely cost is going to be, and you should prepare an estimate of the annual costs of maintenance and consider whether any major expenditure is anticipated over the next 12 months or whether a sinking fund (i.e. a reserve fund) is required to build up funds to cover major items of expenditure if these are anticipated.

Insurance

Generally the landlord will insure the property and pass the cost onto the tenant. It is usual for the landlord to insure for loss of rent to protect his income for any period where rent is not payable because the premises have been damaged or destroyed. The cost of insurance is normally passed on to the tenant through the service charge. The tenant will be responsible for insuring his contents and possibly any plate glass at the property.

Minimum Energy Efficiency Standards (MEES)

You will need to have an Energy Performance Certificate (EPC) for the property when you market it for rental and it is advisable to double check the rating that has been given to the property. Landlords cannot lawfully let a property that has a rating lower than E unless they have registered an exemption and from 1 April 2023 will not be able to continue renting a commercial property that has a rating lower than E.

It should be noted that with the commitments the UK has made to meet Net Zero targets by 2050, that EPC ratings of C will be required by 1 April 2027 and B by 1 April 2030. This is a significant increase and it is likely that you need to factor in when and how to carry out improvement works to the property. If the lease term will extend into 2027, it may be advisable to carry out any necessary works before the tenant is granted occupation.

Condition of property

The property will be let in its present condition and the tenant will normally become responsible for keeping it in good repair and condition including making good any existing disrepair. This will also include an obligation to repair fixtures and fittings, such as sanitary ware. The tenant may negotiate a limited repairing obligation particularly if the lease is only for a short period. This is often done by preparing a schedule of current condition of the property which is attached to the lease and the tenant agrees to keep the property in that condition. If you agree to this you should consider asking the tenant to pay the cost of preparing the schedule and you must carefully review the schedule's contents before you approve it.

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Agreement for lease

An agreement for lease may be necessary in certain circumstances. For example you may have agreed to carry out work to the property before the lease is granted or planning permission may need to be obtained. An agreement will ensure both landlord and tenant are legally committed to the transaction before any expense is incurred. It will also set a completion date.

The Lease

We will prepare the lease based on the heads of terms. The tenant's solicitor will review the lease to see if it is acceptable from a tenant's point of view and reflects the heads of terms. If any changes are suggested, we will negotiate these with the tenant's solicitor. If there are any matters that cannot be agreed and that you feel strongly about, we may ask you to try to negotiate with the tenant directly to save time and costs.

Licence for alterations

You should consider whether you want to limit the works and alterations that the tenant can make to the property. If so the lease can require your consent before any alterations are made. If your consent to any alterations is required, we will prepare a licence for alterations which will impose obligations on the tenant when he carries out the works. These obligations can include a requirement for the tenant to reinstate the property when he leaves and to pay your legal costs for preparing and agreeing the licence.

Rent deposit deed

If a financial deposit is required from the Tenant as security for payment of the rent or complying with any other of the lease terms, we will prepare a deed setting out when and how the deposit can be used. This money will be the property of the tenant but it is usually held in a separate account. Normally, notice must be given to the tenant following any withdrawal from the deposit.

Information about the Property

We will review your title to the property to ensure that you are entitled to grant the lease and advise you should you need consent from any lender. We will ask you to prepare replies to standard enquiries used in letting transactions and reply to any further enquiries about the property raised by the tenant's solicitor. We will also assist in preparing a pack of information for the property that the tenant's solicitor is likely to require including for example, any asbestos reports, fire risk assessments, planning documentation, information relating to the VAT tax status of the property.

Documents for signing

The documents will be sent to you to sign with our reports summarising their contents. The fact that you have signed the documents will not bind you until they are completed.

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Completion

We will respond to any pre-completion questions raised by the tenant’s solicitors. On completion the tenant will be required to pay any sums immediately due under the lease and we will send you a financial statement. Until we confirm completion you should not enter into any financial or other commitment relying on the lease being granted.

Further information

This information sheet highlights some of the key issues involved in granting a lease of commercial property. It is intended to be for general guidance only and is not a substitute for specific advice. It is based upon our understanding of the law as at October 2021 and may be affected by subsequent changes to the law. For more information, please contact Sarah Easton on 01892 510000 or email at sarah.easton@ts-p.co.uk.

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