

New Rules Regarding Commercial Leases During the Pandemic

The *COVID-19 Emergency Response (Commercial Leases No 2) Regulations 2020* came into operation on 15 May 2020.

The Regulations apply retrospectively from 30 March 2020, and will cease to apply on 30 September 2020.

Previously, the rules in South Australia regarding commercial rent relief and related issues during the pandemic were set out in section 7 of the *COVID-19 Emergency Response Act 2020*.

Section 7 has now been repealed, and new rules governing commercial leases during the pandemic apply under the Regulations.

The Regulations repeat most of the provisions that were previously in section 7, and then go further than section 7 did towards implementing the *Mandatory Code of Conduct – SME Commercial Leasing Principles During COVID-19* published by National Cabinet on 7 April 2020.

The obligation to negotiate

All commercial lessors and lessees (and guarantors) must negotiate in relation to the rent and other lease terms that apply during the period from 30 March 2020 to 30 September 2020.

In those negotiations, all parties must:

- make a genuine attempt to negotiate;
- act in good faith;
- have regard to the economic impact of the pandemic on the other party; and
- have regard to the *Mandatory Code of Conduct – SME Commercial Leasing Principles During COVID-19* published by National Cabinet on 7 April 2020.

The only exception is that if a new lease is entered into between 30 March 2020 and 30 September 2020, there is no requirement to negotiate. However, if a lease is renewed or extended on the same or substantially the same terms during that period, that lease is not included within this exception (accordingly, the obligation to negotiate applies to that lease).

Additional rules regarding ‘affected lessees’

If a lessee is an ‘affected lessee’, there are other rules that apply in addition to the above obligation to negotiate.

An ‘affected lessee’ is a lessee:

- who is suffering ‘financial hardship’ as a result of the pandemic; and
- whose turnover (including internet sales) in the 2018/2019 financial year was less than \$50 million.

There is no definition of financial hardship, although a lessee is automatically considered to be suffering financial hardship if the lessee receives, or is eligible to receive, a Jobkeeper payment (whether as an employer or on their own behalf). It cannot be assumed that all lessees who are not entitled to receive a Jobkeeper payment are also not suffering financial hardship for the purposes of the Regulations.

When determining turnover for the purposes of the Regulations, the following applies:

- for a franchisee, only the turnover for the business conducted at the particular premises is considered;
- for a lessee that is a 'related body corporate' of another company or other companies, the turnover of the entire group of companies is considered (to be a related body corporate, there needs to be a group structure involving a holding company or subsidiary company);
- for other situations, such as where the one lessee has multiple business premises, only the turnover for the business conducted at the particular premises is considered.

No 'prescribed action'

A lessee who is an affected lessee cannot be the subject of any 'prescribed action' from 30 March 2020 to 30 September 2020 if the lessee fails to:

- pay rent or outgoings; or
- open during mandatory trading hours.

Prescribed action includes terminating the lease, calling on a bank guarantee, pursuing distraint against the lessee's plant and equipment, and similar enforcement action.

However, if the parties have negotiated and agreed on rent relief, and the lessee defaults on payment of the agreed, reduced amount, then the above prohibition against prescribed action does not apply.

No rent increases

A lessee who is an affected lessee cannot have their rent increased between 30 March 2020 and 30 September 2020, even if the lease provides for a rent increase during this period.

The Regulations are silent on whether forfeited rent amounts under a disallowed increase can be claimed back after 30 September 2020. The position is most likely that forfeited rent amounts are permanently waived for the period from when the increase would have applied to 30 September 2020.

The Regulations are also silent about whether a disallowed increase can be implemented on and from 1 October 2020. It would be consistent with the underlying intent of the Regulations, which is to apply emergency measures only during the pandemic period, to permit all disallowed increases to be implemented on and from 1 October 2020.

Mandatory rent reduction if the lessor receives land tax relief

If a lessee is an affected lessee and Revenue SA provides the lessor with land tax relief during the period from 30 March 2020 to 30 September 2020, the lessor is required to pass

the benefit of that waiver through to the lessee by way of a rent reduction for that period. The rent reduction must be a permanent waiver, not a deferral.

Land tax liability

A lessee who is an affected lessee and who is liable for land tax cannot be required to pay land tax during the period from 30 March 2020 to 30 September 2020.

In those situations, land tax must be paid by the lessor during that period.

It should be noted that it is only lawful for a lessor to require a lessee to pay, or contribute to, land tax in certain limited circumstances. Lessors who currently require lessees to pay land tax and who are unsure about whether this practice is lawful in their particular circumstances should seek legal advice.

Mediation by Small Business Commissioner

Either a lessor or an affected lessee can apply to the Small Business Commissioner to mediate a dispute in relation to:

- whether a lessee is suffering financial hardship as a result of the pandemic;
- provision of rent relief, including a failure by the other party to negotiate as required; or
- other issues arising from the pandemic in relation to the Regulations, the lease, or the premises or the lessee's business.

Application to the Magistrates Court

If a mediation is arranged by the Small Business Commissioner and it does not resolve the dispute, a party can apply to the Magistrates Court.

The Court must consider various matters, including the following, before making any orders:

- the lessee's reduction in turnover during the period 30 March 2020 to 30 September 2020;
- whether the lessor has waived recovery of outgoings or other expenses payable under the lease from 30 March 2020 to 30 September 2020;
- whether a refusal of rent relief would compromise the lessee's ability to fulfil the lessee's ongoing obligations under the lease;
- the lessor's ability to provide rent relief, taking into account any relief the lessor may receive from third parties in response to the pandemic; and
- any reductions to outgoings in relation to the premises.

The Court has wide powers to resolve a dispute, including:

- granting rent relief (which, if granted, must result in at least 50% of the rent relief to be permanently waived);
- modifying the terms and conditions of a lease; and

- deferring the payment of rent for a maximum period of 24 months.

If an order is made to defer the payment of rent, the Court may also make an order extending the term of the lease for the period of the deferral.

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Andrew Fisher (0413 387 606) / Rick Harley (0418 848 186)

Jones Harley Toole Lawyers – 8414 3333