

A Guide to Renting Business Premises

Business Information Factsheet
BIF010 · December 2016

Introduction

Renting business premises involves entering into a lease, or a licence to occupy the premises, with the owner of the property or landlord. A lease is a legal document issued by the property owner or landlord that gives a business the exclusive right to occupy premises as a tenant for a fixed term, in exchange for the payment of rent. Some commercial premises are available on short-term, flexible 'licence to occupy' arrangements that provide 'easy-in, easy-out' terms.

This factsheet outlines what is involved in agreeing a lease or a licence to occupy. It explains what terms and conditions a lease agreement should cover, what the process of agreeing a lease entails, the costs incurred when renting premises for the first time and issues arising on termination of the lease.

This factsheet does not include information about finding or choosing premises, which is covered in BIF057, Choosing Commercial Premises. It does not cover managed workspace, which is explained in BIF397, An Introduction to Managed Workspace.

Licences to occupy

A licence to occupy is a flexible short-term agreement that enables a business or organisation to occupy premises on 'easy-in, easy-out' terms that often require only one month's notice to quit from either party. An upfront payment of one month's rent plus a refundable deposit equivalent to a month's rent is usually payable, making it an economical way of renting premises on a flexible basis.

A licence to occupy does not grant exclusive occupation of the premises, which means it is not possible to exclude the landlord and third parties from occupying parts of the premises. A licence to occupy is often appropriate for new business start ups and organisations who are unsure about the length of time they wish to occupy the premises. For example, it is useful for concessions in department stores or for renting short-term office space.

A licence to occupy differs from a lease in that a lease typically provides the tenant with exclusive possession of the premises and specifies a fixed period. If the agreement does not provide a fixed period for occupation, or does not provide exclusive possession to the tenant, then it is likely that the agreement is a licence to occupy the premises.

Lease agreements

The purpose of a lease agreement is to set out the rights and obligations of both the landlord and tenant. The lease should provide the landlord with the security that a tenant will adhere to certain covenants (promises). The lease should also provide the tenant with assurances that the

terms of the lease are not too restricting and that they will be able to carry out their business activities as necessary from the premises.

The terms usually covered in a lease agreement include:

- **Lease term.** This may be between three and five years, but can be longer, with some as long as 25 years or more. It can be more difficult to agree a short-term lease, depending on the state of the commercial property market at any given time.
- **Notice period to terminate the agreement, including break clauses.** These clauses allow the tenant (or the landlord, depending on the agreement) to terminate the agreement early, after a specified length of time. For instance, there may be a break clause in the agreement that allows the tenant to terminate a six-year lease after three years. However, the tenant or landlord must give notice of intention to enforce the break clause, and may have to comply with certain conditions to be able to do so. Not every commercial lease will include a break clause.
- **Value of the rent and review dates.** Rent may be charged monthly or quarterly in advance, and may be subject to VAT. It may also be subject to periodical rent reviews. It is important to check whether any rent increases will be linked to changes in the commercial property market and whether it is possible for the rent payments to fall as well as rise (although most leases contain upwards-only rent reviews) as a result of these periodic reviews.
- **Insurance obligations.** It should be clear who is responsible for insuring the premises. If the landlord insures the premises, they may pass on this cost to the tenant via a service charge in addition to the rent.
- **Access rights.** Does the tenant have access to the premises at all times? How do they access the premises? Are there any rights of access reserved to the landlord? Is access provided to any shared areas in a multi-let building?
- **Repairs and renewals.** What responsibilities does the tenant have for maintenance and repairs to the premises?
- **Decorations and signs.** The tenant may need to seek the landlord's permission for any signs they want to install at the premises. There may also be local restrictions and planning regulations (see **Obligations as a tenant**, below).
- **Service charges.** The tenant may be charged an additional fee for shared services provided by the landlord, such as maintenance of the grounds around the premises and any shared parts of the building.
- **Sub-letting and assignment.** Sub-letting involves a tenant leasing all or part of the premises to another tenant. Assignment involves a third party taking over the full lease agreement. It is important to check the lease agreement to see if either of these options is allowed.
- **Security measures.** A lease agreement usually specifies who is responsible for the security of the premises and whether extra security measures, such as CCTV cameras and physical barriers, can be installed if required.
- **Use.** A lease agreement will usually stipulate the purpose for which the premises can be used. It is important to check whether there are any restrictions on use and that the landlord

has the correct planning consent to use the premises in the way the tenant requires before signing the agreement.

