HERBERT SMITH FREEHILLS

COVID-19: PRESSURE POINTS: REAL ESTATE LANDLORD TENANTS UPDATE (AUSTRALIA)

08 April 2020 | Australia
Legal Briefings – By **Jane Hodder, Dinh Ptok and John Slater**

Updated as at 8 May 2020

The shockwaves from the outbreak of COVID-19 are being felt right across the Australian economy – and commercial real estate is no different. Tenants and landlords are facing the prospect of a prolonged reduction in business activity, remote working and some have endured total shutdown – none of which were anticipated at the time they signed their lease. The legal implications of this invidious state of affairs have been the subject of both considerable interest and uncertainty.

To assist, we have prepared this guide on the key legal issues arising under commercial leases in the COVID-19 environment and what Government measures are presently available for landlords and tenants.

This guide covers:

- the impact of measures imposed by the state and federal Governments in response to COVID-19 for landlords and tenants, including the Mandatory Code of Conduct (the **Code**) for SME commercial leases;
- the Government's temporary changes to the foreign investment review framework (**FIRB**);

- the typical issues arising from a tenant being unable to occupy their premises as a result of a Government-mandated shutdown; and

- practical tips for navigating a COVID-19 related shutdown for both landlords and tenants.

1. MANDATORY CODE OF CONDUCT FOR SME COMMERCIAL TENANCIES

On 7 April 2020, the National Cabinet approved a Mandatory Code of Conduct for SME commercial leasing principles during the COVID-19 pandemic. The Code provides a binding framework for resolving the fraught question of how the financial burden of the COVID-19 pandemic should be shared between landlords and their small-to-medium sized business tenants. In summary, the Code achieves this by requiring landlords to negotiate with tenants amendments to existing lease arrangements during the COVID-19 pandemic, including reductions to rent, in accordance with a set of good faith leasing principles.

Below we outline some of the key features of the Code and what they mean for landlords and tenants.

Which tenants are protected by the Code?

The Code applies to 'SME tenants', defined as businesses who:

1. have an annual turnover of up to $50 million; and

2. are eligible for the Commonwealth's JobKeeper program (although some states have required actual participation in the program – see below).[1]

The $50 million threshold will apply at the retail corporate group level for retail tenants and the franchisee level for franchises.[2] As the threshold is not assessed at the individual retail outlet level, this will exclude a significant number of well-known retailers and major national businesses from the Code's protection.

To be eligible for the Commonwealth's JobKeeper program, a business must have suffered a fall in turnover of more than 30 per cent for at least a month.

One of the overarching principles of the Code is that landlords and tenants will act in an open, honest and transparent manner, and provide to each other sufficient and accurate information (which is defined to include information generated from an accounting system and/or received from a financial institution) within the context of negotiations.[3] Accordingly, landlords will be within their rights to request that tenants verify they are covered by the Code by providing access to their business financial records.

What reduction in rent are tenants entitled to?

The foundation of the Code's approach to rental relief is a principle of proportionality which seeks to balance the financial risk and cashflow impact of COVID-19 between landlords and tenants. In essence, tenants are entitled to a reduction in rent proportionate to the decline in the tenant's turnover during the COVID-19 pandemic period and a reasonable subsequent recovery period. Rent reductions may consist of a combination of waivers and deferrals in accordance with the following requirements:

- rental waivers must comprise no less than 50 per cent of the total rent reduction allowed to the tenant under the proportionality principle (unless waived by the tenant);[4] and
- payment of rental deferrals must be amortised over the balance of the lease term and for a period of no less than 24 months, whichever is greater (unless otherwise agreed by the parties).[5]

The Code is expressly designed so that landlords and tenants can tailor their approach to rent relief to their own circumstances. However, the leasing principles impose a range of conditions on such arrangements aimed at striking an appropriate balance between the interests of both parties, which notably include:

