

A BASIC PRIMER ON COMMERCIAL LEASES FOR TENANTS

There are many important things for a would-be tenant to consider when negotiating a commercial lease. This article will outline a few of those things that in my legal practice seem to be more central than others.

The first thing is whether your proposed lease is a gross lease or a net lease. You want a gross lease.

In a gross lease you pay one regular, fixed, monthly rent to the landlord and that's it.

In a net lease you pay a fixed, monthly base rent and then, on top of that, you pay a further monthly additional rent, being a fixed percentage of all the costs the landlord incurs in relationship to his ownership and operation of the rental property, such as property taxes, insurance, utilities, minor and major repairs.

The main problem with a net lease from the tenant's perspective is that he never really knows for sure what his final rent costs are going to be. If the landlord suffers some extraordinary costs in relation to the rental property, such as a roof replacement, a parking lot re-paving or a foundation leak, he passes these costs on to you, the tenant, as additional rent.

The best way to handle the unpredictability and financial risks inherent in a net lease is to negotiate a cap or ceiling on the amount of additional rent you may be called upon to pay in any year of the term. In this way you will attain financial predictability.

Read the indemnity and insurance provisions in the proposed lease carefully. Most landlords try to contract out of their legal responsibility to you in circumstances where their negligence might have caused injury to your person or property, or the persons or property of your staff or customers.

Don't sign a lease without having your lawyer or insurance broker read the indemnity and insurance provisions and approve them.

If you want an option to renew the lease, make sure it's a true option and not a phony one. You may be intending to spend a lot of money on leasehold improvements and, if your business goes well, you will want to exercise the option to renew in order to, amongst other things, amortize the cost of those improvements over the longer combined term.

A true option is one where the rent for the renewal term is agreed to in advance in the original lease, or where there is an agreed-to method or formula for fixing the rent in the renewal term if agreement cannot be voluntarily reached; the basic idea being that the tenant is guaranteed security of tenure for the initial term, plus, if he wants it, the renewal term, and that he will pay no more than market rent in the renewal term.

A phony option to renew is where the renewal provision merely states that the rent for the renewal term will be "as agreed to" by the parties at renewal time.

What if the landlord secretly wants you out? He just won't agree to a reasonable rent, he will demand an extortionate rent for the renewal term which you won't agree to and you'll end up having to go, leaving your expensive leasehold improvements behind.

Some leases make a tenant's right to assign or sublet completely dependent on the landlord's whim. You don't want this. You may want to sell your business or re-locate during the term of the lease. You need to know that in this eventuality you can transfer your lease to the purchaser of your business or to whomever else you may want to transfer it to. The wording you are looking for gives you the right to assign or sublet, "subject to the landlord's approval, which approval will not be unreasonably withheld". In this scenario, basically, the landlord must approve so long as the proposed assignee or sublessee is creditworthy.

Finally, if the premises you are renting are in a multi-unit building, and you don't want any other tenant in the complex competing with you, then insist on a clause in the lease prohibiting the landlord from renting out any other unit in the complex to anyone who carries on a similar type of business to yours.

The actual operation of leases is more complex than it seems and can involve some unhappy surprises for tenants. Before you sign any lease agreement have it reviewed by a lawyer with experience dealing with commercial leases.