- **Provision of services.** The agreement should specify who is responsible for services and other utilities such as water and broadband connectivity. It should specify who is responsible for installing, maintaining and paying for such services.

The process of agreeing a lease

The process of agreeing a lease can be divided into three key stages:

- **Agreement of Heads of Terms.** This is a summary of the agreement between both parties in the potential lease agreement. Solicitors use Heads of Terms to produce the formal lease.
- **Lease negotiations.** When negotiating a lease the tenant should ensure that they understand every term used by the landlord and that they are clear about the full extent of the cost of leasing the premises and their responsibilities under the lease.
- **Signing of the lease.** The lease, once signed, is a legally binding document. A solicitor should review it thoroughly and explain its terms before it is signed by the tenant.

Obligations as a tenant

Once a tenant has signed the lease, the landlord will expect them to adhere to the terms and maintain the integrity of the property. While occupying the premises the tenant has a duty to care for them and maintain them to a reasonable standard. The lease agreement should provide details of how often the landlord or their authorised agents can inspect the property internally. Tenants should be given notice of an inspection and they should be entitled to be present throughout.

A tenant's obligations also include making sure that the premises are adequately insured (unless this is the landlord's responsibility), payment of business rates and complying with health, safety and fire regulations. There may be specific clauses in the agreement about waste and rubbish disposal, not interfering with neighbours' access, air and light, etc.

Many commercial landlords require that tenants restore the premises back to their original condition when leaving. For example, there may be specific instructions about repainting the premises in a neutral colour or selecting materials of the landlord's choosing. It is important to ensure that the costs involved in reinstating the premises at the end of the lease have been budgeted for.

There will be a limit to what a tenant can do to the outside of a building. Restrictions may be made under local planning regulations and, if the premises are in a conservation area, external signs and appearance may be subject to specific planning consents.

It is also important to check whether change-of-use planning permission will be required in order to operate certain types of business from the premises. See BIF031, A Guide to Applying for Planning Permission, for more information.

Maintenance and repairs

Tenants are obliged to maintain and repair certain aspects of the premises. These obligations can be split into three stages:

- **Before moving in.** The premises should be in a suitable state of repair. If they are in poor condition, or if the obligations to repair the premises during the term of the lease are strict, it will be necessary to prepare a photographic Schedule of Condition prior to signing any lease agreement. A Schedule of Condition provides a record of the condition of the premises before the lease is entered into and is vital to prove the original state of the premises when the lease comes to an end.
- **During the lease.** It is important to be aware of the tenant's responsibilities regarding repairs once they occupy the premises.
- **The end of the lease.** The property must be left in an acceptable state of repair. The tenant may be served with a Schedule of Dilapidations, itemising repairs that must be carried out. Allowances should be made for fair wear and tear. If a Schedule of Condition is in place this is the starting point for comparison of the premises' condition at the start and the end of the lease.

If the entire premises are leased, the landlord may expect the tenant to take full responsibility for all repairs (including structural). In this case, it is advisable to have a survey carried out and to have any defects remedied before signing the lease. It may be possible to negotiate an upper limit to the contributions made to the cost of repairs, or to include this in the rent.

Rights as a tenant

The purpose of renting the premises is to run a business enterprise. A tenant is entitled to use the premises in any lawful way they choose in order to promote and carry out their business activities. The lease agreement should provide for them to do so without undue interference, and to maintain the security and privacy of their business.

A tenant has a right to lay out the premises as they think appropriate for their trade, as long as they are not contravening the terms of the lease.

They should be free under the agreement to rearrange the internal space as they see fit. They should be able to make temporary divisions of the space while not interfering with the fabric of the building or destroying fixtures and fittings. If they intend to make radical changes to the appearance of the interior, they will probably need to get their landlord's approval for the alterations before undertaking the work. They may also need to seek approval under the Building Regulations 2010 and obtain any required planning permission. See BIF005, A Guide to the Building Regulations 2010, for more information.

The Commercial Landlords Accreditation Scheme (CLAS) promotes good practice in the commercial property industry. Landlords are awarded the CLAS scheme Standard Mark and agree to follow a code of practice. Go to www.clascheme.org.uk for more information.

The Landlord and Tenant Act 1954 provides that most business tenants have a legal right to renew their leases (known as security of tenure).

The Code for Leasing Business Premises in England and Wales 2007 promotes fairness in commercial leases, and recognises a need to increase awareness of property issues, especially among small firms. Go to www.leasingbusinesspremises.co.uk for more information.

