



Exercising an option under a retail or commercial lease

Author: [Chris Alfonso](#)

Email: chris@ealawyers.com.au

Date: Monday October 3, 2022

If a retail or [commercial lease](#) includes an option period, it typically will require that the Lessee exercise their option if they intend to renew the lease. The option period does not automatically renew. The lease will usually have specific requirements that the Lessee must follow in order to correctly exercise their option, allowing them to require that the Lessor provide a new lease to them for the term of the option period.

Every retail or commercial lease is different, and the terms of the lease should be considered to understand what applies in your particular situation. This blog is intended to be general in nature.

What is an option in a retail or commercial lease?

Many retail and commercial leases will include an option to renew the lease. This is a right for the Lessee to require that the Lessor provide to them a new lease with a further term.

If a lease does not include an option period, then the Lessee would need to negotiate a new lease term with the Lessor, and the Lessor could refuse to allow the Lessee to continue to occupy the premises.

The Lessee is usually able to decide whether or not they will exercise their option. This will give the Lessee the right to decide whether they will continue the occupation of the premises under the lease, or whether they will allow the term of the lease to end, subsequently ending their occupation of the premises.

The option lease (that is, the renewed lease) will have nearly identical terms to the current lease. The current lease will specify any clauses that are to be deleted when the lease renews. The existing lease will usually specify any clauses that are to be deleted in the new lease, and outline how the initial rent in the new lease is to be calculated (for example, by a review of market rent, a fixed percentage or by CPI).

When do I need to exercise the option in my lease?

The lease will specify the timeframe during which the Lessee must exercise their option. This is often a period of time several months prior to the terminating date on the lease.

Common timeframes are between 6 months to 3 months or between 9 months to 3 months before the terminating date on the lease. This period will depend on the terms of the lease.

Crucially, the timeframes contained in the lease are strict.

If the Lessee does not exercise their option during the dates specified in the lease, then the right to require a Lessor to provide a new lease term will be lost. If a Lessee waits until the end of the option period to exercise their option, they may be at risk of inadvertently missing the deadline. If a Lessee intends to exercise their option, it is advisable to do so well prior to the end of the option period.

How do I exercise the option in my lease?

Usually, the option is exercised by providing the Lessor with written notice of the exercise the option.

Any notice should be unambiguous as to the intention of the Lessee to exercise their option.

The terms of the lease may specify what types of delivery of notice (eg, mail, hand delivery or email) are acceptable, and exclude other types of delivery of notice. The terms of the lease should be carefully considered prior to exercising the option.

The Lessee should also consider obtaining an acknowledgement or proof of receipt from the Lessor to confirm they have received the notice exercising the option within the relevant option period. This is particularly important if the option is being exercised only shortly before the deadline for the option period.

For example, the *Evidence Act 1995* (NSW) includes a presumption that mail is not received by the recipient until the 7th business day after sending unless it can be proved that the mail was received sooner. If there is no acknowledgement of receipt from the Lessor, or if the Lessee has no other evidence of the Lessor receiving the correspondence in the mail, then the Lessee may inadvertently miss the deadline for the exercise of option even though the letter was sent prior to the expiry of the option period.

Can a Lessee change their mind and cancel the exercise of option?

No.

If a Lessee exercises their option in accordance with the terms of the lease, it will result in a binding and enforceable agreement for the new lease term to arise. The Lessee would not be able to change their mind and refuse to take the new lease, unless otherwise agreed by the Lessor. The Lessor could legitimately decide to rely upon the agreement for the new lease and seek to enforce its provisions against the Lessee.

The Lessee should ensure they wish to take the lease for the option term prior to exercising their option.

When can the Lessor refuse a new option in a commercial or retail lease?

If there is an option within a lease and the Lessee validly exercises their option, then a Lessor is bound to provide the Lessee with the new lease for the option term, unless otherwise provided in the terms of the lease.

The lease will usually prevent the Lessee from exercising their option if they are in breach of the conditions of the lease, including if there is overdue rent at the time of the attempted exercise of option.

Will I be reminded when my option period starts?

The Lessor or any managing agent engaged by the Lessor is not required to advise or remind a Lessee that the option period is upcoming. The Lessee remains responsible for exercising the option correctly within the timeframes specified under the lease, and in accordance with the terms of the lease.

Most lawyers also will not record the dates that Lessees need to exercise their option within, nor will they remind Lessees of the relevant times. It is crucially important that Lessees have a mechanism for recording the dates for exercising their option.

What can a Lessee do if the option was not exercised correctly?

If an option was not exercised correctly and the period in which the option could be exercised has expired under the terms of the lease, then the lease will expire on the terminating date or the parties may enter into a month-to-month holding over period.

If the Lessee then seeks to take the new option lease or extend the term of the current lease, they could only do so with the agreement of the Lessor. The Lessee would no longer be able to unilaterally require that the Lessor provide the Lessee with the option lease.

If the Lessor refuses to extend the term or grant the Lessee a new lease and seeks to have the Lessee removed from the premises, then the Lessee may be required to vacate the premises (which typically will also require that the Lessee "make good" the premises).

Conclusion

If a retail or commercial lease includes an option period, then the terms of the lease need to be carefully followed if the Lessee intends to exercise their option.

Need help with your retail or commercial lease?

E&A Lawyers have significant commercial law experience, in particular with drafting and reviewing commercial leases. Contact one of our commercial lawyers for advice and assistance about your lease.

Contacting E&A Lawyers

For more information or to arrange a consultation with a lawyer, you can call or email us.

[02 9997 2111](tel:0299972111)

info@ealawyers.com.au

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