

Commercial Tenancies – Update

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Commercial Tenancies – Update COMMERCIAL TENANCIES CODE GAZETTED ON 29 MAY 2020

The WA Government Gazetted the *Commercial Tenancies (COVID-19 Response) Regulations 2020*, on Friday 29 May 2020, following the *Commercial Tenancies (COVID-19 Response) Act 2020* passing 5 weeks earlier on 23 April 2020.

1. SUMMARY

Mostly, the situation is as was expected, but not entirely:

- “small commercial lease” tenants are entitled to rent relief;
- rent relief is [proportional](#) tenant’s drop in [actual overall turnover](#);
- rent must [usually](#) be 50% waived altogether, and 50% deferred;
- [reduction of outgoings](#) must be “considered” by the landlord, but in reality, it is doubtful that there will be a decrease unless services are no longer provided;
- [negotiations](#) are compulsory;
- [agreements](#) must be in writing; and
- the tenant may opt to extend the lease for a period equal to the deferred rent period.

Below are:

- the [key points](#) in more detail;
- expected [problems areas](#);
- an [example](#); and
- some [suggested points](#) for any agreement to cover.

2. KEY POINTS IN MORE DETAIL

- 2.1 Clause 5: [Eligible tenants](#) (see item 3 below for details) may request rent relief during the [emergency period](#)¹. The request must be [in writing](#), confirming eligibility and providing [sufficient documents to support both that eligibility and the tenant’s turnover](#). Names, addresses, business process information and financial information provided by either the tenant or the landlord during this process is only permitted to be disclosed to certain third parties, in certain specific circumstances – see clause 13.

- 2.2 Clauses 6 and 7: Following receipt of a request that meets the criteria, the landlord **MUST**:
- (a) negotiate with the tenant;
 - (b) make an offer of rent relief within 14 days of receipt of the request for rent relief²;
 - (c) provide rent relief which is at least proportional to the tenant's drop in turnover;
 - (d) at least 50% of that rent relief must be a waived², and the balance by rent deferral; and
 - (e) in some circumstances, the landlord must waive more than 50% of the rent – see item 4 below.
- 2.3 Clause 8: The rent relief agreement must be reduced to writing, in the form of a formal variation or an agreement.
- 2.4 Subclauses 9(1)-(5): Unless otherwise agreed between the landlord and tenant, the landlord must not request payment of deferred rent until the earlier of:
- (a) the day upon which the emergency period ends; and
 - (b) the end of the lease term,
- ... and unless otherwise agreed between the landlord and tenant, the deferred rent must be repaid before the later of:
- (c) the end of the lease term, or
 - (d) 24 months,
- ... with the method of amortisation to be agreed between the landlord and tenant.
- 2.5 Subclauses 9(6)-(8): The landlord **MUST** offer an extension of the lease term for a period equal to the term during which rent is deferred, unless otherwise agreed by the parties. The tenant need not accept the extension.
- 2.6 Clause 10: A tenant can ask for further rent relief if circumstances change, or rent relief provided prior to the Code coming into force was less than would be obtained pursuant to the Code – subclauses 10(1) and 10(2) or if an agreement is made and financial circumstances then change – subclause 10(3).
- 2.7 Clause 11. The landlord must **consider** waving recovery of **outgoings** that are otherwise payable by the tenant, if the tenant is unable to conduct their business from the premises, but there is no obligation to make any reduction. Most landlords will probably opt not to reduce outgoings at all. They may even go up, for example, if extra cleaning is required.
- 2.8 Subclause 11(3): The landlord **may** cease to provide, or reduce, some services at the premises, if reasonable to do so, or the tenant reasonably requests the landlord to do so.

2.9 Clause 12: The landlord:

- (a) where an [outgoing relates to multiple tenants](#) - must not require the tenant to pay an amount in respect of an outgoing that is greater than the tenant's proportional share of the reduced outgoing payable under the lease; and
- (b) must [reimburse](#) the tenant if the tenant has already paid more than that amount.

3. ELIGIBLE TENANT?

To be an **Eligible Tenant**:

- (a) the tenant must be [eligible for JobKeeper payments](#), or suffer at least a [30% downturn](#) in trade at [some point during the emergency period](#), and have a turnover less than \$50 million; and
- (b) secondly, the lease must be a [small commercial lease](#), i.e. where the tenant:
 - (i) [operates a retail shop lease](#)³; or
 - (ii) [owns or operates a small business](#)⁴, from the leased premises; or
 - (iii) is an [incorporated association](#)⁵.

4. SUBCLAUSE 7(7) - WHEN MUST THE LANDLORD WAIVE MORE THAN 50%?

The Code is [extremely vague](#) on this point, making this fraught with danger. In our view subclause 7(7) is almost impossible to apply or give advice upon! It states:

An offer of rent relief must provide that more than 50% of the rent relief is to be in the form of a waiver of rent if—

- (a) *failure to provide more than 50% of the rent relief in the form of a waiver of rent would compromise the tenant's capacity to fulfil the tenant's ongoing obligations under the small commercial lease; and*
- (b) *the landlord has the financial capacity to provide more than 50% of the rent relief in the form of a waiver of rent.*

Sorry, but your guess is as good as anyone's as to when this would apply. Each rent relief waiver request would have to be judged on its merits.

