

Option to Purchase, and Right of First Refusal

Option to Purchase

- right to buy the land currently under the lease at a pre-determined price if the tenant performs all terms and conditions of the lease, lasting until a specified time has expired and could be within lease term or at end of lease.
- Usually used when a tenant knows that they want the land or that they may want it within a certain time period. Landowner needs to be sure they indeed are willing to sell the property.
- In addition to rent the tenant will pay a non-refundable premium on top of the negotiated rent price often called an “option fee” which is an initial payment the tenant makes based on a percentage of the home’s value (generally between 2.5-7%) that will go towards the down payment at the end of the term.
- The tenant will also pay a “rent credit”, an additional premium that also goes towards the down payment at the end of the term.
- The owner of the property does have to sell the property if tenant meets all the terms and conditions

Example:

- Jane a landowner, enters into a lease-to-own agreement with Jill, her tenant who has been farming for many years with a thriving business and wants to continue to grow on land that one day will be hers Jill and Jane have talked about how to best arrange the purchase of Jane’s land and decided to have a lease for two years and then Jill will have the option to purchase the land at an agreed price. Jill puts down an option fee of \$2500.00 to secure the option to buy the land when the lease ends. Based on the land’s value a fair monthly rent would be \$500.00 before rent credits and since Jill wants to own the land at the end of the lease she will pay rent credit that goes towards her down payment. Jill and Jane agree that \$100.00 is a fair monthly rental credit, so when the lease goes into effect, each month Jill pays \$600.00 to Jane—\$500.00 for renting the property, and \$100.00 per month to go towards her eventual down payment for the land.

Right of First Refusal

- Indication that should the landowner ever wish to sell the land, the tenant is then given the right to buy the land at the same terms and conditions offered by another purchaser at some point in the future.
- If the owner receives an offer that they want to accept, the tenant with a right of first refusal has a specified amount of time to match that offer and buy the property.
- Usually used if the tenant wants to have the opportunity to buy the land should it come on the market. Works for landowner if they are not ready to make commit to sell property at current time but can still offer tenant ability to own property if they do decide to sell in the future.

What can you negotiate in your lease agreement or arrangement?

Between landowner and tenant you need to decide on:

- Option fee
- Rent credit
- Length of lease (usually 1-3 years)
- Price of the land

Also discuss and consider:

- Maintenance and repair responsibilities
- What happens if the value of the home changes significantly
- What will happen if you need to extend the terms
- Opt-out clauses

What to include in your agreement?

It is suggested that the landowner obtains legal advice in creating the contract to ensure all issues are considered and both the landowner (and tenant) are protected with respect to the difficulties and expense that the landowner may need to enforce in purchase agreement and if tenant stops making payments etc.

Some common clauses in agreement are based on the following:

- **Conditional on Legal Advice – Agreement for Sale:** The Seller agrees to carry the remaining balance of \$_____ by way of an Agreement for Sale at an interest rate of _____%, _____ year amortization, _____ year term, principle and interest payments of approximately \$_____ per month. The parties agree to sign a formal Agreement for Sale. This offer is subject to the Buyer and Seller receiving satisfactory legal advice with respect to the Agreement for Sale by _____, 20____.
- **Conditional on Legal Advice-Lease with Option to Purchase:** This offer is subject to the parties negotiating and executing a formal agreement with the benefit of legal advice by _____, 20_____.
- **Option to purchase:-**Tenant, upon satisfactory performance of this lease, shall have the option to purchase ("Option") the land described herein for a PURCHASE PRICE OF \$xxx.xxx,xx beginning with the term of this lease and expiring on date ,20_____ (date of lease expiration) OR ON DATE OF SALE, or, if the lease is earlier terminated, at that time. Tenant shall notify Landlord in writing, prior to the termination date of the option, of Tenant's intent to exercise the option to purchase. When exercising the option, Tenant shall also deposit with Landlord the sun of \$xxx,xx as a option fee/deposit towards the purchase price of the land. Upon exercise of this option by Tenant, a closing shall take place within _____days.
- **Additional terms relating to option to purchase:** Tenant(s) agree to take the necessary steps to become 'credit ready' to purchase the residence within a twelve (12) month period. Upon written request a minimum of thirty (30) days, prior to lease expiration, an extension of up to twenty-four. (24) months may be granted with an approved plan of action

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