- repayments should avoid placing any undue financial burden on tenants and should only commence until the earlier of the COVID-19 pandemic period ending, or the lease expiring, taking into account a reasonable subsequent recovery period;[6]
- tenants should be provided with an opportunity to extend their lease for an equivalent period of the rent waiver and/or deferral period to provide additional time to trade, on existing lease terms, during the recovery period after the COVID-19 pandemic ends;[7]
- rental waivers 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 (while having regard to the

landlords ability to provide such waivers);[8] and

- no fees, interest or other charges may be applied to waived or deferred rent.[9]

One of the key issues for landlords approaching these negotiations will be how to account for the potential of fluctuations in the tenant's revenue during the COVID-19 pandemic period. Given the uncertainty around how long restrictions on certain businesses and industries will remain in place, landlords may consider requesting a mechanism that allows for agreed rent reductions to be adjusted as trading conditions change.

Worked example of proportionate rent reduction

A tenant paying weekly rent of $3,000 that suffers a 60 per cent decline in turnover will be entitled to a $1,800 reduction in their weekly rent, consisting of:

- a rental waiver of no less than $900 per week; and
- a deferral of the balance of the rent reduction, to be repaid over at least a 24 month period.

If the tenant only has three months remaining on their lease, they would still be entitled to pay off the deferred rent over a 24 month period, beginning on the earlier of the end of the COVID-19 pandemic period or the lease expiring.

Protections for tenants

Tenants who are covered by the Code will be protected from the following during the COVID-19 pandemic period (which may include a reasonable subsequent recovery period):

- termination of their lease for non-payment of rent (lockouts and eviction);[10]
- rent increases (except for turnover leases);[11]
- penalties for tenants who stop trading or reduce opening hours during the COVID-19 pandemic period;[12] and
- landlords making a claim on a bank guarantee, cash deposit, personal guarantee or other security for non-payment of rent.[13]

How do landlords benefit?

The most significant benefit for landlords under the Code is that tenants covered by the Code will not be able to terminate their lease. Notably, the Code makes clear that the protections afforded to tenants are not a get out of jail free card, reaffirming that tenants must remain committed to the terms of their lease. Material failures to abide by the substantive terms of their lease will see tenants forfeit any protections provided to the tenant under the Code.[14]

Landlords must pass on savings

In keeping with the Prime Minister's statement that in commercial leasing "there will be a burden for everyone to share", the Code requires landlords to pass on to tenants the benefit of loan deferrals and relief from statutory charges such as rates and land tax.[15]

Specifically, landlords are required to share with tenants:

- any benefit from the deferral of loan payments provided by a financial institution as part of the Australian Bankers Association's COVID-19 response in a proportionate manner;[16] and
- any reduction in statutory charges or insurance in the appropriate proportion applicable under the terms of the lease.[17]

Remember, as noted above, one of the overarching principles of the Code is that parties must act in an honest and transparent manner and will each provide sufficient and accurate information within the context of negotiations. Accordingly, landlords should consider whether it may be necessary to provide tenants with details of any relief they receive in relation to tax or loan repayments.

What if the parties can't agree?

Where the parties are unable to agree on what relief should be available during the COVID-19 pandemic period, the Code provides that either party may refer the matter for binding mediation by the applicable state or territory dispute resolution process, which may include Small Business Commissioners/ Champions/ Ombudsmen.[18] As state and territory governments have implemented the Code, this dispute resolution process generally contains two steps:

1. referral of the dispute to the relevant commission for mediation; and

2. if the relevant commission certifies in writing that mediation has failed or is unlikely to resolve the dispute, the parties can bring proceedings in a court or tribunal.

When does the Code take effect?

The Code will take effect on a date determined by each state and territory government, and will operate for the same period as the Commonwealth's JobKeeper program.[19] Details as to the commencement date in relation to each state and territory are contained below.

