

The Model Commercial Lease

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The launch of the Model Commercial Lease family of leases and property management documents earlier this year is expected to speed up the process of negotiating leases of commercial property. This article explains the origin of the MCL and summarises its principal provisions.

It is just possible that a small group of property lawyers are about to accomplish a major change in the manner in which commercial property leases are granted in England and Wales. In July this year, this group (termed the “working group” in this article) unveiled the Model Commercial Lease (MCL), a family of commercial leases and property management documents, freely available on a website for the legal profession to use.

Standardisation is currently in fashion everywhere. The construction and banking industries have used standard documents for years, but commercial property lawyers have so far resisted the trend. Admittedly, there have been various attempts over the last 20 years to standardise leases. Most disappeared without trace, although there have been some successes: the Law Society publishes two forms of business lease and the RICS recently published a lease for short-term lettings of shops, in connection with the Government’s initiative to invigorate high streets. But such documents are rarely used for investment-grade lettings.

The working group hopes that this is about to change. Back in 2011, the BPF commercial committee decided that it was time to review the commercial leasing process in England and Wales. Many major landlords produce fairer terms as a first draft than they did 25 years ago. However, a lack of standardisation in both lease structure and content means that every letting is treated as an individual negotiation of a lengthy document. This distracts the parties from the specific parts of the transaction that actually matter to them, and of course drags out the negotiation, and increases the costs. In today’s ever-faster world, this is simply not a sensible way of doing business.

A working group of property lawyers and landlord representatives was set up to find a solution. Their remit was to produce a form of lease that could be used as a fair starting point for the majority of transactions. At the same time, there was an opportunity to modernise the wording and the style. As part of the process, the working group consulted informally with most of the major law firms in England and Wales, and consulted more formally with a number of BPF members.

MCL documents

After over three years’ work, the MCL is now available, comprising not just a family of templates for commercial leases but also the more common asset management documents. They are all freely available for anyone to download without charge from the MCL website (<http://www>

[.modelcommerciallease.co.uk](http://modelcommerciallease.co.uk) [Accessed August 28, 2014]) and customise to their particular requirements. As explained in the second section of this article, the templates are largely compliant with the Code for Leasing Business Premises (the Lease Code).

Different versions of MCL leases are available to suit different types of commercial buildings: offices, shops, shopping centre units and industrial/logistics units. Most leases are available as two versions: a lease of whole and a lease of part. The working group has also provided optional bolt-on provisions, including two different types of rent review clause (turnover rent and index-linked rent), an offer-back clause, an option to renew clause, a service charge cap provision and specialist clauses for premises from which food and drink are supplied (A3/A4/A5 planning uses). The asset management documents include a rent deposit deed and the commonly encountered licences—assignment, underletting, change of use and alterations.

The MCL is intended to avoid much of the unnecessary negotiation on most routine letting transactions by representing a fair starting point for both parties, and in many cases a fair end point as well. The aim has been to remove the “ritual dance” at the start of a transaction, so effectively rendering unnecessary the first round of the parties’ amendments. The parties are therefore freed up to discuss the issues that are specific to their deal and those that actually matter to them.

The working group intends to keep the MCL under review to ensure that it remains up to date. Successive versions of every document—the current version and all previous versions—will be available for everyone to view and download free of charge on the MCL website.

Specific provisions

This second part of the article considers the key provisions in the MCL and draws attention to any differences between the MCL and a traditional lease. Given that the MCL has expressly been drafted as an institutional lease, there are relatively few departures from the norm and most of these are found either in the boilerplate, or in the covenants that are affected by the Lease Code.

The working group has provided (on the MCL website) a Guidance Note that summarises the main provisions of the MCL, and users should refer to it for more information about the issues mentioned below. Also available on the MCL website is a note that highlights the areas where the MCL provisions do not comply with the provisions of the Lease Code.

Format

The MCL starts with the Land Registry Prescribed Lease Clauses. These must be retained whether or not the landlord’s title is registered. There are no particulars. All defined terms are in the definitions section, unless used only in a particular schedule.

