

THE GOOD GUIDE TO BUSINESS TENANCIES

Rent reviews, lease renewals and break options



RENT REVIEWS

- Unlike a lease renewal, when the rent can go up or down, with a rent review, in most cases the rent is only reviewable upwards, assuming that an increase is justified at all. Also, the actual date of review is generally fixed which may or may not be to your advantage depending on how the market is moving.
- The review will usually be instigated by the landlord serving a notice, sometimes dictated by formal provisions stated in the lease. Following receipt of such a notice it is imperative to take appropriate action and, if a rental figure is quoted, you must ascertain whether or not the figure is excessive. Also, the lease may contain deadlines within which you need to serve counter notice in order to avoid paying the quoted rent.
- The basis of review is generally governed by the wording of the lease, a close study and understanding of which is important as it may reveal onerous covenants such as a restrictive user clause or limitation on alienation, that could assist in reducing the rent, or artificial assumptions which could negate the benefit to the tenant of any such onerous covenants! If, for example, it is necessary to assume a lease term for say fifteen years, even though the actual lease has far less than this remaining and, in a market where lettings for fifteen years are hard to achieve, a reduction will be appropriate for the additional hypothetical term. Conversely, there may be advantageous covenants which the landlord can argue should increase the rent, such as a low capped service charge or a limited repairing liability or tenant's options to determine the lease.
- It is sometimes possible when negotiating a rent review to strike a deal with the landlord to amend some provisions in the lease, in exchange for a mutually acceptable rent.
- Comparable evidence is the basis upon which the market rent will be assessed and it is important to be aware of open market lettings, rent reviews and lease renewals on other similar properties that have or may be taking place at about the same date. In practice, not every other building is likely to be identical both in terms of accommodation and the lease upon which it is held and appropriate adjustment sometimes needs to be made to reflect such differences.
- the time of a rent review, the most common procedure is for the landlord and tenant each to appoint a surveyor who will liaise and carry out negotiations in order to arrive at a mutually acceptable rent that they can each advise their clients to pay. Depending on the complexity of the situation such negotiations often take many months or longer. Apart from trying to agree what is being valued in terms of the type and quality of property and the form of lease, it is also necessary to agree floor areas.
- With our detailed local knowledge, expertise and extensive database and archive, we are well placed to collate and investigate rental evidence in order to assess the correct rental value and then put together a case and carry out the often tricky negotiations, to resist the landlord's demand and to achieve the correct and lowest possible settlement.

RENT REVIEWS

- If you are in a multi-tenanted building it is important to establish when your neighbouring leases are subject to review and to liaise closely with them. It is not uncommon for a landlord in such circumstances to try and target tenants who they consider to be the weakest link, in order to try and agree a high rent which they will then use in evidence against other tenants.
- In the event that the rent cannot be agreed by negotiation, the lease will provide for the appointment of an independent chartered surveyor to determine the rent, acting either as an arbitrator or an independent expert. Such surveyor may be agreed between the parties but is normally appointed upon application to the Royal Institution of Chartered Surveyors. Quite often application is made for a third party to be appointed as a tactical measure and in order to create a deadline to negotiations and may result in a negotiated settlement.
- Following appointment of an Arbitrator or an independent expert, the surveyor acting for each party will put forward submissions and counter submissions containing their opinion of the rental value, backed up by comparable transactions and any other evidence to support their case. Your surveyor will be acting as an Expert Witness in accordance with the RICS Practice Statement and Guidance Notes which must include a Statement of Truth in relation to the facts contained in the submission.