Landlords to waive outgoings and reduce services where appropriate

Where appropriate, landlords should waive recovery of other expenses, such as outgoings, during the period that tenants are unable to trade. In these circumstances, the Code notes that landlords reserve the right to reduce services as required.[20]

As discussed below, landlords who plan to shut down a building or stop providing certain services should check their lease to ensure they are not in breach of any covenants, and seek waivers from tenants where appropriate.

WHAT ABOUT TENANTS WHO AREN'T COVERED BY THE CODE?

Although the Code is only mandatory for businesses eligible for the JobKeeper program with a turnover of up to $50 million as set out above, it does note that the principles of the Code should nevertheless apply in spirit to all leasing arrangements for affected businesses.[21] This reflects the Prime Minister's remarks when announcing the Code that it is designed for "smaller tenants [who will] have the protections they need to be able to sit down with their landlords" and that "larger retailers and the big landlords [will] sort [their own arrangements] out".[22]

2. STATE-BASED RELIEF FOR COMMERCIAL TENANCIES

2.1 IMPLEMENTATION OF THE CODE BY THE STATES AND TERRITORIES

Most states and territories have announced or passed legislation that implements the Code in some way. These measures are summarised below. As at 7 May 2020, Queensland and the Australian Capital Territory have passed legislation granting the relevant Minister power to make regulations implementing the Code, but those powers have not been exercised yet.

(a) Victoria

The Victorian Government has implemented the Code, with retrospective effect from 29 March 2020 to 29 September 2020, in relation to retail and commercial leases where:

- the tenant's annual turnover for the current year is likely less than $50 million; and
- the tenant is an employer who qualifies for the JobKeeper program and is a participant in the scheme. This is stricter than the eligibility criteria under the Code, which only requires that tenants be *eligible* for the program.[23]

In respect of those leases:

- the landlord and tenant must cooperate and act reasonably and in good faith;[24]
- to request rent relief the tenant must make a written request accompanied by a statement that the lease is an 'eligible lease' and evidence that the tenant is an SME entity;[25]
- the landlord has 14 days to make an offer of rent relief (or longer if agreed). At least 50% of the rent relief is to be a rent reduction (unless agreed otherwise).[26] Notably, the Regulations do not expressly reflect the proportionality principle from the Code, where the rent reduction is to be in proportion to the tenant's loss of turnover;
- the landlord cannot increase the rent payable under the lease (unless otherwise agreed in writing);[27]
- the landlord must consider waiving the recovery of any outgoings or expenses payable by the tenant for any period that the tenant is not able to operate their business at the premises;[28]
- the tenant is not in breach of the lease if they reduce the opening hours of the business or cease to operate on the premises;[29] and
- if any outgoings are reduced, the landlord must not require the tenant to pay any amount that is greater than the tenant's proportional share of the reduced outgoings payable under the lease.[30]

(b) New South Wales

On 24 April 2020, the New South Wales Government implemented the Code in relation to leases:

- subject to the *Retail Leases Act 1994* (NSW), or the *Conveyancing Act 1919* (NSW) and relating to the leasing of premises or land for commercial purposes;
- where the tenant qualifies for the JobKeeper program; and
- where the tenant has had a turnover in the 2018-2019 financial year of less than $50 million.

In respect of those leases:

- a landlord must not take prescribed action including, inter alia, eviction, possession or termination of the lease, due to a breach consisting of a failure to pay rent, outgoings or the business not being open during the hours specified in the lease;
- a landlord must not increase the rent payable under the lease; and
- where the tenant is required by the lease to pay a fixed amount that represents land tax, statutory charges or insurance and that amount is reduced, the tenant is exempted from the operation of that provision to the extent of the reduction.[31]

The parties are also subject to an obligation to renegotiate in good faith the rent payable under, and other terms of, the lease having regard to the economic impacts of the COVID-19 pandemic and the leasing principles set out in the Code.[32] The NSW Regulation has effect from 24 April 2020 to 24 October 2020.

