

## **LANDLORD & TENANT LAW BULLETIN 1 November 2016**

### **Break clauses in commercial leases**

*Please note that this e-bulletin just provides an overview of the law in this area. You should talk to one of our team for a complete understanding of how it may affect your particular circumstances.*

This briefing highlights the practical issues that a tenant should consider when exercising a break clause in a commercial lease.

#### **What is a break clause?**

- A break clause can be included in a fixed-term lease allowing either the tenant or landlord to terminate the lease early. Some leases include breaks for both the landlord and the tenant.
- Exercising a break clause brings the lease to an end.
- Depending on how the lease has been drafted, the right to break the lease may:
  - arise on one or more specified dates; or
  - be exercisable at any time during the term of the lease on a rolling basis.
- A formal notice is normally required to exercise a break clause.
- A break clause may only be exercised if any conditions attached to it have been satisfied. For example, if the tenant seeks to exercise its break clause, the clause might specify that the tenant must give vacant possession of the property at the date when the lease is to come to an end. A break clause will be strictly construed by the courts and any conditions must be strictly performed.

#### **Practical issues for tenants to consider when exercising a break clause**

- Once a notice exercising the break clause has been served, it cannot be withdrawn. This means that a tenant must be sure that it wants to end the lease early before serving the notice triggering the break right. Even if the landlord and the tenant both agree to waive the break notice, this does not prevent the lease from ending. Instead, the agreement between the landlord and the tenant will be deemed to constitute the grant of a new lease that will take effect immediately after the original lease ends under the break clause.
- Tenants should comply with all the relevant requirements in the break clause and keep evidence of their compliance to help protect their position.

- Serve the break notice in good time and strictly in accordance with the terms of the lease. The lease may contain provisions relating to serving the break notice that are not in the break clause itself. If there are two or more tenants, usually the break clause must be exercised by all of them.
- Keep evidence of the method of posting or delivery of the notice. If there are no provisions in the lease that relate to serving the break notice, the tenant could request that the landlord acknowledge receipt, although the landlord is not obliged to comply with that request.
- If the notice is being served by an agent, make sure the landlord is aware of the existence of the agency arrangement and the agent's authority.
- Consider carrying out a compliance audit with a surveyor's advice before serving the break notice. A tenant can then take steps to remedy any breaches of the lease to ensure compliance with its covenants. This is particularly important where such compliance is a condition of the break clause.
- Pay any outstanding sums due, even if these are in dispute. Payment can be made on a "without prejudice" basis and discussed later. Again, this is particularly important where such payment is a condition of the break clause.
- The tenant might not be aware of all the money it owes. The lease may oblige the tenant to pay interest in respect of late payments, so check if any such interest is due in respect of arrears in the past. The tenant may owe interest on historic arrears, even if the arrears have been cleared and the landlord has not requested the interest. Unless the tenant has received a demand for such interest, it may have difficulty knowing precisely how much interest is due. The tenant should try to estimate the amount due and err on the safe side when paying. The cost of over-estimating the amount due for interest is likely to be far less than the cost of remaining bound under the lease. The exact amounts owed can be settled later.
- Make sure that payments are made in cleared funds by the required date, unless the landlord has expressly agreed to accept a cheque.
- Ask the landlord for confirmation of the steps required to comply with any conditions in the break clause. In particular, the tenant may want to be sure that it has complied with its repairing obligations under the lease. In order to do this, the tenant may ask the landlord to prepare a list of items that are in need of repair, and for which the tenant is responsible under the lease. This list is known as a schedule of dilapidations.
- If a tenant agrees to carry out works to the property before the break date, be careful to ensure that the works are completed and vacant possession is given by the break date.
- Remember that there may be general obligations that apply at the end of the term of the lease, which will need to be complied with before the break date. For example, the lease may require the tenant to remove signage, reinstate alterations and redecorate the property. You should also check supplemental documents, such as any licences granted for works to the property, in case these contain obligations that are relevant to the break.
- Consider asking the landlord to accept the break notice on payment of an agreed amount as liquidated damages for any outstanding breaches of covenant. Liquidated damages are a fixed or determined sum agreed by the parties to a contract to be payable on breach by one of the parties.
- Ensure that any waiver of a break clause condition by the landlord is not made "without prejudice" and that it is clear to which condition(s) the waiver applies.

- Do not assume that the tenant is only obliged to pay an apportioned part of sums due under the lease, for the period up to the break date. The lease may require full payment.
- If the tenant is obliged to pay any sums in advance, such as rent, service charge or insurance rent, check to see if the landlord is obliged to refund any part of those sums that can be attributed to the time after the lease ends. The tenant will not normally be entitled to a refund of rent paid in advance, unless there is an express provision in the lease to the contrary.

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Kind regards



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