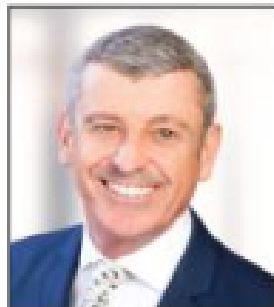


Re-Negotiating Your Rent – What Operators Need To Know To Get It Right



Comment from John Deane,
Partner, Gannons Solicitors

It's a fact. The majority of restaurant operators are spending more than they can afford on rent and rates. In their latest report, leisure and property agent Cedar Green Group states operators are seeing turnover hit by an average

of 21% just on rent - an increase of 16% on the previous year. The Group says historically, 12% of turnover is the maximum rent restaurant businesses can afford. However, current statistics show a completely different story, with the industry suffering rent hikes of 70% over the last five years and 140% over the preceding decade. Has hospitality now reached breaking point with commercial landlords? What can restaurant operators do to secure sustainable leases in such a precarious landscape?

Here are 10 key tips for operators looking to re-negotiate their rent in a difficult climate:

AT THE START

1. Often a restaurant lease has been inherited from the previous occupant of the premises, which means the lease terms have already been agreed with the landlord. If a new lease is being offered by a landlord, it presents an opportunity to negotiate terms. Leases for 20 years or more were commonplace in the 1980s when rent reviews were usually every five years. Today operators prefer flexibility and are less willing to be tied into leases for 20 years, which means shorter leases are more commonplace. We see many five-year terms. Five-year rent reviews are also still common but with lease terms generally getting shorter, we sometimes see reviews arranged for every three years. Ideally an operator should try to negotiate a five-year lease with no review of rent.

2. Operators should aim to negotiate a rent-free period and a tenant's break-clause – the latter enables a rental contract to be broken early and ideally should be actionable, for example, halfway through a five-year lease. If the landlord requires a 10-year lease, operators might request two break-clauses for the period. It's fairly common for break-clauses to be linked to rent review dates too so that if an operator is unhappy with the rent payable as a result of the review, they may exercise the break-clause and end the lease. It's about establishing as much flexibility as possible to contain future liability.

3. When negotiating conditions, restaurant operators should ensure the lease contains the appropriate type of rent review (some examples are market rent, indexation and turnover rent) and the procedure for operating the review and final determination if no agreement can be reached. Whilst upwards-only rent reviews are of course popular with landlords, they are potentially unfair to tenants if the market falls. Upwards-only reviews are slowly becoming less common so do remember, as an operator, you have the right to request terms that state rents can, on review, be decreased as well as increased – a useful tool for protecting against unknown events in the future.

4. A tenant in financial difficulties might look to let all or part of their premises at a rate under the market value to minimise losses. However, many leases contain provisions that prevent underletting of part of the premises and also state the rent on an underlease of the whole of the premises cannot be less than either the market rent or the rent currently payable under the lease, whichever is higher. Where the market value of the property has dropped below the current rent, it will be almost impossible to find someone willing to take an underlease, which means that as a tenant, the operator would be paying the whole of a rent that no longer reflects the market value of the premises. It is worth trying to negotiate a relaxation of such restrictions so that if financial difficulties arise, underletting is a viable option.

LOCATION, LOCATION, LOCATION

5. Flat Iron recently closed its Notting Hill branch, citing not only a rent increase but also the impact of poor transport links to the location. There are many other premises that will have their own pain-points but if a site appeals to an operator in every other way, it shouldn't immediately be ruled out on one sticking point. If a property might be difficult to let because of a transport issue, like the case with the Flat Iron site, there are legitimate grounds for a new operator to use any negative factors in the lease negotiation process. Perhaps the poor transport links could be offset by a decrease in rent to cover the reduced footfall. All the aspects of regular due diligence should be in play, and a prospective leaseholder should attempt to speak to the present or previous incumbent of the lease to establish any fundamental issues.

A PRIVATE MATTER

6. It's important for restaurant operators to look out for their own interests when negotiating a lease. There doesn't appear to be any kind of regulatory reform on the horizon that could help to contain commercial rents, and indeed this is not somewhere a government would generally attempt to enforce control, given the general view that, in the private sector, market conditions should prevail. It's therefore up to the operator to ensure they get a fair deal.

7. Some industry commentators believe tenant security is diminishing as many landlords seek to bypass the security of the 1954 Landlord & Tenant Act. Broadly speaking, the Act gives business tenants a degree of security by giving them the right to renew their lease based on the same terms as the original (except for rent) unless the landlord intends to occupy the premises itself or redevelop the premises. A landlord may also stipulate that a lease is excluded from the protection of the Act – in practice, many landlords will market a lease on the basis that it is excluded and in fact, more than a

quarter now fall outside this protection.

THE FINER DETAILS

8. Operators need to have their wits about them when negotiating and checking the terms of a lease. In addition to speaking to the landlord about a new contract, restaurant operators buying an established business with an ongoing lease should look closely at how they can sustain or improve turnover in that location. Apart from the customer base and the accounts, a potential buyer should consider website traction, any presence and reputation on service providers such as OpenTable and TripAdvisor, and its social media accounts. It might not always be a case of can the new operator improve on those metrics, but at first, can they even maintain the standard that has made the business so attractive in the first place? These areas can significantly affect whether a concept thrives or fails, and should be an important part of an operator's due diligence upon entering a new lease.

9. It goes without saying that restaurant operators should take the advice of agents on commercial terms, a solicitor on legal conditions and a surveyor on the state of the building repair. It's also wise to consider obtaining professional quotes for the cost of any refurbishment or fit-out the operator will need to do before trading as this can help to negotiate lease costs. Only then should an operator consider entering into a rental contract.

10. A surveyor's input is also useful when drawing up the terms for exit. Operators must establish at the outset what the landlord expects at the end of the lease and the condition in which the building must be left. The surveyor can prepare a schedule of condition as part of the negotiation process which could be attached to the lease as evidence of the state of the premises when the lease was granted, for referencing compliance with the operator's repairing obligations when leaving.

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