(c) Western Australia

The *Commercial Tenancies (COVID-19) Response Act 2020* (WA), which has retrospective effect from 30 March 2020 until 29 September 2020, prohibits landlords of a small commercial lease from taking prohibited action, including evicting the tenant on the grounds of a failure to pay rent or outgoings, increasing the rent payable under a lease and charging interest on rent arrears.

The Western Australian Government has also introduced the *Commercial Tenancies (COVID-19 Response (Early Termination)) Bill 2020* which, if passed as law, would go further to allow a commercial tenant under severe financial distress and who has attempted to negotiate waivers or deferrals of rent but is still not in a position to perform its obligations under the lease, to give a notice of proposed termination to the landlord. If the landlord does not agree to the termination, the matter will be referred to the tribunal for determination.

(d) South Australia

The *COVID-19 Emergency Response Act 2020* (SA), which has retrospective effect from 30 March 2020 until 9 October 2020, prohibits landlords of commercial tenancies where the tenant is eligible for the JobKeeper program from terminating a lease for non-payment of rent or outgoings, or failing to trade during prescribed hours and from increasing the rent payable under a lease.

(e) Tasmania

On 9 April 2020, the Premier issued a notice under the *COVID-19 Disease Emergency (Miscellaneous Provisions) Act 2020* (Tas) immediately halting terminations for unpaid rent or other moneys and suspending rent increases (except for turnover rent) for commercial tenants with a business turnover of less than $50 million where that business is also eligible for the JobKeeper program. That notice is effective until 30 September 2020.

(f) Northern Territory

On 28 April 2020, the NT Government issued a notice under the *Business Tenancies (Fair Dealings) Act 2003* (NT) prohibiting a landlord from giving a tenant a notice to quit unless the landlord has, for a period of 30 days, made good faith efforts to negotiate with the tenant to allow the tenant to remain in the premises. That notice is effective while a COVID-19 public health emergency is declared in the Northern Territory.

2.2RENTAL RELIEF IN GOVERNMENT-OWNED BUILDINGS

Some states and territories have announced rent relief plans designed to assist small businesses who are tenants in Government-owned buildings, by providing them with temporary rental relief during the COVID-19 pandemic period. These include Western Australia, Victoria, Queensland, New South Wales as well as the Adelaide City Council.

2.3 LAND TAX RELIEF

Each state and territory Government has announced land tax support packages for commercial tenants. As at 8 May 2020, the packages announced by the state governments are outlined below:

a. There are two measures in Victoria:

1. Landlords of commercial tenants with an annual turnover of under $50 million and who have experienced a 30% reduction in revenue can apply for a 25% discount on their land tax and any remaining land tax can be deferred until March 2021 if they provide rent relief; and

2. Landowners that have at least one non-residential property and taxable land valued at less than $1 million can defer their 2020 land tax payment until 31 December 2020;

b. In NSW, landlords of commercial tenants with an annual turnover of less than $50 million and who have experienced a 30% reduction in revenue can apply for a land tax concession of up to 25% of their 2020 calendar year land tax liability if the relief passed onto tenants is of the same value. If the relief is of greater value, then a further land tax deferral for any outstanding amounts will be granted for a three month period;

c. In South Australia, businesses and individuals that pay their 2019-20 land tax on a quarterly basis can defer their third and fourth quarter instalments for six months;

d. In Western Australia, interest free repayment plans for land tax have been made available to landowners who demonstrate they are unable to pay their tax;

e. Queensland has announced a 3 month rebate for the financial year 2019-20 followed by a 3 month deferral for the financial year 2020-21 of land tax for certain landowners who agree to provide rent relief for tenants affected by COVID-19. To be eligible, land owners must have at least one tenant whose ability to pay their normal rent is affected by the COVID-19 pandemic or the their ability to secure a tenant must be affected by the COVID-19 pandemic. The landowner must provide rent relief to affected tenants commensurate with the amount of the land tax rebate and comply with new leasing requirements; and

f. Tasmania has announced that land tax will be waived for commercial property for the 2020-21 financial year where the business owner is liable for land tax and can demonstrate that their business operations have been affected by CVOID-19.

