

Looking for a New Space to Call Home for Your Business? Three Common Types of Commercial Leases – Their Pros and Cons

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Practice Area: Business and Corporate Law & Real Estate

In commercial real estate leasing, the three most common types of leases are: a Gross Lease, a Triple Net Lease, and a Modified Triple Net Lease. While the terms of any given lease will vary from building to building and landlord to landlord, this *Update* covers the basic elements of each of these three lease types.

Triple Net Leases

Triple Net Leases (or a net-net-net lease) are typical in a situation where there is a single tenant building and the lease will be long-term. A triple net lease is as close as a tenant can get to "owning" the building without actually having their name on the deed. The rent payable to the landlord is net of taxes, insurance, and maintenance expenditures. A tenant will pay a monthly base rent, along with property and real estate taxes, insurance on the building, and substantially all maintenance costs. Maintenance costs in a triple net lease will generally include both operational expenses and capital expenditures. Operational expenses will include recurring expenses such as cleaning, landscaping, snow removal, and routine maintenance, while capital expenses include extraordinary, non-routine expenses such as repair of structural components (like the roof) or replacement of the HVAC system.

Pros: Higher level of control over the building; base rent is usually lower than the other two types of leases.

Con: High level of responsibility for all elements of the building with substantial added cost responsibilities.

Modified Triple Net Leases

A modified triple net lease is commonly seen in a multi-tenant commercial facility. Rent will be net of taxes, insurance, and operational maintenance expenditures. Typically, capital expenditures will be handled in one of two ways: (1) the expenditures will be the responsibility of the landlord or (2) the expenditures will be depreciated, and the tenant will pay for depreciation during the lease term. For example, if a newly installed HVAC system has a useful life of 15 years, and the lease term is 5 years, the tenant will be charged for 5 years of the HVAC's useful life. Common area utilities and operating expenses will often be assessed against the tenant in this type of lease with the landlord typically estimating the expenses and charging the tenant for its pro-rata portion based on the tenant's square footage, with a reconciliation of actual expenses versus budgeted expenses to be made at year end.

Pros: Transparency in building operating expenses; base rent is generally lower than a gross lease.

Con: Triple net costs are often not fixed and are subject to fluctuation (usually increases).

Gross Rent Leases

Gross rent leases are routinely found in residential settings, however this type of lease can also be found in some commercial spaces (such as shopping centers). The gross rent lease is "all-inclusive." The tenant pays a set rental rate, and the landlord is solely responsible for all other expenses (including taxes, insurance, and maintenance). While this lease is very tenant-friendly, the rental rate will usually be higher than the base rent of a triple net or modified triple net lease in order to offset the costs that the landlord will incur.

Pros: Easy for tenant to budget for lease costs; no responsibility for maintenance costs.

Con: Rental rates can be significantly higher than a triple net or modified triple net lease.

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