

# Common Property Phrases

## Assignment

An assignment of a lease takes place when the tenant (assignor) transfers/sells to another person (assignee) their entire interest in the property for the unexpired residue of the lease.

Section 52 (1) of the Law of Property Act 1925 requires that for the legal estate to pass to the assignee, then the assignment must be by Deed.

Under the doctrine of “privity of contract”, the original tenant remains liable to perform all the covenants in a lease throughout the term. Thus, if the lease is assigned to a third party, in the event that the new tenant defaults, the original tenant remains liable for the covenants contained therein.

In some cases therefore, if an assignee is found to be in breach of contract, the landlord is able to look to the assignor to seek redress; even though the original tenant has no control over the subsequent occupiers business.

The Landlord and Tenant (Covenants) Act 1995 sought to address this issue and relieve the original tenant from such liability upon assignment. Modern leases granted on or after 1st January 1996 usually incorporate this change in legislation.

## Break Options

A ‘break option’, ‘break clause’ or ‘option to determine’ is a clause in a lease which gives either the landlord, tenant, or both, a right in specified circumstances to terminate the lease before it’s contractual expiry date.

The break option will usually define the length of notice to be given by either party in order to operate it and any other conditions. A break clause may also be subject to contractual or statutory financial provisions that need to be complied with in order for it to be legally binding.

In addition, it can also be linked to a rent review date and its subsequent operation may make “time of the essence” for the purpose of invoking the rent review provisions within a lease.

## Building Insurance

This is an insurance policy which covers the landlord against damage, destruction and loss of rental for their building, against the usual perils. The tenant of a commercial lease is usually responsible for reimbursing the cost of the landlord’s premium.

## Building Survey

A building survey is an examination of a building by a surveyor (which may include specific tests by the surveyor or other experts) in order to produce a report on the structural integrity of a building and the state of repair.

Such a report would usually cover the condition of the structure, incidence of any defects to the fabric of the building and the state of repair of fixtures and fittings, services and plant installations.

Depending upon the instructions given to the surveyor, these physical features would also be described in relation to safety, stability, strength, efficiency and economy in use, ease of maintenance and other factors as required.

A building survey is often required as a condition to the grant of a mortgage or loan secured against the value of a property.

## Compulsory Purchase

This is an acquisition in accordance with statutory procedures and practice, of interests in land or rights, by a public or private body empowered to do so by an Act of Parliament, and authorised so to do by an appropriate Compulsory Purchase Order.

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A compulsory purchase order (CPO) is a legal function in the United Kingdom that allows certain bodies which need to obtain land or property to do so without the consent of the owner. It may be enforced if a proposed development is considered one for public betterment - for example, when building motorways where a land owner does not want to sell. Similarly, if town councils wish to develop a town centre, they may issue compulsory purchase orders. Compensation rights usually include the value of the property, costs of acquiring and moving to a new property, and sometimes additional payments. Costs of professional advice regarding compensation are usually reimbursed by the Authority, so that people affected by a compulsory purchase order can seek advice from a solicitor and a surveyor and expect to be reimbursed.

## Contents Insurance

This is essentially an insurance policy, which covers the tenant against damage, destruction and loss of their goods and chattels.

## Fit Out Costs

These are costs which are usually incurred by the ingoing tenant prior to being able to occupy any new or alternative accommodation.

Fit out items will include a range of goods from the erection of partitioning, installation of electrical or telecommunications cabling, through to purchasing furniture.

Fit out costs will vary according to each tenant's particular requirements and it may be possible to obtain a landlord's contribution towards the expenditure. The amount spent on fit out costs is usually written off over the duration of a tenancy. In the circumstances it is important to have regard to the length of any new lease prior to incurring the costs.

During the period of time when any fit out works are

taking place, it would be usual to obtain a rent free period until such time as the property is ready for beneficial occupation.

