



You've Got A Deal: Heads of Terms - Part 5 (Dark Stores Focus)

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Sophie Henwood This is the fifth in a series of posts discussing the key points to be considered when negotiating heads of terms. In line with the other four ([one](#), [two](#), [three](#) and [four](#)), whilst our discussion is tailored to dark stores, the points raised will be equally applicable across other asset classes.

real estate
landlords
commercial property
tenants
dark stores

- **Service Charge** - If a tenant is taking a lease of part of a building or a lease on an estate (an industrial estate, or in a business park, for example), it will be required to pay a service charge. A service charge is a contribution towards the landlord's costs in maintaining, repairing and keeping in good order the common parts of a building or an estate - i.e: those parts that are used by all the tenants and not any one tenant's responsibility.

In terms of typical negotiation points:

- Service charge exclusions - The landlord will want to ensure that, as between all the tenants in the building or on the estate, it can recover its total expenditure. Tenants, on the other hand, will be looking to ensure that there are some limitations on what the landlord can recover. For example, should the landlord be able to require the tenant pay for any improvements or for remedying inherent defects or uninsured damage?

In a dark stores context, given such stores are likely to be ground floor only, is it appropriate for a tenant to be required to contribute to costs such as lift repairs when the lift itself only benefit upper floor tenants?

Service charge exclusions can be quite a contentious negotiation issue as, in the vast majority of cases, there are very good arguments both sides. It will be up to the parties to negotiate commercially what (if any) are agreed and this should be done within the HOTs not as part of document negotiation.

- Service charge cap - Many tenants try to negotiate a service charge cap so that they can be confident of their maximum financial liability to the landlord. If a landlord is going to agree a cap then it will want to ensure that it is indexed linked and revised upwards each year.
- Service charge reconciliation - The majority of tenants will want their landlord to be under an express obligation to reconcile the service charge year within a set period of the year end, for example four months. This is to avoid landlords being able to delay reconciliation for long periods before then issuing a swathe of invoices for long prior periods, thereby impacting a tenant's cash flow and ability to plan ahead.
- Reserve fund - Such a fund is usually built up to pay for one-off large items of future expenditure. For tenants, such a fund is a double

edged sword. On the one hand, they might benefit from such a fund. If a large item of expenditure arose during the term of the lease, the tenant would be sheltered from the full extent of expenditure by the fund. However, if such expenditure is not required during the term then they will have parted with monies that will only benefit future tenants.

- **Proper landlord expenses** - Tenants should ensure that items which are properly for a landlord to bear itself are not recoverable under the service charge. These might include a landlord's administrative expenses relating to other tenants; costs in respect of enforcing the tenant covenants in other tenants' leases; and costs relating to void units.
- **Buildings insurance*** - The normal position in relation to insurance is for the landlord to insure the property and for the tenant to pay a fair proportion of that insurance.

Landlords are often keen to insure, rather than requiring tenants to, so that they are in control of insurance being put in place and to ensure the values insured are correct.

The risk of a tenant not insuring, the property suffering insured damage and the tenant having insufficient funds to rectify the damage, is too great for most landlords. Small store tenants are typically companies in their infancy stages, without great financial covenant strength, and so this standard position is very much appropriate for them. Assuming that standard position, tenants will want to ensure that the landlord's obligation to insure is for the full reinstatement value, that the landlord is under an obligation to reinstate the building in the event of insured damage and that any shortfall in the insurance proceeds is met by the landlord. Tenants should also check that, in the event of insured damage, the rent is suspended and that if the property is not reinstated by the end of the rent suspension period the lease can be terminated.

Landlords will want to ensure that the tenants pay for a revaluation of the property every couple of years and that the tenants pay for loss of rent insurance as well as buildings insurance.

*Note that we are talking about buildings insurance only here. Not business, contents or any other insurance.

- **Uninsured damage** - Usually, landlords are required to insure against a set list of insured risks (ie: flooding, fire, burst pipes, etc) but only so long as insurance for those risks is available and available at a commercial rate. If insurance is not available, or is prohibitively expensive, then these risks move to being uninsured risks.

The current market position is that it is reasonable for the landlord to be responsible for damage by uninsured risks and tenants should ensure the heads of terms reflect this. Usually a landlord will be able to choose whether or not to reinstate uninsured damage within x months of the damage happening (at its own cost) and, if the landlord does not do so, either party should then be able to terminate the lease.

In our next post, we will discuss alienation and group sharing.





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