Costs to expect when renting business premises

- **Rent and rates.** An initial deposit may need to be paid as security (which could be up to six months' rent) and the tenant is responsible for ensuring that rent is paid on time each quarter or month. Business rates vary according to the local area. See BIF061, An Introduction to Business Rates, for a detailed explanation of business rates.
- **Service charges.** These apply to multi-occupied buildings. The landlord usually pays for common costs, such as structural repairs, common areas, heating and a caretaker. This cost is recharged to tenants on a proportional basis (normally a ratio of floor areas). Tenants should ensure that the basis of the calculation is stated, that they have the right to check the landlord's expenditure and that they are not paying for any empty areas in the premises.
- **Legal fees.** The lease agreement may be in a standard format but it should still be checked by a solicitor to ensure that it fits the tenant's business requirements. Money spent on professional advice at this stage can prevent expensive legal disputes.
- **Installation of landline telephones and broadband connectivity.** The cost of installing telephone and broadband should be budgeted for, especially if the business has specific requirements for high-speed broadband or high bandwidth.
- **Insurance premiums.** It is important to know in advance exactly what needs to be insured. This may be limited to the contents of the premises but the tenant or landlord may require more comprehensive insurance cover to protect their business, including cover for business interruption in case the premises are damaged by fire or flooding. The buildings insurance premium is usually paid by the landlord and then recharged to the tenant. See BIF006, Insurance Cover for Business, for further information.
- **Legal compliance.** If the premises are being opened up to the public for the first time, they must comply with relevant regulations covering accessibility and health and safety before a business starts trading. This may involve costly modifications so it is vital to check whether these adjustments are the responsibility of the tenant or the landlord.
- **Internal furnishings and fittings.** If furniture and fittings are not provided it will be necessary to budget to furnish the premises and to install any fittings or signage.

Termination of a lease

It is important to check that if the tenant wishes to vacate the premises before the lease period ends, the terms of the agreement allow the tenant to terminate the lease, to sub-let to another business or to reassign the lease to another tenant.

The lease will define the minimum period of notice to terminate that the tenant must give to the landlord, but the wording of the termination clause must be checked carefully. The tenant or the landlord may be able to terminate with a period of notice, but under some commercial leases this is not possible.

In some cases, the tenant must agree to pay the rent for a minimum of six months or one year, even if they choose not to occupy the premises for the full term of the lease. There is usually a minimum deposit payable of a number of months' rent, which may not be refundable if the tenant terminates within that time. The termination clauses within commercial leases can vary significantly so it is important to take legal advice before signing a lease, and when considering termination.

There may also be circumstances in which the landlord can terminate (forfeit) the tenant's interest in the premises. These situations occur when a tenant has failed to adhere to their obligations under the lease, such as illegal use of the premises or failure to pay the rent on time. A tenant has the right to apply to the court for the landlord's termination to be set aside by remedying the breaches of the lease.

Once a tenant has given notice of their plans to leave the premises, the landlord will visit the premises and prepare the Schedule of Dilapidations. The tenant may choose to carry out any necessary repairs themselves, or allow the landlord to carry them out and charge for the work. The schedule may also require the tenant to empty the premises of all equipment, remove any alterations, clean the premises and arrange for qualified contractors to test and service any gas and electrical installations such as fire alarms and emergency lighting.

Hints and tips

- It is important to plan ahead to identify the timescales and costs associated with moving into new premises.
- The landlord is likely to require a financial reference and may ask the tenant for personal guarantees to cover the rent payments. A returnable deposit may be an alternative to providing a personal guarantee.
- It is essential to check all obligations under the lease, especially any restrictions on alterations that can be made to the interior and exterior of the premises
- If changing the use of the premises, the tenant may need planning approval from the local authority before signing a lease agreement.
- Legal advice should always be taken when reviewing the terms of the agreement.
- Every commercial agreement is different and, while some common terms appear in most leases, every agreement should be reviewed on its own merits.

Further information

BIF006 Insurance Cover for Business
BIF019 A Guide to Commercial Mortgages
BIF031 A Guide to Applying for Planning Permission
BIF057 Choosing Commercial Premises
BIF061 An Introduction to Business Rates
BIF397 An Introduction to Managed Workspace

Useful contacts

The British Property Federation (BPF) is a membership organisation that represents property owners and investors. It operates the Commercial Landlords Accreditation Scheme (CLAS).

Tel: (020) 7828 0111

Website: www.bpf.org.uk

The Royal Institution of Chartered Surveyors (RICS) represents the property profession and sets, maintains and regulates standards in the industry.

Tel: (024) 7686 8555

Website: www.rics.org/uk

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