## Fixtures & Fittings

A fixture is usually an item that has been annexed to a property to such an extent that it becomes part of it, i.e. the article cannot be removed without significant damage to the land or building. A fitting is more commonly regarded as an item that is easily removable from the land or building.

Items may be defined as either landlord's or tenant's fixtures and fittings.

Landlord's fixtures and fittings are usually non structural/non material parts of the property which are present at the start of the tenancy; such as lightweight or demountable partitions, purpose built kitchens, individual air conditioning units and carpets.

Tenant's fixtures and fittings are things that the tenant may have added at their own cost. Normally it is recommended that the tenant has a list of these items and is able to prove that they have been added by them. It may be necessary to obtain permission to add them to the property if required to do so under the terms of the lease.

## Freehold

This is the term used as shorthand for the tenure of an estate in land which exists in "fee simple absolute in possession" and identifies the ultimate owner of a property. Such ownership usually includes not only the surface land or building, but also the sub surface of a property and all the air space above.

As part of the aim of simplifying the conveyancing process, the Law of Property Act 1925 set out two estates or interests in land, namely the "fee simple absolute in possession" or 'freehold' and the "term of years certain" or 'leasehold'.

## Ground Lease

This is usually a long lease, granted at a ground rent but subject to an initial premium payment. A ground lease can vary in length from 30 years up to 999 years.

The principle of a ground lease is that the rent paid relates to the value of the land only. The terms of the tenant's lease usually provide an obligation to develop the land. The building is then owned by the tenant, usually free of any rent. Ground Rent levels vary from a peppercorn, i.e. nil rent, to a percentage of the open market rack rental value of the building.

## Incentive

An incentive is a payment or concession that often arises when a lease is first granted or subsequently assigned during the course of its term. A common example might be where a landlord pays a new tenant a sum of money to take on a new leasehold contract.

This sum may be in the form of a capital contribution towards the tenants initial fit out costs. Or it might be in the form of a rent free period or stepped rent until the first rent review date.

## Incentive Fee

An 'incentive' or 'contingency' fee is a charge related to the degree of success achieved in the task for which it is payable.

A client may agree an incentive based fee for property instructions with their appointed commercial property agent. For example, in rent review cases an incentive based fee, if appropriate, is usually based on the degree of success achieved in the negotiation that takes place between the parties. Thus, in the case of representing the landlord, the higher the level of the revised rent achieved, the greater the fee payable to the commercial property agent, or vice versa in the case of representing the tenant.

## Landlord & Tenant Acts

These are a statutory framework for the occupation of a building or land where a landlord and tenant relationship exists.

Business tenancies were first given protection and an entitlement to compensation by the Landlord and Tenant Act 1927. This act was substantially amended by the Landlord and Tenant Act 1954, which now forms the main legislation for owners and occupiers, although further amendments were made by the Law of Property Act 1969.

In essence the 1954 Act provides a business tenant with (i) security of tenure and the right to apply for a new tenancy, subject to specified grounds of opposition and (ii) a right to compensation (in certain cases) upon opposition to a new continued tenancy, for improvements and disturbance.

Not all business tenancies are protected by the 1954 Act and there are strict Notice procedures that need to be complied with in order to maintain such protection.

## Lease Expiry/Renewal

The Landlord & Tenant Act 1954 limits the way in which a business tenancy may come to an end. Thus a tenancy that falls within the provisions of the Act, will not come to an end unless it is terminated in accordance with the provisions set out in the Act.

The statutory methods of terminating a lease are set out in Part II of the 1954 Act. Namely:-

- (i) by a Landlord's notice under Section 25
- (ii) by a tenant's request for a new tenancy under Section 26, or
- (iii) a tenant's notice to quit under Section 27.

The landlord and the tenant must comply with the provisions set out within these various notices, since failure to do so could result in the loss of the

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automatic right for a new tenancy. There are also strict procedures to be followed during the interim period between the expiry and grant of a new lease, either by negotiation or through a court.