LEASE RENEWALS

- Your lease will be held either within the protection of the Landlord and Tenant Act 1954 (the Act) or contracted outside Sections 24-28 inclusive of this Act. After 50 years in operation various reforms to amend the Act took effect from 1st June 2004.
- If the lease is held within the Landlord and Tenant Act it means that:
 - The lease will automatically continue until it is determined, either by the landlord serving a notice under Section 25 of the Act or by the tenant serving a notice under Section 26 of the Act. Both notices must be for a minimum of six months or a maximum of twelve months, to expire no earlier than the date upon which the lease would otherwise have contractually expired.
 - If the landlord's Section 25 notice does not oppose the grant of a new lease, the notice will need to contain proposed terms for the new lease. However, there will be a "health warning" on the notice to the effect that the proposals are not binding.
 - In order to object to the grant of a new lease the notice under Section 25 must specify one of a number of grounds upon which a landlord can validly oppose the grant of a new lease. It does not necessarily follow that such opposition would be upheld if challenged in court.
 - Under the previous rules, following receipt of a notice under Section 25 it was necessary for the tenant to serve formal counter notice within two months in order to protect its legal entitlement to a new lease and to then apply to the court within four months. Under the new rules this has been abolished and either party are entitled to apply to court for a new tenancy to be granted. Such application must be made no later than the date of expiry of the landlord's section 25 notice or the tenant's section 26 notice although the parties are allowed to mutually agree in writing an extension of time.
- In response to a tenant's notice under Section 26, if the landlord wishes to oppose the grant of a new lease it will need to respond by stating one of the grounds of opposition.
- When a lease has been contracted out of the Landlord and Tenant Act:
 - This would, under the old rules, have been by means of a Court Order. However, it is no longer necessary to obtain a Court Order and the exclusion will be by agreement with the Landlord serving a "health warning" on the tenant at least 14 days before the lease is entered into, explaining that there will be no security of tenure. The tenant will sign either a simple declaration or a Statutory Declaration to confirm that he understands the implications.
 - Upon expiry the tenant will not have the ability to apply to court, for the grant of a new lease.
 - It does not mean that, at the end of the tenancy, a new lease will not be available by negotiation but you will be in the Landlord's hands as well as the strength or weakness of the letting market at that time. For example, in a poor letting market a Landlord may be keen to retain a tenant and therefore offer a new lease at sensible terms and not take advantage of the fact that the lease is excluded as against the type of tactics that might be adopted in a buoyant market.
 - It is important to try and ascertain the Landlord's intentions well before expiry rather than to wait until the last moment in case a new lease is not available.

LEASE RENEWALS

INTERIM RENT

- Unlike previously when only the landlord could apply, either party may apply to the Court for the determination of an interim rent to be set for the period from expiry of the lease and, in the absence of terms having already been finalised for a new lease. It was therefore only in the landlord's interests to apply in the past if the passing rent was below the then market rent but not if it was above and, in the latter event the tenant could do nothing to reduce the rent other than by negotiation.
- The interim rent is payable from the earliest termination date that could have been given in the landlord's Section 25 Notice or the earliest commencement date for the new tenancy that could have been given in the tenant's 26 Notice. In some circumstances this might actually be prior to the date specified in either notice.
- Application for interim rent will not be entertained if it is made more than six months after the termination of the relevant tenancy.
- The interim rent is set at the same level as the rent for the new tenancy, which is usually the open market rent but, subject to adjustment where market conditions or the terms of the tenancy change significantly during the interim period.

COMPENSATION FOR REFUSAL OF A NEW TENANCY

Provided that Sections 24-28 of the Act do apply to the lease and the Tenant is in actual occupation at the lease expiry date, if the Landlord opposes the grant of a new tenancy within grounds (e),(f) or (g) of Section 30(1) of the 1954 Act the tenant is entitled to Statutory Compensation. If the tenant accepts the landlord's ground for opposition without dispute, the compensation is automatically payable. However, if the ground for opposition is successfully challenged at Court the tenant will then be entitled to a new lease and will have lost the right to compensation.

- Where Statutory Compensation is payable it is equivalent to the rateable value of the premises where a tenant has been in occupation of the property for less than 14 years and twice the rateable value for a continual occupation in excess of 14 years.

TERMINATION OF TENANCY BY TENANT

- A tenant does not need to serve notice if he intends not to renew and to vacate the premises on or before expiry of the lease. However, if he remains in occupation after expiry it is then necessary to serve three months notice.

BREAK OPTIONS

- Some leases contain the advantage of the tenant being able to bring the term to an end by exercising a break clause, generally allowing the lease to be determined at a specific date or dates but sometimes a rolling break permitting determination at any time beyond a specific date. Notice provisions need to be strictly adhered to and it is most important to comply with the wording of the break clause and to be aware of any preconditions that might apply. For example, the lease may imply that, for the notice to be valid, at the time it is served, all rent and other outgoings must be paid to date and any liability in relation to repair and redecoration must have been carried out. If such conditions apply, these should be dealt with before serving notice in order to avoid the landlord being able to validly refuse to allow the lease to be determined.
- The lease may also contain a landlord's option to break, again subject to the need to serve notice within time limits. If the lease is within the protection of the Landlord and Tenant Act the landlord would need to give valid grounds opposing continuation of the lease, similar to a lease expiry and Statutory Compensation may also then become payable.

This is only a brief résumé of these complicated subjects and, should you therefore be faced with an imminent rent review or lease renewal or be considering exercising a break option, we recommend that you seek professional advice from a chartered surveyor and/or a lawyer on the practical and legal implications.

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