The layout is familiar. Clauses 1 and 2 contain definitions and interpretation provisions respectively. Clause 3 covers the demise, rent and term. Clause 4 covers the tenant’s specific obligations and clause 5, the landlord’s specific obligations. General agreements are in clause 6. There is an optional guarantee provision in clause 7 and an optional break clause in clause 8. Detailed provisions have been put into schedules, which cover such matters as rights and reservations, rent review, service charge, insurance, title, permitted works, sustainability and underletting provisions. There are extensive footnotes, which explain why the lease has been drafted in a particular manner or act as prompts to delete definitions that might not be needed (“break date”, for example, where there is no break clause).

The lease uses modern language, although it has retained “landlord” and “tenant” rather than “we” and “you”, which might be used in modern consumer contracts. Some modern terms have been introduced, including End Date (instead of “expiration of the term”) and Rent Date (instead of “Quarter Days”). The verb “must” is used to indicate an obligation to do something, rather than “shall”, “will” or “is to”. It is sensible to try to retain this modern drafting style when amending the existing text or adding new provisions (although this may not come naturally to many practitioners).

Clause 2—interpretation clause

The interpretation clause contains a number of innovations intended to streamline the drafting and speed up the negotiation process. The user will need to become familiar with them, especially where new provisions are introduced into the lease that might be affected by them. For example, any reference to notifying a party means not only notifying that party in writing, but also service on it in accordance with the MCL service provisions; references to approvals or consents mean prior written approvals or consents, which are not to be unreasonably withheld; any costs to be paid must be reasonable and proper; and any reference to a request, requirement or stipulation made by the landlord means one that is reasonably imposed, unless the lease stipulates that the landlord has an absolute discretion.

Clause 3—demise, term and rent

This contains provision for an optional title guarantee, and an option for monthly rents, which are now becoming increasingly common, particularly in shorter leases.

Clause 4—tenant’s covenants

The MCL contains the usual tenant’s covenants but the following provisions are of particular interest:

Indemnity: this has been tempered considerably so that it does not cover breaches by the tenant of its covenants. It applies only to third party claims. It also requires the landlord to keep the tenant properly informed and to mitigate its loss (at the tenant’s cost). This is an example of a balanced provision that provides what tenants are seeking, while at the same time not disadvantaging the landlord in any practical sense (given that informal investigation concluded that landlords rarely rely upon the standard all-singing all-dancing indemnity in any case).

Repair: the tenant’s repairing obligation is a traditional “good and substantial repair and condition” obligation. However, there is also an optional provision for a schedule of condition, given that this is a requirement of the Lease Code. It is of course up to the parties to decide which option to choose. Damage by both insured risks and uninsured risks is excluded.

Alterations: again following the Lease Code, internal non-structural works that have no adverse impact on the environmental performance or the building systems do not require landlord’s consent. Other alterations do require consent. Certain alterations that might traditionally be prohibited completely as they involve structural elements outside the demise are permitted with the landlord’s consent, including installing service media (these are termed “Tenant’s Business Alterations”). There is optional provision for a streamlined protocol for the landlord to grant consent to permitted works—effectively incorporating within the lease the provisions that would traditionally be included in a licence for alterations.

User: the user clause prohibits any use other than the permitted use, but there is no positive “keep open” provision. The list of standard prohibited uses has been reduced in length substantially.

Alienation: this is in a standard form although the detailed underletting provisions are in a separate schedule for convenience. Following the *K/S Victoria Street* case, assignment of the lease to a current guarantor is not permitted. There is no prohibition of intra-group assignments. For assignment, there is a condition that the principal rent has been paid but there are no other conditions. The requirement for the tenant to provide an authorised guarantee agreement is “if reasonably required” and so complies with the Lease Code. The “reasonableness” is incorporated by the interpretation provision mentioned above.

Reinstatement: an innovative mechanism for reinstatement has been provided, to avoid the brinkmanship that typically occurs towards the end of a lease. The tenant is able to serve a request on the landlord towards the end date, asking the landlord to inform the tenant, within six weeks of receipt of the notice, which works the landlord wants the tenant to remove. The landlord can only stipulate works that it reasonably considers should be removed (which complies with the Lease Code). The tenant is required to give the premises back with vacant possession, except for any permitted undertenants who have rights to remain under the Landlord and Tenant Act 1954. This is different from the position when the lease ends following a break notice (when vacant possession must be given).