## Leasehold

The Law of Property Act 1925 simplified the conveyancing process by creating two “estates” or interests in Land.

The freehold estate or “fee simple absolute in possession” and the Leasehold estate, or “term of years certain”. Leasehold is therefore an estate in land which is held for a term certain, or on a periodic tenancy basis, for a length of time less than the landlord’s interest.

A lease usually provides the tenant with exclusive possession of demised premises, for a definite period, in exchange for a payment in the form of rent or a premium.

## Legal Costs

These are the costs incurred by both a purchaser and vendor of a property, or in connection with the sale or grant of a new lease by a landlord and a tenant. Such costs can include conveyancing fees, litigation advice, counsel’s opinion, stamp duty (controlled by HMRC), local authority search fees, bank transfer fees and court expenses, plus other disbursements and VAT.

Since Legislation is constantly being updated, it is advisable to instruct a solicitor to assist in the preparation of all sale contracts or lease documentation. Fees will vary considerably but they are usually based on between 3% to 7.5% of the first year’s rental, depending on the size, nature and complexity of the matter in hand. Alternatively sale costs are usually based upon a percentage of the sale/purchase price.

Specific legal advice or consultancy fees are usually based upon an hourly rate of charge.

## Length of Lease

A lease is a legally binding contract between a landlord and a tenant which sets out the basis on which the tenant is permitted to occupy a property.

The length of the term will vary depending upon the particular requirements of the landlord and the tenant and will be influenced by business requirements, investment strategy and general matters such as economic conditions.

In broad terms, the landlord will often seek to create a lease of between 15-25 years, whereas the tenant is more likely to require a shorter term of 5-10 years, particularly in times of economic and political uncertainty. The lease length may also be influenced by the incidence of break clauses and the prospect of a formal option that might exist to extend the lease upon expiry.

Large properties, or those involving the tenant in significant investment in fit out costs, might attract longer leases in order to allow sufficient time for the tenant to recoup the initial costs of taking on the property.

## Licences

A licence is essentially the lawful grant of a right to do something which would otherwise be illegal or wrongful.

A licence does not transfer any “interest” in land, but it may authorise the occupier (licensee) to enter the owner’s (licensors) land for some specific purpose.

A licence does not provide a licensee with security of tenure of rights as set out in Part II of the Landlord and Tenant Act 1954, although the distinction between a “licence” or a “lease” is not always clear. It is essential that a licence is documented correctly and that the parties’ obligations are clear from the outset.

Under a licence, the consideration paid is known as the ‘fee’ instead of the ‘rent’ which is the case for a lease.

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## Local Authority Searches

A local authority search is essentially an application for an official search of the Local Authority's records, for written confirmation or a certificate disclosing matters or encumbrances affecting the land. Where a lease is being granted or conveyancing takes place, a local authority search should be undertaken.

Typical information that might be revealed by a local authority search includes:-

- (i) ownership of roads and sewers affecting the property.
- (ii) any road widening schemes in the vicinity of the property.
- (iii) any breaches of planning legislation.
- (iv) a history of the planning applications made in respect of the property.
- (v) details of any pending Compulsory Purchase Orders (CPO's).
- (vi) any smoke control orders.

## Purchase Costs

With property acquisitions, a prospective purchaser will normally incur "acquisition" or "purchase costs" in addition to the actual purchase price. These costs are essentially legal and surveyor's fees, VAT and stamp duty. The level of these costs will vary depending on each particular property, the nature of the client/surveyor relationship and any changes in the rate of Stamp Duty imposed by HMRC.

At present the purchaser of a property sold with a purchase price in excess of £500,000 could expect to have a combined acquisition cost equivalent to about 5.75% of the purchase price.

A prospective purchaser may have additional costs of acquisition arising from a building survey or environmental survey.

## Rating Liability

A Rating Liability is a charge based on the occupation of commercial land and buildings, administered by the Local Authority.

