

The Lease Agreement

One of the most important aspects of leasing a new property is the functionality of the building. Will it allow efficient operation of your business? Is there ample office space? Is the power distribution adequate? Is vehicle access and parking sufficient? These are common questions asked but equally important can be the lease agreement itself. Here are some questions that should be answered before making an informed business decision.

Types of Leases:

There are basically two types, Net and Gross.

Net Lease:

Commonly referred to as NNN, 3N, Net Net Net or Triple Net, lessee (tenant) is responsible for, in addition to rent, all operating expenses such as property taxes, insurance and maintenance.

Gross Lease:

Lessor (landlord) pays all expenses of ownership, such as taxes, assessments and insurance. Many lessees believe that the rent covers all the expenses under a Gross lease but this is usually incorrect. Most Gross leases have provisions that pass along many expenses to the lessee. Some of these charges may be termed CAM (common area maintenance) charges, such as landscaping, trash disposal, water, gas, electric, repairs and maintenance. In addition, increases in property taxes and insurance can also be the lessee's responsibility. Many times lessors will charge a monthly CAM fee but this may only be an installment with the lessee responsible to make up any shortfall annually. Even if the lessor waives all additional charges, the lessee will usually be responsible to pay for all maintenance inside their unit including the mechanical equipment and associated systems.

Percentage Lease:

A variation of both Net and Gross leases. More commonly used for retail operations, a percentage lease requires the lessee to pay not only a base rental amount but also a percentage of their gross business income.

Rent Increases:

Other considerations are annual rental increases. Many leases have annual CPI (consumer price index) rent adjustments. These adjustments may have guaranteed minimum and maximum increases, or in some cases may be predetermined fixed rate increase.

Options:

Does the lease have an extension option? This is a clause that allows the lessee to extend the term of the lease at the expiration of the current term. Without this clause a lessor has no obligation to re-lease the premises to the current lessee and the lessee may be forced to vacate whether they want or not.

Lease Compliance:

Does the lessee's operations comply with the lessor's guidelines? Typically the lease will state the type of business to be conducted at the premises. Although the lessee may have possession of the premises, generally they are limited in the type of business operations they can conduct. Many times a lessee will not fully disclose their business operations, only to find that they run into legal problems when they try to broaden their use of the facility. It is much better to fully disclose the extent of your operations to the lessor before the lease agreement is signed. This will lessen future landlord/tenant problems.

Tenant Improvements:

Most standard lease documents have a section called Alterations and Additions. Under those provisions the lessee has certain obligations to the lessor if lessee intends to make physical changes or improvements to the premises. In most cases lessor's prior approval is required. Upon expiration of the lease, the lessor usually has the discretion to require the lessee to return the premises to its original condition or require that the improvements remain in place. Many times lessees incur considerable expense in adding electrical power, lighting, additional air conditioning, etc. under the assumption that they will be able to take those improvements

with them when they leave. This is frequently incorrect. Usually most improvements, alterations or utility installations become the property of the lessor once installed. Additionally, a lessee may take out or move walls and partitions and again assume they have no further responsibility. This is also frequently inaccurate. The lessor has the right to demand the premises be returned to its original condition and configuration at lessee's sole expense. The lessee should thoroughly discuss these issues with the lessor before any modifications are attempted. For your own protection, get the lessor's prior written permission and a clarification of what your obligations will be at the expiration of the lease.

Condition of Premises:

One last consideration before signing the lease, is the condition of the premises. Most leases have provisions requiring the lessee, at the end of the lease, to return the premises in the same condition as received, less normal wear and tear. It is important that you document the condition upon lease execution so as not to be held responsible for pre-existing damages or non-operational equipment. Photographs and written notification to the lessor is your best protection, especially if you are taking a unit in "as is" condition. Keep in mind, the lessee is responsible to keep all components of the premises in good working condition. This is the condition of the premises that the lessor will expect to receive at the expiration of the lease.

With all of the possible variations in today's lease forms, it is critical that a lessee reads and fully understands the lease documents to minimize unpleasant surprises. What might look like a good deal in the beginning could have many hidden costs associated with it. At Bel/Co we strive to minimize additional costs and problems for the lessee.