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# COMMERCIAL TENANCY CODE OF CONDUCT

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The Commercial Tenancy Code of Conduct recommenced on 13 August 2021 and applies from 13 July 2021 to 13 January 2021.

We assisted many landlords and tenants during the first lockdown and have described some of our case studies at the end of this article. A table containing a summary of the Code of Conduct is set out at below:

## ***Overarching Principles***

- 1** Sharing the financial risk and cashflow impact of the COVID-19 pandemic between the landlord and tenant.
- 2** Landlords are to arrange bespoke, appropriate and temporary agreements with tenants.
- 3** Developing temporary arrangements mutually beneficial to the landlord and tenant.
- 4** Negotiating in good faith.
- 5** Communicating honestly and transparently.
- 6** Negotiating with regard to COVID-19's impact on the tenant's revenue, profitability and expenses.
- 7** Tailoring a negotiated agreement proportionate to the magnitude of the pandemic's impact on the tenant.
- 8** The landlord must not permanently mitigate its risk under a temporary arrangement.
- 9** Negotiated agreements will be dealt with case by case.
- 10** A negotiated agreement should consider:
  - a. The financial hardship of the tenant;
  - b. Whether the lease has expired or expires soon;
  - c. Whether there are arrears;
  - d. Whether the lease has expired and is in hold-over;
  - e. Whether the tenant is insolvent.

## ***Leasing Principles***

- 1** No termination of leases during the pandemic period.
- 2** Tenants must remain committed to their amended leases.
- 3** Material non-compliance with a lease voids the termination protection offered (number 1 above).
- 4** Landlords must offer proportionately reduced rent to a tenant who has reduced trade.
- 5** There must be a 50% minimum waiver out of the total reduction in the rent payable as negotiated and should constitute a greater percentage where the risk of the tenant defaulting is high.
- 6** Payment of deferred rent must be amortised over the lease term or over a minimum of 24 months, whichever is greater.
- 7** Any reduction in statutory charges to a property must be passed on proportionately to the tenant.
- 8** Landlords should share benefits received from the deferral of loan payments with the tenant.
- 9** Landlords should waive any expense or outgoing during the period in which the tenant cannot trade.
- 10** Repayment of deferred rent must not begin until the earlier of the end of the pandemic, or the expiry of the lease.
- 11** There should be no interest on waived or deferred rent.
- 12** Landlords must not draw on a tenant's security because of non-payment of rent during the pandemic.
- 13** Landlords must freeze rent increases during the pandemic period (except turnover based retail leases).
- 14** Landlords may not levy penalties against tenants for reduced opening hours or ceased trading during the pandemic.

## ***Features of Code***

### *Impacted Lessee*

Under the 2021 Leasing Regulations, an impacted lessee is an individual/entity which satisfies the following criteria:

1. Turnover during FY 2020-2021 was less than \$50,000,000.00; and
2. Qualifies for either:
  - a. 2021 COVID-19 Micro-business Grant; or
  - b. 2021 COVID-19 Business Grant; or
  - c. 2021 JobSaver Payment.

### *Obligation to Renegotiate*

Where an impacted lessee requests a renegotiation of the rent payable, or other terms of the lease, the landlord must renegotiate the rent and other terms of the lease in good faith, within 14 days of a request.

### *Rent Waivers and Deferrals*

Perhaps the most important principles laid out in the Code regulate rent. Under the Code, landlords must offer proportionately reduced rent to a tenant, taking into account reduction in trade, their degree of financial hardship, any arrears owed, and whether a tenant is insolvent.

Where rent is reduced, waivers and deferrals must account for not less than 50% of the reduced rent. Any rent that is deferred must be amortised and paid over 24 months, or until the expiry of the lease, whichever is earlier. The requirement to pass on reductions in outgoings has not been codified in any of the regulations.

### *Protection*

Impacted lessees are protected from being sued for damages, having their lease terminated or being subject to enforcement action while rent negotiations are on foot. Importantly, if a tenant fails to provide evidence that it is an impacted lessee and cannot demonstrate adequate loss in turnover, the protection from prescribed action does not apply.

However, a landlord will still need to attempt mediation before it can take any enforcement action while the regulations are in force.