In addition to the above land tax relief, in the ACT landlords are entitled to have their commercial rates waived, depending on how affected their tenants are by the COVID-19 pandemic. Any waiver that is granted must be passed onto the tenant in a proportional cost-sharing arrangement. The Northern Territory has also announced that landlords will be eligible to receive payroll tax and utilities bill relief if they negotiate rent relief with their tenants in line with the Code.

2.4 INCREASED FIRB SCRUTINY

Finally, FIRB is set to run the ruler over every proposed foreign acquisition in Australia, with the Treasurer announcing a temporary reduction in the screening threshold for foreign investments to $0.

Under these changes, ‘foreign persons’ under the relevant Act have a higher likelihood of needing to seek approval from FIRB when acquiring a leasehold interest. Previously an acquisition of a leasehold interest in (non-low threshold) developed commercial land was subject to a monetary threshold of $275 million. Now the monetary threshold has been reduced to $0. The temporary change does not affect the meaning of significant or notifiable actions other than the monetary thresholds under those definitions. It also does not change the meaning of a ‘foreign person’ and will remain subject to any other relevant criteria or exemptions that may apply under the FIRB legislation.

The FIRB’s Guidance Note released on 24 April 2020 contains the following guidance:

- foreign persons entering into a lease agreement where the lease tenure is in excess of 5 years (including any right or option to renew the term of the lease) is subject to the $0 monetary screening threshold;
- amendments to a lease (e.g. a change to the term of a lease where the extension plus the remainder of the term exceeds 5 years) may be considered a material variation, giving rise to a new significant or notifiable action occurring;
- amendments to a lease (e.g. a change to the term amounting to the surrender of the initial lease and the grant of a new lease) may result in a new lease requiring FIRB approval if the new lease is reasonably likely to exceed 5 years;
- as entering into an AFL and entering into a lease are generally considered to be two separate actions, foreign persons with an existing no-objection notification in relation to an AFL may need to apply for a separate notification for the lease (where the tenure is in excess of 5 years); and
- all foreign persons proposing to acquire interests in residential land used for residential care, retirement villages and certain student accommodation must notify the Government to get prior approval, unless the proposal falls within certain exemptions.

This temporary measure will remain in place for the duration of the COVID-19 crisis.

FIRB’s timeframe for reviewing applications has also been extended from 30 days to up to 6 months to enable it to review the significant increase in FIRB applications which it anticipates. Priority will be given to processing applications for investments that protect and support Australian businesses and jobs.

3. RISKS FOR LANDLORDS

There are four main types of claims landlords are likely to face by tenants unable to trade or access their tenancy due to COVID-19:

1. rental or other relief on the grounds of frustration;
2. abatement and/or suspension of rent under *Force Majeure* provisions;
3. abatement of rent under a ‘damage and destruction’ clause; and
4. abatement of rent for breach of tenant’s right to quiet enjoyment or other rights associated with access to the building or the provision of services.

Can tenants seek relief on the grounds of frustration?

Under present law, no.

Whilst there has been recent criticism of the current situation, the present state of the law is that the doctrine of frustration does not currently apply to leases in Australia. This is in accord with a 1926 decision of two justices of the High Court (the decision is not unanimous) - *Firth v Halloran* (1926) 38 CLR 261.

Courts of Appeal at state level have suggested that the 1926 decision should be overturned, and it may well be that the High Court will do so if it has an opportunity to consider this issue again. Until then, the State Courts are bound by the current High Court decision.

Assuming the High Court will overturn the 1926 decision and apply the doctrine to leases, the doctrine will apply where, without fault of either party, an unforeseen event(s) renders performance of the lease radically different from that intended by the parties.

To terminate on the grounds of frustration, a tenant must demonstrate that COVID-19 and/or the Government’s response has either:

- rendered performance of the lease impossible; or
- rendered performance of the lease radically different to what was envisaged by the parties.