Break clause: there is an optional break clause. The conditions are simply payment of the principal rent and vacant possession (which complies with the Lease Code). The lease notes that best practice is to specify the calendar date for the break and to make the break date the day before a rent payment date (rather than the rent payment date itself). This ensures that the tenant is not legally obliged to pay a full period’s rent on the day the lease ends. However, there is also a separate provision for the landlord to repay the tenant any overpaid amount of rent, which applies however the lease ends. It requires any rent paid in advance to be refunded. A similar provision relating to service charge is in the service charge schedule.

Clause 6—landlord’s covenants

The landlord’s covenants are largely standard (apart from the repayment of rent obligation mentioned above). The provisions protecting the tenant if the landlord needs to enter the property are possibly wider than landlords normally offer but not unusual in terms of what is eventually agreed.

Rent review schedule

This is a neutral rent review clause, not intended to achieve a headline rent. There is a qualification to the assumption that the landlord’s covenants have been complied with where the landlord has been in material or persistent breach. The disregards specifically address tenant’s fitting-out works and (in the retail leases) any mezzanine floor areas. The landlord needs to decide at the outset whether the rent review surveyor will act as an arbitrator or as an expert. It does not have the luxury of waiting until the review to make the decision. There is no provision relating to rent restriction legislation as (in the unlikely event that one is ever introduced) it is likely to cater for existing leases.

Service charge schedule

Service charge schedules contain possibly the greatest range of variations in modern leases, depending on landlords' particular concerns and the type of building under consideration. This schedule is intended to form a generic starting point. There is no obligation to "comply" with the RICS Service Charge Code, although the landlord must "take into consideration" its administrative, accounting, procurement, management and operational provisions. The schedule contains a long list of the sort of exclusions that a well-advised tenant might require, and this needs to be considered carefully in each case. There is insufficient space in this article for a full explanation of the MCL service charge schedule. Users should read the wording carefully and refer to the relevant part of the MCL Guidance Note.

Insurance schedule

In terms of damage by insured risks, the schedule is conventional. The landlord insures the building (although not the tenant's fixtures). The list of insured risks has been modernised after discussion with the BPF Insurance Committee. Terrorism is now an insured risk. The landlord must insure against terrorism, if cover is available. The schedule also contains suggested wording for uninsured risks but the parties will need to consider it carefully, since there is no standard practice yet. The basic principle is that the tenant has all the benefits it would have had if damage had been caused by an insured risk except that the landlord has a choice as to whether to reinstate. If it wishes to reinstate (at its own cost), it must tell the tenant within 12 months of the damage. Unless it does so, the lease will end at the end of that twelve month period.

Sustainability schedule

An innovative approach sees all sustainability provisions gathered together in one schedule, enabling the parties to answer the question "how is sustainability addressed?". The obligations in this schedule are administrative only, and no attempt is made to impose onerous obligations on either party.

Conclusion

Lawyers and their clients who have already trialled the MCL have been surprised by how convenient it is to adapt for particular transactions and particular buildings. One of the reasons for this is that the documents have been drafted on the basis that they will be amended before use. They are merely a fair starting point for the production of a draft document. The parties are free to customise them as they wish.

Lawyers, incidentally, are surprisingly supportive of the project. Concerns had been expressed that they would see it as a threat, reducing fee income. The contrary is true. Lawyers are often on fixed fees for lease negotiations, so anything that speeds up and simplifies the process has to be advantageous. Furthermore, after many years (sometimes decades) of negotiating the same points, mostly to reach the same end, lawyers themselves feel that life is too short to argue points that have little or no benefit for the parties in practice. Clients too are supportive: the landlord and tenant relationship is now less confrontational than in the past, and many experienced counterparties do not relish unnecessary conflict, especially at the start of the relationship.

The working group is aware that the MCL has already been used on a number of one-off lettings. Obviously, introducing it into a building where a standard form of lease is already in use (a shopping centre, for example), will be more complex. The ideal will be a brand new

development, where the MCL will be used as the basis for each of the leases. However, the MCL will happily sit alongside existing forms of lease that are already in place and it could be introduced gradually as new tenants move in to fill vacant parts of the building.

The law is stated as at August 21, 2014.