The "Rateable Value" of a property is assessed by the Government's Valuation Office and can have similarities to the rental value of the property.

All Land and Buildings are re-valued every 5 years. The Local Authority use the Rateable Value to calculate the level of business rates to charge to the property occupier, by adopting a multiplier known as the Uniform Business Rate.

An appeal against a Rateable Value can be lodged by a person having an interest in the property. If successful, and the Rateable Value is reduced, then the local authority will reimburse overpaid rates, backdated to the date of the Appeal.

There are various grounds for lodging an Appeal. Also a number of reliefs from a rating liability are available; for example in the circumstances of temporary non-occupation of a property, charitable status of the occupier, and the effect of major works of construction adjacent or nearby to a property.

## References

When a new tenant enters into a lease, the landlord will normally require the provision of satisfactory references as a condition of the lease being granted. In these circumstances, the tenant is usually required to provide references from a bank, an accountant and two trade references, although this may vary depending on each individual case.

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## Rent Deposits

A rent deposit is principally a sum of money which is held in an account, for an agreed period of time, to act as financial security in case of default by a party to a contract. The money would usually earn interest at a fixed or variable rate.

When new leases are entered into, a landlord will often require a rent deposit from the in-going tenant. The terms of such a rent deposit will vary depending on the financial status of the tenant, but can involve the tenant paying up to 6 months rent in advance. This amount is then held by the landlord in an interest bearing account for the duration of the lease, or until the financial integrity of the tenant becomes established. Alternatively, it might be held until such time as the lease is assigned and a new deposit is obtained from the subsequent assignee.

## Rent Reviews

Rent review provisions in commercial property leases were originally introduced to counter the effect of inflation during the term of the lease.

A standard rent review clause will generally require the rent to be reviewed at fixed intervals, usually five yearly, during the term. The vast majority of rent review clauses require the assessment of the open market rack rental value, at the review date, in accordance with specified terms. Some rent reviews are however geared to the tenant's turnover or profitability, or movement in the Retail Price Index.

In the case of calculating the market rent for a demised premises, the form of the review clause will vary from lease to lease. In general however the clause should make clear:

- (i) the review period
- (ii) the procedural steps for having the rent reviewed

- (iii) whether or not time is of the essence in the service of notices
- (iv) the basis of valuation, i.e. assumptions and disregards
- (v) any hypothetical terms and conditions to be adopted
- (vi) in default of an agreement, the procedure for the appointment and determination by a third party surveyor such as an Independent Expert or Arbitrator
- (vii) the effect of a late review, i.e. from when the rent is payable and whether interest is payable thereon
- (viii) whether the rent can be reviewed upwards or downwards

## Repair Covenants

Covenants in a lease are the terms of the contract between the landlord and the tenant and they specify responsibility for matters arising out of the lease.

Normally, a lease will make express provision for one party to repair and maintain the whole or part of the demised premises and for the other party to repair and maintain the remainder.

In short leases the landlord will often be directly responsible, while in long leases the tenant will usually take on the obligation for repair and maintenance.

For leases held in respect of premises that form part of a larger building, it is frequently the practice to require the tenant to keep the interior repaired, while the landlord is responsible for the exterior and common parts and the structure of the overall building. The landlord will often seek to recover the cost of fulfilling this liability by way of a service charge.

## Schedule of Dilapidations

This is a list of outstanding repair and maintenance items, that a landlord has assessed have accrued under the terms of a tenant's repair and maintenance obligations.

It is often served by the landlord at the end of the lease in the form of a "Terminal" Schedule of Dilapidations. The tenant is obliged to carry out the outstanding works listed in the schedule or pay damages which represent the cost to the landlord of doing the works.

The items in a Schedule of Dilapidations are often the source of dispute between the landlord and the tenant and a court will ultimately decide upon the relevance or otherwise of the contents of the Schedule.