## **CASE STUDY 1 – HAIR AND BEAUTY SALON**

We acted for a sole proprietor of a hair dressing business in the Bankstown area. Prior to the pandemic, our client had occupied the premises since 2010 and had always paid rent 2-3 months in advance. In March 2020, she highlighted that her business was not receiving bookings and she was concerned about paying rent. After the Code was released but prior to introduction of the first NSW regulation, the landlord refused to consider any form of rent relief or that our client's lease could not be terminated. A termination notice was served and the landlord foreshadowed a claim for damages in excess of \$100,000 for the remainder of the lease term on 30 April 2020. At mediation, we argued that the landlord had breached the Code by refusing to renegotiate the rent and for taking enforcement action under an impacted lease. Given those arguments, our client was able to get out of the lease by allowing the landlord to retain the bond in exchange for a surrender of the lease and release from all claims for damages under the lease.

## **CASE STUDY 2 – INTERNATIONAL STUDENT COLLEGE**

Another dispute we were involved in, with liabilities exceeding \$600,000, concerned a business college for international students. The rent for the premises was \$120,000 + GST per annum. Our client entered this 5-year lease in October 2019. With virtually non-existent international arrivals, the very basis of our client's business did not exist.

Nonetheless, the large firm acting for this commercial landlord deliberately went slow during negotiations, failing to confirm whether the rent concessions we requested were agreed. For 6 months, we engaged in correspondence that showed signs of good faith from the landlord but did not achieve a negotiated agreement. Numerous statements were made by the landlord, indicating it would accommodate the tenant's requests for relief.

Finally, one week prior to the expiry of the 2<sup>nd</sup> COVID-19 Regulation, a termination notice was served claiming in excess of \$600,000. However, a rent schedule was attached that showed no reduction had been applied to the rent in 2020. We provided financial documents that evidenced an average drop in turnover between 60-80% throughout 2020. We argued that it was unlawful for the landlord to terminate when it had acted in bad faith and deliberately stalled negotiations long enough for the COVID regulations to expire without having to concede relief. Furthermore, since the very basis for our client's use of the premises no longer existed, we said that the contract had been discharged by frustration. Since January, no attempt at enforcement action has been made and our client no longer occupies the premises.

### **CASE STUDY 3 – SHOPPING CENTRE CAFÉ**

The most recent dispute we acted in involved a large, well-known shopping centre. Our client operated a café with a seating capacity of 100 people. The café had been operating at the centre since 2013. The premises, which was less than 100m<sup>2</sup>, had a yearly rent of \$247,935.24 including GST. This did not include monthly shopping centre outgoings, or a separate licence agreement for a storage space. As cafes are low-margin businesses with high overheads, any change in economic conditions has the potential to cause severe impact to their viability.

The large shopping centre owner proposal strictly complied to the wording of the Code, affording the minimum of relief required. It did not consider all of the other charges required under the terms of the lease.

The shopping centre owner also demanded that repayment of the deferred rent commence at a time the tenant had not fully recovered or at a time when the pandemic or lease ended. The unique feature in this case was that the shopping centre owner could have ended the lease in June 2020 as it had expired. However, it chose to allow the tenant to incur huge debts relying on personal guarantees as security. We argued that the landlord was acting unconscionably and importantly, did not mitigate its losses by terminating the lease when it expired, or on one month's notice.

### **Final Thoughts**

Lease disputes will often turn on the degree of the landlord's compliance with the Code. While regulations are in place, it would be wise for landlords to offer impacted tenants proportionate waivers and deferrals. This will give landlords the benefit of enforcement rights if the tenant continues to breach the lease even after relief has been applied. For tenants, it is essential that they back up their requests with documents evidencing the required drop in turnover and they continue to observe the terms of the lease. If a tenant is able to pay a reduced rent, then they should at least pay that reduced rent while the dispute continues. If a landlord refuses to offer reductions or does not offer proportionate reductions, a lessee has a strong defence to an action for damages. The lease and your particular circumstances could also have unique features like the shopping centre lease above so it is always advisable to seek advice. While case law on this topic has been limited, we expect the courts to clarify key features of the regulations during 2021 as more disputes emerge.

If you have any questions, please contact Vinesh George on 0404077078.

V.S. George Lawyers, PO BOX 4236, BEXLEY NORTH, 2207

Ph (02) 9150 6991