Australian courts have applied this test strictly, generally declining to find frustration where an event is only temporary or transient. Similarly, in a case involving the SARS epidemic of 2003, a Hong Kong court found a lease was **not** frustrated where a tenant was unable to access their premises for 10 days because this period only formed a relatively minor proportion of the overall 2 year lease term.

This suggests that for the typical long term commercial lease or five-year retail lease, even a Government-mandated shutdown of several months would be unlikely to meet this threshold. Tenants would also face the practical problem of demonstrating prospectively how the parties' obligations have "radically changed" while the extent of the Government's COVID-19-related restrictions continue to change and their duration remains unknown.

The longer the period of lock down, the stronger the argument that a lease has been frustrated - noting once again that the point may have to be taken to the High court to prevail, and even then only if the High Court overturns its 1926 decision. The current weight of judicial and academic commentary suggests that there is a good chance that the High Court would take the opportunity to restate the law and to apply the doctrine to leases.

Frustration is also unlikely to be the most suitable remedy for many tenants during the COVID-19 pandemic. This is because a frustrated lease will terminate immediately, with entitlement to damages limited and only available in certain states.[33] Accordingly, tenants suffering financial stress as a result of COVID-19 who hope to return to normal trading once restrictions are lifted are more likely to seek an abatement of rent or similar relief.

Is COVID-19 a *Force Majeure* event?

Probably not – but check the lease.

There is no common law doctrine of *Force Majeure* under the general law in Australia, meaning any relief available to tenants must derive from the terms of the lease. Parties should carefully review the *Force Majeure* provisions in their lease to determine if they apply to a pandemic or any restrictions on trade imposed by Government in response. In our experience, it is uncommon (but not unprecedented) for leases to define a *Force Majeure* to include a pandemic or outbreak of deadly disease. The effect of having a *Force Majeure* provision in a lease could excuse one or both parties from non-performance or delay their contractual obligations – this will depend on the wording and context of the specific clause in the lease.

Could tenants seek an abatement for 'damage and destruction' in the context of COVID-19?

In our view, no.

It is common under commercial leases for a tenant to be entitled to an abatement of rent and outgoings in the event that their premises is damaged or destroyed. Relief under these clauses generally requires physical damage to the premises as opposed to a shutdown prompted by a pandemic.

In saying that, it may be arguable that tenants are entitled to an abatement of rent on the grounds of 'damage' where the premises has to be closed for deep cleaning due to a COVID-19 contamination. The merits of such a claim will depend on the specific terms of the lease – and, potentially, whether such contamination was caused by the tenant or the landlord. That said, landlords may argue that these costs are recoverable from the tenant as a service charge. This will depend on whether deep cleaning in a COVID-19 scenario is captured by the services clauses in the lease. Keep an eye out for any 'catch-all' provisions that allow the landlord to recover costs reasonably incurred in the management and upkeep of the building.

Is a COVID-19 shutdown a breach of a tenant's right to quiet enjoyment?

Unlikely – but check the lease.

A landlord will not breach the tenant's right to quiet enjoyment by performing an action that is authorised by the lease. This means the key issue is whether the landlord is empowered by the lease to shut down the premises or building due to COVID-19. Such powers are likely to be contained in two types of provisions:

a. the landlord's obligation to comply with laws and the requirements of government authorities; and

b. the landlord's power to close the building in the event of an emergency.

Whether a shutdown is authorised by the lease may depend on the circumstances. For example, while a shutdown initiated by a landlord due to a building contamination may not be authorised under the landlord's obligation to comply with laws, it may still be covered by the landlord's power to close the building in an emergency.

A risk with a shutdown unilaterally taken by the landlord is that the tenant may assert the shutdown is wholly unnecessary and overly disruptive. Landlords may wish to consult with tenants or give prior notice (if time allows) if that is a risk, before embarking on the relevant steps.