In certain situations the tenant is entitled to relief from the obligations set out in a "Terminal" Schedule of Dilapidations, as provided for by Section 18(1) of the Landlord and Tenant Act 1927.

An "Interim" Schedule of Dilapidations can be served by a Landlord during the course of a tenancy, specifying outstanding works of disrepair that need to be attended to whilst the tenant is in occupation. Relief from complying with the obligations of an "Interim" Schedule may also be available in accordance with the provisions of the Leasehold Property (Repairs) Act 1938.

## Service Charge

This is a sum of money payable by a tenant on account of services provided by the landlord and is often collected quarterly in advance at the same time as the rent.

A service charge usually arises when a property is in multiple occupation, such as an office block or shopping centre.

Typical service charge items include the repair and maintenance of the external or structural parts of a

building. Also, costs arising from repair and upkeep of common parts, together with managing agent's fees and a sinking fund.

A service charge payment can be capped in order to limit the amount of a tenant's financial liability. In addition some service charge costs have a limit to the amount of increase that applies during the term of a lease. For example, the charge cannot rise in excess of the movement in the Retail Price Index. This provision enables the tenant to restrict future service charge liabilities.

## Stamp Duty

This is a Government fixed tax, chargeable on the execution of documents, pertaining to transactions such as Leases, Agreements for Leases and Conveyances.

The duty is payable by the purchaser or lessee, and the disposal document can not be adduced as evidence of the transaction unless adequately stamped.

The rate applicable is set by Central Government and varies depending upon the value of the transaction.

Current rates are as follows:

- Up to £60 000 - nil
- Over £60 000, up to £250 000 - 1%
- Over £250 000, up to £500 000 - 3%
- Over £500 000 - 4%

## Sub-Letting

A sub-letting takes place when a tenant grants a new lease for their property, or part thereof, to an alternative occupier, for a period less than the residue of the tenant's lease.

The period of the sub-letting must be at least one day less than the unexpired period of the superior lease.

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If a tenant attempts to sub let the property for a period equal to, or more than, the unexpired period of their own lease; this operates as an assignment of the term and not as a sub-letting.

## Tenant's Improvements

The expression Tenant's Improvements is used to describe a wide range of works, that are usually carried out by a tenant, at their own cost, and usually require the landlord's prior approval. Tenant's improvements may not necessarily increase the value of the demised premises, but can have an impact upon the future rent payable by a tenant.

Section 19 (2) of the Landlord & Tenant Act 1927 provides that a covenant in a lease against the making of improvements, without the consent of the landlord, is deemed to be subject to a proviso that consent will not be unreasonably withheld.

As a condition of consent however, the landlord will often require:-

- The payment of a reasonable sum in respect of any damage to or diminution in the value of the premises or of any neighbouring premises also in the landlord's ownership.
- The payment of the landlord's legal and other proper expenses incurred in connection with the granting of consent, usually by way of a Licence.
- In cases where the improvement does not add to the value of the demised premises, a covenant from the tenant to re-instate at the end of the lease.

Most rent review clauses will include a provision whereby Tenant's Improvements are ignored for the purposes of assessing the revised rental value.

## User Clause

This is a contractual provision within a lease, that specifies the use, or uses to which a property may be put and the uses which are prohibited.

The formal classification of "Uses" are set out in the Town and Country Planning (Use Classes) Order 1987 as amended, which is a statutory instrument defining various use classes.

The terminology of a user clause contained within a lease is critical in determining whether the use specified is restrictive or open. This aspect can be very important when considering the open market rental value of a property.

## VAT

Value Added Tax is a tax that is charged on the supply, actual or notional, of certain goods and services in the United Kingdom.

In cases where the landlord has elected to charge VAT on their property, this tax will be payable by the tenant in addition to the rent paid for the demised premises.

Currently levied at a rate of 20%, if the tenant is VAT registered, in most cases they will be able to recover the amount charged from Customs & Excise. This tax should therefore be comparatively neutral for most parties, except for the ultimate consumer.