

Key Considerations for Solar Panel Rooftop Leases

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Solar panel rooftop leases have become increasingly popular among real estate owners in Florida, and beyond, as an additional revenue generator for commercial properties, in large part because owners often perceive them as low-hanging fruit: a steady cash flow from the tenant to install and operate solar panels on underutilized portions of the owner's property.

Consequently, for property owners holding mortgages, we have seen rising requests for mortgage lender consent to borrowers' entering into rooftop solar panel leases. Putting the immediate business benefits aside, mortgage lenders and property owners must carefully evaluate the legal and financial implications before entering into such agreements. While these leases can generate additional revenue from otherwise unused rooftop space, they also introduce risks that must be managed effectively. Below, we break down the key considerations, lease-specific issues, and financing concerns associated with solar panel leases.

General Considerations and Risks

Before entering into a rooftop solar lease, landlords and lenders must conduct thorough due diligence on the solar power provider ("SPP Tenant"). Important factors to assess include:

- **Financial Stability & Expertise:** The SPP Tenant must demonstrate financial strength and operational expertise. If the tenant is affiliated with the landlord, lease terms must be scrutinized to ensure they are arms-length transactions, particularly under CMBS Special Purpose Entity loan requirements.
- **Licensing & Permits:** The SPP Tenant must obtain all required governmental approvals, including zoning compliance and environmental clearances.

- **Structural Integrity & Insurance:** Landlords should provide lenders with structural engineering reports confirming the roof's ability to support the installation, and ensure that insurance policies cover potential risks such as leaks, fire hazards, and damage to the roof and property at no additional cost. Lenders should be named as an additional insured or a loss payee, as applicable.
- **Impact on Existing Roof Warranties:** The lease should include assurances that the installation does not void or compromise existing roof warranties. The SPP Tenant should provide indemnification for any related damages.
- **Potential Property Sale & Valuation Concerns:** The presence of a long-term rooftop solar lease may affect future property sales. Outdated lease terms could deter buyers or impact property valuation, particularly if newer solar providers offer better financial terms.

Key Lease Issues

Negotiating favorable lease terms is critical for landlords and lenders. Key considerations include:

- **Rent & Term Structure:** Lease payments should be structured to provide reasonable returns, including rent increases, over the lease term (often 20+ years), while accounting for potential technological advancements that may render equipment obsolete.
- **Description of Leased Premises:** The lease should clearly identify (graphically and by legal description) the leased premises, including any required staging, storage and access areas.
- **Approval & Security Measures:** The lease should include clear outside dates for obtaining necessary approvals and permits, commencement of rent payments, and security measures, such as performance bonds or escrowed funds, to ensure project completion.
- **Maintenance & Repairs:** Clearly define responsibilities for roof maintenance. The landlord should retain the ability to repair or

replace the roof without unreasonable interference from the SPP Tenant.

- **Assignment & Easements:** Landlords should restrict the SPP Tenant's ability to freely assign the lease and ensure that any easements granted terminate upon lease expiration to prevent clouding title.
- **Regulatory Compliance:** The lease must require adherence to all laws and allow the landlord and lender to review and approve improvement plans. Future upgrades should not exceed the originally agreed space or load without landlord and lender consent.
- **Lease Termination & Removal of Equipment:** Landlords should negotiate provisions requiring the SPP Tenant to remove equipment at the end of the term, or earlier termination of the lease, and restore the roof to its original condition. Financial security should be provided to cover these decommissioning costs.
- **Lender Rights & Protections:** Lenders should have the right to consent to the lease, and any construction contemplated thereby, and any amendments thereto.

Financing and Power Purchase Agreement ("PPA") Considerations

When an SPP Tenant seeks financing for the solar installation, additional risks arise:

- **Construction Loan Implications:** The SPP Tenant may finance the project by obtaining a construction loan. The construction lender will most likely require a subordination, non-disturbance, and attornment agreement ("SNDA") from the mortgage lender to make sure that the mortgage lender cannot terminate the revenue paid to the SPP Tenant through the sale of the solar power that is produced after the foreclosure of the mortgage. However, lenders may be reluctant to be bound by related power purchase agreements over the long term.
- **Potential Foreclosure Issues:** If the SPP Tenant defaults, the construction lender may foreclose, raising questions about ongoing operations and responsibility for maintaining the solar system.

- **Ensuring Limited Liens:** Any financing arrangement should clearly specify that liens apply only to the solar equipment and not to the underlying real estate.
- **PPA Risks for Landlords:** If a landlord is required to purchase power from the SPP Tenant, the agreement's pricing, duration, and termination rights should be carefully evaluated. Lenders should have the ability to terminate the PPA following foreclosure.
- **Regulatory & Tax Credit Considerations:** The SPP Tenant's financial model may depend on tax credits, which are subject to political and regulatory shifts. If incentives expire, the tenant may abandon the project, potentially leaving landlords with stranded assets.

Conclusion

While rooftop solar leases offer opportunities for additional income, they also introduce significant legal and financial complexities that should be addressed with the help of qualified counsel to avoid costly headaches down the line. Lenders and landlords must conduct thorough due diligence, negotiate lease protections, and consider financing implications to mitigate risks. By addressing these critical factors upfront, they can ensure that these agreements enhance property value rather than create long-term liabilities.



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