5. OTHER AREAS WHERE TROUBLE IS EXPECTED ... ?

- 5.1 Determining the actual overall drop in turnover will be difficult and it will be up to the tenant to prove a turnover drop. If rent is paid monthly, arguably it is the monthly figures that should be used. There could be a reconciliation for the whole period at the end of the Emergency Period, depending on the agreement that is reached.

- 5.2 The definition of "small business" (see note 4 below) requires that a corporation is "*managed personally by the owner or owners or directors*". There may be circumstances, where there are inactive non-executive directors, for example, which cause a small business to not qualify. It is unclear just how much personal management is required to meet the criteria.
- 5.3 Where a franchisor is the tenant and sub-leases or licences to a franchisee, the franchisor should make the application for a reduction in rent, but it is the franchisee's turnover from the leased premises which is relevant. The franchisee should also seek the reduction in the sub-lease rent, or occupation licence fees from the franchisor.
- 5.4 Please note that there are overarching negotiation obligations, which require both parties to:
- (a) cooperate;
 - (b) act reasonably and in good faith;
 - (c) act in an open, honest, and transparent manner;
 - (d) provide each other with sufficient and accurate information which is reasonable for each of them to provide in the circumstances for the purposes of the negotiation; and
 - (e) not make onerous demands for information of each other.

The parties should also consider re-negotiation triggers and ongoing disclosure obligations in any written agreement.

- 5.5 Although there are no mandated penalties for a landlord's failure to comply with the Code, if a landlord does not respond within 14 days to a written request for rent relief, the tenant could reasonably not pay anything until a response is received, leaving the landlord to have to make an application to the State Administrative Tribunal for any remedy which would otherwise be prohibited⁶, and then it would be open for the State Administrative Tribunal to mandate a rent relief amount. It is unlikely that the State Administrative Tribunal would be particularly sympathetic to a landlord in those circumstances.

6. EXAMPLE

- 6.1 A tenant of a small gift shop, which is in a shopping centre with one landlord and various tenants, suffers:
- (a) a 20% reduction in turnover in March 2020, compared to March 2019;
 - (b) a 40% reduction in turnover in April 2020, compared to April 2019;
 - (c) a 30% reduction in turnover in May 2020, compared to May 2019;
 - (d) a 20% reduction in turnover in June 2020, compared to June 2019; and
 - (e) a 10% reduction in turnover in July 2020, compared to July 2019.

- 6.2 In August 2020, turnover is back to normal.
- 6.3 The monthly rent is \$10,000.
- 6.4 The outgoings are \$5,000 per month.
- 6.5 The due date for expiry of the lease was 30 September 2021, but the tenant elects to extend by the rent deferral period.
- 6.6 The tenant is eligible for rent relief, but must request rent relief in writing, with supporting documentation to show the respective drops in turnover.
- 6.7 The landlord is not required to provide rent relief for the last 2 days of March, but rent waivers and deferrals that must be given until 29 September are as follows:

	Waiver	Deferral
April 2020	\$2,000	\$2,000
May 2020	\$1,500	\$1,500
June	\$1,000	\$1,000
July	\$500	\$500
August	Nil	Nil
September	Nil	Nil
Total		\$5,000

- 6.8 Rent was deferred during 4 months, so the landlord must offer the tenant a 4 month extension of the lease, from 30 September 2021 to 31 January 2022.
- 6.9 The deferred rent will be payable from October 2020 over 16 months, at an extra \$312.50 per month for the remainder of the term of the lease, as extended, unless otherwise agreed.

7. TERMS OF A NEGOTIATED AGREEMENT

- 7.1 We suggest that the agreement negotiated between the landlord and tenant should state that:
- (a) Turnover figures should be based on an accruals basis, if the tenant usually accounts for tax on an accruals basis, but on a cash basis if the tenant usually accounts for tax on a cash basis. Note that for JobKeeper eligibility, either method is acceptable.
 - (b) Rent relief is provided in relation to actual turnover, with an estimate given at the date when the rent is due, and a reconciliation made shortly after the end of the period, and more or less being paid, accordingly.
 - (c) The tenant is required to provide figures in a timely fashion, failing which the full rent is payable.
 - (d) The tenant is not allowed to artificially reduce turnover and the tenant must continue to provide turnover figures after the emergency period, so that the figures can be checked.

Notes

1. 30 March 2020 to 29 September 2020, unless regulations provide for a different end date.
2. Unless otherwise agreed by the landlord and the tenant.
3. A retail shop lease under the *Commercial Tenancies (Retail Shops) Agreements Act 1985*
4. A small business being as defined in the (as defined in the *Small Business Development Corporation Act 1983*), which is broad, and means a business which:
 - (a) is wholly owned and operated by an individual or persons in partnership or by a company; and
 - (b) has a relatively small share of the market in which it competes; and
 - (c) is managed personally by the owner or owners or directors, as the case requires; and
 - (d) is not a subsidiary of, or does not form part of, a larger business or enterprise.
5. An incorporated association under the *Associations Incorporation Act 2015*
6. See item 2 in our previous Commercial Tenancies update.



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As well as being a solicitor, Michael Paterson is also a software developer and is actively involved in both the legal and computer industries. He has dual qualifications in both disciplines: Bachelor of Science (Computer Science) Bachelor of Laws (Hons.) from A.N.U. (1982-1986).

With his knowledge and practical experience in the computer industry, Michael has developed a niche practice area in computer, technology, and intellectual property law. In addition, he regularly presents seminars on computer-related legal issues to various industry and professional bodies and gives guest lectures at Curtin University and Edith Cowan University.