

Splitting up the costs

Knowing the difference between the costs met by the landlord and the tenant is essential information for the non-residential investor.

Council rates, land tax, water supply, maintenance, contract fees... knowing what costs can and can't be passed on to the tenant of a non-residential property may have a major bearing on whether the astute investor actually goes ahead and purchases the property.

While different states may have different laws in relation to tenant responsibilities, there's a general acceptance across the nation of what non-residential tenants can expect to pay. A range of costs can be passed on to the tenant in the nonresidential market that would never be allowed in a normal housing situation. Ultimately, it generally all comes down to negotiation in the non-residential rental market.

The general consensus among commercial and retail property experts is that both parties should and will receive legal advice rarely employed in the residential sector and that costs, however small, need to be sorted out before signing the lease.

Painting and fit-out requirements which, respectively, rarely and never enter into residential discussions, are costs the nonresidential owner may wish to include in the lease.

It depends on the lease

Real Estate Institute of the Australian Capital Territory deputy president Michael Wellsmore, who specialises in the nonresidential area, says rental costs don't vary greatly across the states. He explains that landlords can offer tenants one of four different types of leases - gross, net, double net or triple net.

Wellsmore says leases are fairly standard across Australia, with gross leases the most common form of non-residential agreement. The exact costs, he adds, are often worked out between the parties, often after seeking legal advice.

"How long is a piece of string," he asks. "It depends upon the agreement the two parties have because there are a range of leases which are as broad as the parties agree. In most commercial leases, you'll find there are solicitors acting for both parties.

"With a gross lease, the tenant will pay an amount of money as simple rent and the owner will pay all the charges. In that sort of lease, there's then a provision to allow for the tenant to pay for an increase in costs over what is termed a base year. For instance, the base year on a new lease would be 2007 and if the rates go up in 2008, the tenant would pay any increases in rates and taxes over that period.

"In a normal gross lease for strip shopping or office accommodation, there will be charges over and above a base year. There is some argument over the difference between a double net and a triple net lease. In a triple net lease, for instance, the owner leases out the bare shell and the tenant pays all the outgoings such as rates, taxes, fit-out and cost of electricity.

"The difference between a gross lease and triple net lease is that there's a major variation in what the actual rent per square metre might be.

"There might be \$30, \$40, \$50 per square metre variance or higher between these types of leases but the reason some tenants are happy with that is that it allows them to manage all those costs and perhaps even bring those costs down."

Wellsmore says the amount the landlord tries to charge tenants tends to be selfregulating in a competitive market. If the landlord is imposing too many additional costs, he suggests, the tenant will tend to look for a cheaper rate per sum. Among these, owners of retail premises sometimes pass on charges for promotional requirements but these charges need to be spelled out in the lease.

What the landlord forks out for

Property management director for Tim Green Commercial in Sydney, Danny Condell, says while a range of charges can apply in a commercial or retail lease, capital costs can't generally be passed on for any class of property. The operative word, however, is "generally".

"There are exceptions such as a 'fully repairing' type of lease, where the property may be a heritage premises that requires extensive capital repairs. In this case, a minimal rent may be agreed on the basis that the capital works are paid for by the tenant.

"Other standard charges that aren't usually included in allowable outgoings are leasing fees and advertising fees for vacancies. In New South Wales, also, the Retail Leases Act doesn't allow you to pass on owner's legal costs to the tenant.

"Non-residential leases differ greatly from residential for obvious reasons. Obviously everyone's got to have a roof over their head so they legislate heavily to protect tenants who aren't renting for any sort of business or financial reason.

| WHAT GOES? | | |
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| Here's what you can generally charge the non-residential tenant: | | |
| | Commercial | Retail |
| Capital improvements | x | x |
| Air con repairs | x | x |
| Restorative painting | ✓ | ✓ |
| Fit-out | ✓ | ✓ |
| Carpets | x | x |
| Structural repairs | x | x |
| Council rates | ✓ | x |
| Maintenance | ✓ | ✓ |
| Lease fees | x | x |

"But it also differs between commercial and retail. There's a general acceptance in commercial that all parties are business savvy so the lease is more open than it might be for retail, where you have more mum and dad operators running shops and, within each state, there's lots of protection there for them."

Condell says in most retail and commercial leases, a standard "make good" clause is often included to ensure the premises is returned to its previous condition.

"When a property is handed over in a certain condition, the clause puts the onus on the tenant to return it in this condition at the end of the lease - fair wear and tear excepted," he adds.

"For example, a business leases a vacant office floor and then proceeds to install a fit-out and change the layout of the lighting, air conditioning and sprinklers. At the end of the lease, all the fit-out needs to be removed and the abovementioned services returned to original layout and any damage due to installation has to be made good. This may include painting and possibly replacement of carpet, if so specified. "

Sydney solicitors and notaries Coleman and Greig, which has produced a guide to commercial, industrial and retail leasing, says it's imperative any and all documentation meets the landlord's needs before it's presented to the tenant.

The company's commercial leasing principal, Andrew Grima, says while many outgoings are negotiated between the parties, some costs such as capital improvements are rarely met by the tenant. Legal costs, he adds, are always met by the landlord.

"In a general commercial or industrial lease, it's what the parties can negotiate and that can be anything from tenants paying rent only to all the various outgoings such as council rates, water rates, land tax and strata levies," Grima elaborates. "If there are strata levies involved, that will generally cover all the outgoings relating to the building and surrounds such as gardens.

"Under the New South Wales Retail Leases Act, there are no restrictions on what outgoings you can pass on to the tenant but there are restrictions on legal costs. That means you can't pass on the cost of lease preparation to the tenant, regardless of negotiations."

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