



Coping with Corona. Managing Commercial Leases through the Pandemic

29 April 2020

Summary

In response to the ongoing COVID-19 pandemic and following consultation with key stakeholders in the commercial property sector, the Australian Government released the Code of Conduct for Commercial Tenancies (**Code**).

Blackstone Waterhouse acts for major landlords and commercial tenants - from SMEs to institutional clientele – all of whom have been impacted by the Corona Pandemic. Whilst some have been critical of the Code, we consider it reflects a necessarily pragmatic and flexible approach – aimed at taking a less legal and more commercial approach to the resolution of an unprecedented business environment.

There is no one size fits all solution for distressed commercial leases. Each requires consideration of the unique financial circumstances of the parties and a collaborative approach to working towards a mutually acceptable solution – this is not business as usual. Early and open discussions are necessary to avoid insolvencies. The focus needs to be on a pain share aimed at preserving the parties' commercial relationship.

Who Does the Code Apply to?

The Code will apply to businesses that are:

- a small to medium size commercial enterprise with an annual turnover of less than \$50,000,000; and
- eligible for the Australian Government JobKeeper program.

If the lessee falls within the above criteria, the Code applies to both parties.

Purpose of the Code

The purpose of the Code is to provide a framework to manage financial and cash flow risk during the COVID-19 pandemic in a way that balances the interests of landlords and tenants. The Code has set out a list of 11 overarching principles for landlord and tenants to observe which include:

- Landlords and tenants share a common interest in working together, to ensure business continuity, and to facilitate the resumption of normal trading activities at the end of the COVID-19 pandemic during a reasonable recovery period;
- Landlords and tenants will be required to discuss relevant issues, to negotiate appropriate temporary leasing arrangements, and to work towards achieving mutually satisfactory outcomes;
- Landlords and tenants will negotiate in good faith;
- Any agreed arrangements will take into account the impact of the COVID-19 pandemic on the tenant, with specific regard to its revenue, expenses, and profitability. Such arrangements will be proportionate and appropriate based on the impact of the COVID-19 pandemic plus a reasonable recovery period.

The above list is non-exhaustive and relies heavily on good faith negotiations taking place between landlords and



tenants across the country. The Code appreciates the uniqueness of each commercial tenancy and envisages that a tailored and appropriate outcome for each specific tenancy will need to be reached.

Leasing Principles

In addition to the overarching principles, the Code mandates the following leasing principles that apply in individual negotiations between landlord and tenants as soon as practicable on a case-by-case basis:

1. No Termination:

Landlords must not terminate leases due to non-payment of rent during the COVID-19 pandemic period (or reasonable subsequent recovery period).

2. Commitment to Lease:

Tenants must remain committed to the terms of their lease, subject to any amendments to their rental agreement negotiated under this Code. Material failure to abide by substantive terms of their lease will forfeit any protections provided to the tenant under this Code.

3. Rent Reductions in Proportionality:

Landlords must offer tenants proportionate reductions in rent payable in the form of waivers and deferrals (as outlined under "definitions," below) of up to 100% of the amount ordinarily payable, on a case-by-case basis, based on the reduction in the tenant's trade during the COVID-19 pandemic period and a subsequent reasonable recovery period.

4. Rental Waivers:

Rental waivers must constitute no less than 50% of the total reduction in rent payable under principle #3 above over the COVID-19 pandemic period and should constitute a greater proportion of the total reduction in rent payable in cases where failure to do so would compromise the tenant's capacity to fulfil their ongoing obligations under the lease agreement. Regard must also be had to the Landlord's financial ability to provide such additional waivers. Tenants may waive the requirement for a 50% minimum waiver by agreement.

5. Rent Deferrals:

Payment of rental deferrals by the tenant must be amortised over the balance of the lease term and for a period of no less than 24 months, whichever is the greater, unless otherwise agreed by the parties.

6. Obligations to Pass on Statutory Relief:

Any reduction in statutory charges (e.g. land tax, council rates) or insurance will be passed on to the tenant in the appropriate proportion applicable under the terms of the lease.

7. Proportionality Benefits:

A landlord should seek to share any benefit it receives due to deferral of loan payments, provided by a financial institution as part of the Australian Bankers Association's COVID-19 response, or any other case-by-case deferral of loan repayments offered to other Landlords, with the tenant in a proportionate manner.





8. Other Expenses:

Landlords should where appropriate seek to waive recovery of any other expense (or outgoing payable) by a tenant, under lease terms, during the period the tenant is not able to trade. Landlords reserve the right to reduce services as required in such circumstances.

9. Payment Plan:

If negotiated arrangements under this Code necessitate repayment, this should occur over an extended period in order to avoid placing an undue financial burden on the tenant. No repayment should commence until the earlier of the COVID-19 pandemic ending (as defined by the Australian Government) or the existing lease expiring, and taking into account a reasonable subsequent recovery period.

10. No Penalty:

No fees, interest or other charges should be applied with respect to rent waived in principles #3 and #4 above and no fees, charges nor punitive interest may be charged on deferrals in principles #3, #4 and #5 above.

11. Restrictions on Enforcing Right to Security:

Landlords must not draw on a tenant's security for the non-payment of rent (be this a cash bond, bank guarantee or personal guarantee) during the period of the COVID-19 pandemic and/or a reasonable subsequent recovery period.

12. Proportional Extension:

The tenant should be provided with an opportunity to extend its lease for an equivalent period of the rent waiver and/or deferral period outlined in item #2 above. This is intended to provide the tenant additional time to trade, on existing lease terms, during the recovery period after the COVID-19 pandemic concludes.

13. No Rent Increase:

Landlords agree to a freeze on rent increases (except for retail leases based on turnover rent) for the duration of the COVID-19 pandemic and a reasonable subsequent recovery period, notwithstanding any arrangements between the landlord and the tenant.

14. No Enforcement on Trading Covenants:

Landlords may not apply any prohibition on levy any penalties if tenants reduce opening hours or cease to trade due to the COVID-19 pandemic.

Take Home Message

The Code is heavily reliant on landlords and tenants engaging in good faith negotiations and working together to reach a mutually acceptable outcome. It is worth noting that there is no obligation on either the landlord or tenant to reach a concluded agreement in which case the matter may be referred to a binding mediation process (to be governed by each state and territory).

There are no perfect solutions under the Code – there is no magic bullet or panacea to the chaos caused by the COVID-19 pandemic. Early and transparent dialogue – within a framework where you know the parameters of the Code – is another piece of the corporate jigsaw required to navigate through the present turmoil.





If you would like to discuss the impact of these changes or if require any assistance or advice on your current leasing arrangement, please contact a member of our property team for a confidential discussion.

We're Working Remotely

It's business as usual for Blackstone Waterhouse through the COVID-19 pandemic. The health and safety of our clients and staff is important to us and whilst our office is currently closed, our service to you will not change. All of our teams are working remotely and remain available by email, mobile or Zoom.





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