If the shutdown is mandated by the Government, even if the lease does not require the landlord to comply with laws it would be difficult to see how a tenant could argue that a building closure to comply with a Government-mandated shutdown was a breach of the lease by the landlord.

Would a building shutdown breach the landlord's obligation to provide building services?

Again, check the lease.

As with the tenant's right to quiet enjoyment, whether a building shutdown breaches a landlord's obligation to provide services, such as air-conditioning, or access to the building, will depend on whether it was mandated by the Government or a voluntary action by the landlord (and in the case of the latter, whether a relevant exemption applies).

In relation to the provision of services, the wording of the clause in question will be paramount. For example, a tenant's claim will be weaker under a general clause which requires the landlord to provide air-conditioning in working condition, as opposed to a specific rent abatement regime allowing a rent abatement if the air-conditioning fails to meet the minimum performance standard.

In our experience, a tenant's right to the provision of building services, including a specific rent abatement regime for failure of specified services, is commonly subject to disruptions for routine repair and maintenance and other exclusion events. In a voluntary building shutdown by the landlord, a review of these exclusion events will be necessary unless the landlord can rely on a contractual right to close the building in the event of an emergency.

As above, if the building shutdown is mandated by the Government, it would be difficult to see how a tenant could argue that the landlord's inability to provide building services during the shutdown period was a breach of the lease by the landlord.

4. RISKS FOR TENANTS

Continuous trading clauses

Aside from the commercial fallout of COVID-19, tenants are not immune from the risk of liability as a result of a shutdown of their tenancy. Retail shop leases, for example, commonly include covenants requiring the tenant to be open for certain hours of trade, which may become impossible if the premises is forced to close due to a mandatory shutdown.[34] This issue is dealt with for qualifying tenants under the Code, which prohibits landlords from levying any penalties if tenants reduce opening hours or cease to trade due to the COVID-19 pandemic.[35]

As with the landlord's inability to perform its obligations under the lease as a result of a Government-mandated shutdown, it would be difficult to see how a landlord could argue that a tenant was in breach if the tenant was unable to perform its obligations as a result of the shutdown – this would only provide the tenant from relief against those obligations which require physical use of the premises, such as the obligation to continue trading. It would not, in the absence of Government intervening measures, provide a tenant with relief from its obligation to pay rent – see above as to the operation of the Code.

If the shutdown of the premises is not Government-mandated but is voluntarily taken by the tenant, the tenant would need to be wary of being in potential breach of its lease, unless the tenant can claim protection from the Government intervening measures and the Code. As with the obligations of landlords, this covenant may be subject to an exemption provided for in the lease.

5. PRACTICAL TIPS

Drawing on bank or personal guarantees to cover rent?

One possible way of alleviating the financial strain of COVID-19 is for tenants to allow their landlord to call on their bank guarantee or cash deposits to cover rental payments for an agreed period of time (bank guarantees and cash deposits are commonly for a period of 6 months' gross rent). However, parties should be aware that landlords are prohibited from calling on qualifying tenants' bank guarantees, personal guarantees and cash deposits during the COVID-19 pandemic under the Code.[36]

Therefore, before entering into these arrangements, parties should carefully consider whether the Code applies to them. These issues are discussed in detail above. Furthermore, tenants should also review their financing arrangements to ensure that a call on their bank guarantee is not deemed a default event.

Pragmatism is key

Given the unprecedented circumstances landlords and tenants are confronting, it may be in the interests of both parties to review their obligations under their lease and where necessary, provide waivers where performance is no longer practical. It would appear that there is room for an approach being taken by both landlords and tenants for mutual benefit.

Landlords should also bear in mind that under recent changes to the *Corporations Act 2001* (Cth):

- the amount that a liquidated debt must reach before a creditor can issue a statutory demand has temporarily increased from $2,000 to $20,000; and

- a debtor will temporarily have 6 months to respond from the date the demand is served before the presumption of insolvency takes effect.

