


Occupying commercial premises in central London – what's the deal?

LONDON IS STILL THE BUSINESS CAPITAL OF THE WORLD EVEN THOUGH THE CONGESTION CHARGE HAS BEEN EXTENDED TO THE ROYAL BOROUGH OF KENSINGTON & CHELSEA.



The competition for space in the centre has pushed rents up to unprecedented levels in the West End, with over £100psf reportedly being achieved on some small lettings. Even the City office market is back on track with rents reaching £62.50psf, at last approaching the 1989 peak of £70psf. Unless you buy a freehold – and central London commercial property prices are historically very high at the moment, driven by this strong rental growth – it is likely that your premises will be let to you on a lease. English rack rent leases (leases without a premium value because they are granted at the open market rent) are usually granted on “FRI” terms. “FRI” means “full repairing and insuring”, the idea being that the landlord does not have to spend any of the rent on maintaining or insuring the premises. These obligations are passed to the tenant by the terms of the lease.

Other key provisions in a commercial lease are:

- **RENT REVIEW.** If the lease is for a term of more than five years, it is likely that there will be a rent review at the end of the fifth year. The effect of this is to return the rent to the market level. Rent reviews are usually upwards only, so even if rents have fallen in the meantime, the rent will not go down. Some landlords prefer indexation by reference to one of the indices published by the Government – usually the Retail Prices Index.
- **ALTERATIONS AND STATUTORY REQUIREMENTS.** The landlord will invariably keep a close control over the tenant's ability to alter the premises. If the premises are to be used for the sale of alcohol, the licensing laws will also have an impact on the tenant's ability to change the layout of the premises. Other statutory requirements – health and safety, disability discrimination and fire regulations – will also fall to be dealt with at the expense of the tenant.
- **USER.** The lease will describe the use to which the premises can be put. Changes may be allowed with the landlord's consent, which may or may not be unreasonably withheld. A restrictive user clause is a two-edged sword. The landlord may like the control, but the limited market for a restrictive lease will have an adverse effect on both the tenant's original rental bid and the rent achievable on review.
- **REPAIRS AND SERVICE CHARGES.** As mentioned above, the tenant will be expected to keep the premises in repair. If the whole building is let to the tenant then this is a relatively simple concept. In central London it is likely that the premises will be part only of a building. In this case, the landlord will usually retain the obligation to maintain the structure and common parts of the building but re-charge the cost of that maintenance to the tenant through a service charge. Unlike residential service charges, where statute has intervened, commercial service charges are entirely a matter for negotiation. Landlords are looking for full recovery of any costs associated with the building coupled with discretion as to what falls within the ambit of the service charge. Tenants have a different agenda because of their relatively short-term interest in the premises. No tenant wishes to find themselves paying towards a new roof or a replacement lift in year three of a five year term. The introduction of "Service Charges in Commercial Property – a code of practice" by the RICS after consultation with various property industry bodies is designed to encourage standardization and fairness in the property industry. However, it is for guidance only and, whilst the listed property companies and institutions who participated in its drafting might reasonably be expected to follow it, it may be some time before it informs the actions of smaller landlords.
- **RENEWAL.** Leases of business premises fall within a statutory regime that entitles the tenant to take a new lease, subject to certain exceptions, at the end of the term. It is, however, possible to contract out of this regime and some landlords require their leases to be contracted out as a matter of course.
- **DEALING WITH THE LEASE.** The tenant can usually assign the lease with the landlord's consent which is not to be unreasonably withheld. Underletting is also possible in theory but, in practice, is often severely circumscribed, especially where the lease is contracted out.

The Code for Leasing Business Premises in England And Wales 2007 was launched on 28 March 2007 – the third attempt in 12 years at encouraging fairness in commercial leases and promoting transparency and flexibility in the property market without the dead hand of legislation having to descend on the process. The Code comprises a suite of documents: a Landlord Code, an Occupier Guide and a set of Model Heads of Terms.

All the matters set out in this article should be considered in detail when heads of terms are being negotiated at the beginning of the transaction. Sadly, it is still the case that many of these matters are addressed inadequately in the heads of terms sent to the parties' solicitors after initial agreement, leaving them to sort out any consequent problems or omissions.

The moral of the story is to make sure that your surveyor is conversant with the Code and, ideally, uses the Model Heads of Terms as a checklist for your requirements.



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