



HELP! I don't know where to start with commercial leasing

So you've decided to finally open up that cafe you've always dreamed of or maybe your home office isn't quite cutting it anymore. It's time to dive into the world of commercial leasing but you have no idea where to start. We asked our friend Josh Biggs from Harris Real Estate a few questions on the basics of commercial leasing and where to start.

Location, Location

Finding the right location for your commercial lease will depend on a number of factors. Firstly, what type of building will you need? Is it for an office space or are you opening up a retail store or cafe? If it's retail or hospitality, location is very important. Do you need high foot traffic? What's your customer demographic? If it's an office space, the location might not be so important but in saying that, you still want to be in a location that is appropriate for your business e.g. CBD and easily accessible for staff and clients. Another key point is to work out what size building you will need because when it comes to commercial leases, it's all about the square metres.

Different from residential where you're looking at the number of bedrooms and bathrooms, the costs are all dependent on square metres. Once you've identified the general location and size you need, it's time to see which agents are active in that area. Build a rapport with agents in the area and they'll let you know what's coming up on the market. A good place to start to research properties in the area is realcommercial.com.au, which is like realestate.com.au but for commercial properties.

Understanding the Lease

If you're starting out and you haven't had any experience with leases there are companies who represent tenants; tenancy advocates. So depending on the size of what you're embarking on, that might be something to consider. Alternatively if you're going to go into it yourself, you'd probably want to ask the agent that you're dealing with for a copy of a draft lease. This will give you an opportunity to read through and get your head around what's involved.

There's a head of agreement, or an agreement to lease, which holds the key parts to a tenancy and then the formal lease which is a much more lengthy document. Starting to read and understand a lease is really important to avoid any surprises along the way.

Length of Lease

The length of lease is a critical one because although landlords like a longer lease, if you're starting a new business then you probably want a slightly shorter term to start with but with some options to extend if it goes well. A lot of businesses will take out a two year lease to start and then at the end of that two year lease, if they are heading in the right direction, they might have a three year option after that. So it would be what we call a two plus three with the total at the time being a five year lease. If it doesn't go to plan after the two years, then the tenant would have the right to not extend that lease if they didn't want to. It's a tenant right not a landlord right.



Lease Costs

Normally you'd sign a lease of up to five years and each year you'd have a possibility of a consumer price index (CPI) increase. In addition to that you generally pay what's called outgoings as well. So you've got a rental component and your outgoings which cover things like council rates, water rates, strata fees etc. When you see leases advertised there'll be a rent figure and then it will generally be including outgoings or plus outgoing. So they're the two things to look for; what's my rent and what are my outgoings likely to be.

The Covid Effect

Tenants are now wanting COVID-19 clauses when negotiating conditions of lease. They want something in writing to state what would happen if we went back into lock down in that area or if the state got affected as it has previously, what would happen then? Initially landlords had to rely on what was put out by the government as a code of conduct for COVID but if it's in the lease, it's far more straightforward. The commercial space, depending on the industry, has seen some big changes.

Landlords have had to nurse tenants throughout the last six months, particularly in the hospitality sector where they were shut down or had heavy restrictions with seating and capacity. COVID will have a long term effect on commercial real estate and we've seen that already.

Now in this 'COVID normal' market, it's going to be much more common for landlords to offer incentives. Speak to agents out there and find out what the going rate is and what's expected/fair. Can I get three months free rent? Can I get six months free rent? Is 50% fit out possible? It also comes back to the length of lease because a landlord is not going to give you six months free if you've only signed a one year lease to start; it's all about the term of lease. The perception is that landlords have the money because they're the one with the property, therefore they can afford half rent or whatever it might be. Unfortunately people forget that although there's investors with multiple properties, there's also mum and dad investors with just one commercial property that may be feeling the brunt of COVID and can't afford to waive rent for six months.

With COVID, landlords have more pressure on them to put more effort into the fit out and have a premises ready to go because tenants aren't wanting to fit out a premise with the unpredictable future. Usually when you go into a commercial tenancy the building is leased as an empty shell and then it is really up to the commercial tenant what they do with it. Now when a tenant leaves and the property becomes vacant, landlords are having to make it more attractive for people to lease the premises. So what we're seeing now is instead of rent free periods, sharing fit-out cost is becoming more common.

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Fit Outs

If you're planning on fitting out a premise you put forward a proposal; an agreement to lease with what you want to do to the property and that needs to be approved by the landlord. For most tendencies it's the tenant's responsibility to coordinate that and pay for that fit out but as discussed, we're not seeing as many businesses refitting properties given the current economic climate so landlords are providing some incentives to help out. Generally when you come into a lease you explain what you want to do and get some costings together and then you'd sit down and negotiate with the agent or the landlord as part of your rental agreement.

In some cases if the previous tenants used the space for a similar purpose e.g. office, they may leave behind a reception counter or kitchen but there's other tenancies where the space will be used for something totally different so it'll be completely stripped bare at the tenants expense. If you spend the money on putting things in then you're also expected to take them out at the end if the next person doesn't want it.

If your lease is within a large shopping centre there are different rules again as they have their own agreements and requirements when it comes to fit outs. It's important to get some really clear independent advice on a lease arrangement in those shopping centres as they vary from a standard lease agreement. It's about knowing the building you're going into and getting that information from the agent.

Summary

If you're starting out in the commercial leasing environment, get someone independent to help you through it. Find someone who can help you as an advocate in negotiating the best arrangement for you as a tenant. Thank you to Josh from Harris Real Estate for his insight into commercial leasing.



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