

## Commercial **Property**

### Upwards only rent review legislation 'a waste of time'



Grafton Street, Dublin 2: a shop owner's campaign to end the principle of upwards only rent reviews when his landlord increased his rent has led the Government to change the law.

Photograph: Matt Kavanagh

In today's business environment no commercial tenant in his right mind would take a long lease for over 15 years - and upwards only rent reviews are on the way out without any need for legislation says **BILL NOWLAN**.

In various recent editions you have extensively covered protests by property owners and their advisors about the banning of upward-only rent reviews as well as the cheering by some tenants for this new legislation. A little perspective is required on the issue. I personally think this legislation was a waste of legislative time.

First this change does not apply to existing leases. If a tenant holds under an old lease he is stuck with the old regime until the lease expires so the pressure group of tenants who sought this change will not directly benefit in the short term. No doubt they are disappointed. Secondly the rest of the world, apart from the UK, works very well without upwards only rent review mechanisms and the market has been moving that way without the need for any legislation.

Thirdly and more importantly, most of your commentators are looking at this change to the working of the Irish property market through their rear view mirrors. They don't seem to realise that the world of property has changed.

In today's business environment no commercial tenant in his right mind would take a long lease for over 15 years and it would more likely be for five years or 10, with breaks to coincide with rent reviews.

The world has changed beyond recognition from the time of the first 35-year lease with upward only rent reviews, which was back in 1966 when the so called "institutional lease" model was imported by Hume Holdings Ltd for Hume House, Ballsbridge, Dublin 4.

This lease model was adopted then because Ireland, in 1966, had a strict landlord and tenant regime dating back to 1931 which was dominated by the courts, who interpreted this legislation to set rents at about 66 per cent of the fair open market rent.

So in 1966 the reason for long leases was to keep leases on new commercial development out of the courts for as long as possible and to create a mechanism to adjust rents for inflation.

Since 1966 the Irish commercial property scene has changed dramatically as follows:

New buildings are the norm in business and no longer scarce – as in 1966.

Our landlord and tenant law has been updated from a 1931 model to a 2008 one reflecting equality between tenant and landlord. The old tenants' paradigm of "owning" their leased property has changed to one of a payment for a facility with no rights other than those in the contract document: just like renting a fork lift truck or a hotel room!

The courts now set rents at fair open market rents in cases that come to them.

The commercial market has matured with balance between tenants and landlords.

But, most importantly, the business environment now focuses on a three to five-year business cycle.

No business tenant wants to commit himself to his premises for longer than his business plan or a foreseeable extension of it. In our fast changing world, flexibility in business is the key to survival and prosperity.

The business attitude is that my business could be half its size or double its size in five years and flexibility is required.

This is why both American and European leases have been for periods of five years with an option to extend for a further five years, ie 10 years (or three, six or nine in the case of France or Belgium). At the break date after five years, the tenant and landlord then have the option to negotiate as equals with the tenant having the right to terminate.

The other mechanism that has recently been imported to Ireland from the USA and Europe in the retail property sector is turnover rents or base rents with turnover top-up rents in lieu of rent reviews.

Indeed the Commercial Property pages have been reporting that most tenants are seeking and getting such flexible leases.

Look to the recent letting The Irish Times reported of an office building in Sandyford (on a 10-year lease with break at five) or nearly all retail deals done by Zara and HM and several shopping centres, which are on a turnover basis.

As an investment advisor I would love to have all my clients' buildings let on fixed 35-year or even 15-year leases with upward only rent reviews. But the reality is that that era is gone.

Those who say the new system can't work, should take a trip to the USA and Europe and look at the thriving property investment markets there.

I strongly suspect that the UK, the last bastion of the long lease and the upwards only rent review, is fast succumbing to the reality of the business environment.

The Government's introduction of this legislation and all the hullabaloo is a total waste of time as in real life this train left the station several years ago.

The only slight reservation is that in this knee jerk and unnecessary reaction to a tiny pressure group of occupiers, a form of structured financing of large scale urban renewal may have inadvertently been lost and this may have to be addressed in due course.

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