

7.0 LEASES

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7.1 Introduction and Summary

A **lease** is essentially a rental agreement, i.e. a contract between the owner (lessor) and the tenant (lessee) stating the conditions under which the tenant may occupy or use the property.

Signing a lease (or rental contract) is one of the most significant financial commitments a company can make. The financial liability defined by a lease lasts the lifetime of the lease, typically three to five years. For this reason alone, a poorly negotiated rental contract can bury a business. Any business considering a lease must pay close attention to the *Critical Issues* described herein.

7.2 Checklist of Lease Considerations

- What if the business fails?
- What if the building is sold?
- What if the business needs to expand or contract?
- What if more parking spaces are needed in future?
- What signage is needed and where can it be placed?
- What has to be done to the space at the end of the lease, e.g. does the space have to be returned to “the condition or state of the space essentially as it was at lease inception.” This is an expensive, often impossible, requirement.

7.3 Critical Issues

The following points should be carefully considered in evaluating a lease agreement:

7.3.1 Space Under Consideration: The lessee (the business owner) should make sure he or she knows the exact area covered by the lease. Measurements are critical to both parties; the lease agreement must spell out precisely the size and characteristics of the space to be leased.

7.3.2 Lease Period: The duration of the lease should be spelled out and must fit with the needs of the business. A typical period is three years, with a clause providing for an option to renew under certain conditions.

7.3.3 Flexibility in Conditions: A favorable lease will allow subletting of the space if the owner decides to vacate or will provide for alternative space in the complex if the business expands.

7.3.4 Timing: The lease renewal process should start as much as a year ahead of the termination date and should anticipate the needs over the next 2 to 3 years.

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- 7.3.5 Costs:** A thorough analysis of insurance, taxes and service costs must be part of the due diligence process. All costs are negotiable.
- 7.3.6 The premises:** The lessee must insure that lease documents describe accurately the space under consideration, including how the square footage is calculated. The provisions should cover any event whereby the space becomes unusable because of environmental conditions beyond the lessee's control. Plans for the subject space and neighboring space should be provided in writing by the landlord for the lease period.
- 7.3.7 Rent increases:** The murky phrase, "based on fair market value" should be avoided. Instead, there should be a clearly understood relationship for rent increases which ties them to something tangible like the Consumer Price Index as stated in a widely recognized publication.
- 7.3.8 Additional costs:** Maintenance costs for common grounds are often passed on to the tenant. The factors that comprise this cost should be clearly stated in the lease, together with the lessee's share, in line with the percentage of the building occupied.
- 7.3.9 Insurance:** Most leases require the lessee to carry business insurance. Real estate experts recommend that tenants have an insurance professional review the lease so that both parties are carrying the appropriate amount of insurance.
- 7.3.10 Defaults and remedies:** The lease must clearly define what constitutes a default by each party. If possible, put language into the lease documents that either party must be notified in writing of a default and be given the chance to fix whatever is viewed as the default.
- 7.3.11 No-competition provision:** If the space is to be used for a retail establishment, the lessee should insist upon a provision that prohibits the landlord from renting space in the retail center to a competing business.