

COVID-19: Mandatory Code of Conduct on Commercial Leasing

The new mandatory Code of Conduct (**Code**) announced by the Prime Minister on Tuesday, 7 April gives direction to landlords on considering requests for rent relief for commercial tenants who are experiencing financial stress as a result of COVID-19, and restricts landlords from taking some types of enforcement action under leases. The Code will be given effect through legislation enacted by each state and territory, on a date to be determined by each jurisdiction.

Who does the Code apply to?

Businesses which:

- (1) are entitled to receive payments under the JobKeeper programme (the bill for which was introduced on Wednesday, 8 April); and
- (2) have a turnover of \$50 million or less.

The Code assumes that any commercial tenant eligible to receive JobKeeper payments is experiencing financial hardship.

Key principles of the Code

The Code provides that in negotiating and enacting appropriate measures, a number of leasing principles should be applied as practicable, on a case by case basis:

- (1) Under the new scheme, landlords will be barred from terminating leases or drawing on a tenant's security during the COVID-19 pandemic period (which is the period during which the JobKeeper payment is available), or any reasonable recovery period following the pandemic.
- (2) Landlords must instead reduce the rent payable under the lease, in the form of either a waiver (the rent is temporarily not payable, and will never be payable) or deferral (the rent is temporarily not payable, but will still accrue and the tenant will have to make it up later), by up to 100% of the amount ordinarily payable, on a case by case basis, in proportion to the reduction in the tenant's turnover. So, if a business is required to close, its turnover has been reduced by 100% and accordingly all rent payable should be waived. If it has suffered a 30% reduction in turnover, then rent will reduce by the same proportion – 30%.
- (3) At least 50% of the rent reduction has to be in the form of a waiver – so that it will never be payable in the future. That means up to 50% can be a deferral – payable by the tenant at a later time, after the end of the COVID-19 pandemic period.

- (4) Further, deferrals must extend over the balance of the term of the lease and be for a period of at least 2 years, and additional fees and interest can't be charged on the amount waived or deferred.
- (5) Tenants still have to perform all of their obligations under the lease, subject to the agreed rent reductions and other changes introduced by the Code. If the tenant doesn't perform their obligations under their lease, then they surrender the Code's protections – including the protection from termination of the lease.
- (6) Where arrangements negotiated between the landlord and tenant requires repayment (for example, deferrals of rent), no repayment is to commence until the earlier of COVID-19 ending (as defined by the Australian Government) or the existing lease expiring.
- (7) Reductions in statutory charges such as land tax and council rates will be passed to the tenant in the proportion applicable under the terms of the lease. While the Code isn't specific, in our view the reference to "the terms of the lease" suggest that these outgoings must already be payable by the tenant under the terms of the lease for the reduction to be passed on.
- (8) The Code provides that the landlord "*should share any benefit it receives due to deferral of loan payments... in a proportionate manner.*" Precisely what proportionality means in this circumstance, particularly where the loan may be cross-collateralised across multiple properties, is not immediately clear, but landlords will need to negotiate this provision with their tenants in good faith.
- (9) The landlord should seek to waive recovery of any other expense or outgoing payable by the tenant under the terms of the lease, where appropriate.
- (10) Landlords must freeze rent increases.

The Code in practice

The application of the Code will be different for each landlord and tenant, depending on the circumstances and financial stresses being experienced by each; the Code is intended to apply flexibly to a variety of different circumstances, rather than rigidly like legislation. For many, it will simply be a negotiation between both parties in an open, honest and transparent manner, to find a solution that conforms with the Code and allows both parties to benefit from the lease still being on foot when the pandemic ends. Where an agreement is unable to be reached, the matter will be referred to a binding mediation process.

A question that we won't know the answer to until we see the implementing legislation is what the consequence of breaching the Code will be – presumably, the Civil and Administrative Tribunal or another forum will have jurisdiction to determine disputes about the application of the Code, but we expect that some cash-strapped tenants and landlords may be limited in their ability to get legal advice and ventilate their rights through formal channels, unless lawyers are themselves prepared to discount or defer their fees.