These changes are aimed at “freezing” the ability of creditors to issue statutory demands on debtors during the COVID-19 crisis which, if not paid, would trigger liquidation and insolvency proceedings. Importantly, however, they do not suspend the contractual obligations of landlords and tenants under existing leases.

ENDNOTES

1. SME Commercial Leasing Principles During COVID-19, page 1.
2. SME Commercial Leasing Principles During COVID-19, page 1.
3. SME Commercial Leasing Principles During COVID-19, Overarching Principles and Definitions.
4. SME Commercial Leasing Principles During COVID-19, Leasing Principle 4.
5. SME Commercial Leasing Principles During COVID-19, Leasing Principle 5.
6. SME Commercial Leasing Principles During COVID-19, Leasing Principle 9.
7. SME Commercial Leasing Principles During COVID-19, Leasing Principle 12.
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9. SME Commercial Leasing Principles During COVID-19, Leasing Principle 10.
10. SME Commercial Leasing Principles During COVID-19, Leasing Principle 1.
11. SME Commercial Leasing Principles During COVID-19, Leasing Principle 13.
12. SME Commercial Leasing Principles During COVID-19, Leasing Principle 14.
13. SME Commercial Leasing Principles During COVID-19, Leasing Principle 11.
14. SME Commercial Leasing Principles During COVID-19, Leasing Principle 2.
15. Prime Minister’s press conference, 27 March 2020.
16. SME Commercial Leasing Principles During COVID-19, Leasing Principle 7.
17. SME Commercial Leasing Principles During COVID-19, Leasing Principle 6.

18. SME Commercial Leasing Principles During COVID-19, Binding Mediation.

19. SME Commercial Leasing Principles During COVID-19, page 1.

20. SME Commercial Leasing Principles During COVID-19, Leasing Principle 8.

21. SME Commercial Leasing Principles During COVID-19, page 1.

22. Prime Minister's press conference, 3 April 2020.

23. COVID-19 Omnibus (Emergency Measures) Act 2020 (Vic), s 13.

24. COVID-19 Omnibus (Emergency Measures) (Commercial Leases and Licences) Regulations 2020 (Vic), cl 8.

25. COVID-19 Omnibus (Emergency Measures) (Commercial Leases and Licences) Regulations 2020 (Vic), cll 9, 10 and 11.

26. COVID-19 Omnibus (Emergency Measures) (Commercial Leases and Licences) Regulations 2020 (Vic), cl 10.

27. COVID-19 Omnibus (Emergency Measures) (Commercial Leases and Licences) Regulations 2020 (Vic), cl 12.

28. COVID-19 Omnibus (Emergency Measures) (Commercial Leases and Licences) Regulations 2020 (Vic), cl 14.

29. COVID-19 Omnibus (Emergency Measures) (Commercial Leases and Licences) Regulations 2020 (Vic), cl 18.

30. COVID-19 Omnibus (Emergency Measures) (Commercial Leases and Licences) Regulations 2020 (Vic), cl 15.

31. Retail and Other Commercial Leases (COVID-19) Regulation 2020, cl 6; Conveyancing (General) Regulation 2018, Sch 5, cl 4.

32. Retail and Other Commercial Leases (COVID-19) Regulation 2020, cl 7; Conveyancing (General) Regulation 2018, Sch 5, cl 5.

33. Damages for frustrated contracts are prescribed by statute in New South Wales, South Australia and Victoria (see the New South Wales (Frustrated Contracts Act 1978), South Australia (Frustrated Contracts Act 1988), and Victoria (Australian Consumer Law and Fair Trading Act 2012). Damages in the event of frustration are not available in the remaining States and Territories.

34. Please note that in Western Australia, provisions in a retail shop which requires a tenant to open the retail shop the subject of the lease at specified hours or specified times is void under the *Commercial Tenancy (Retail Shops) Agreements Act* 1985.

35. SME Commercial Leasing Principles During COVID-19, Leasing Principle 14.

36. SME Commercial Leasing Principles During COVID-19, Leasing Principle 11.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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