

RENT NEGOTIATIONS FOR TENANTS

Preparing to renegotiate rentals
under the Commercial Leases
Code

The Commercial Leases Code was announced by the Federal Government in late April to assist landlords and tenants deal with the challenges provided by the various impacts of COVID-19. While the Code was issued at Federal level, it is being implemented in each State via State based legislation.

This document will help you prepare for negotiations with your tenants to agree rent reductions and adjustments as a result of the impact of COVID-19. It is based on the Federal code rather than the specific legislation in each State.

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What is the Commercial Leases Code

On 24 April 2020, the Federal Government introduced a mandatory code of conduct outlines a set of good faith leasing principles for commercial tenancies. This covers retail, offices and industrial premises and operates between owners, operators, other landlords and tenants.

The code applies where the tenant is a small to medium sized business with an annual turnover of up to \$50 million and where the tenant is eligible for the JobKeeper Payment.

Under the code, there are 14 principles. The **four key principles** are:

- landlords must not terminate leases for non-payment of rent during the COVID-19 pandemic (or reasonable recovery period)
- tenants must stay committed to their lease terms (subject to amendments)
- landlords must offer reductions in rent (as waivers or deferrals) based on the tenant's reduction in trade during COVID-19
- benefits that owners get for their properties (e.g. reduced charges, land tax, deferred loan payments) should be passed on to the tenant (in the appropriate proportion)

The Code provides that in the first instance, landlords and tenants should seek to reach mutually agreeable outcomes. Where this is not possible, parties must attend a binding mediation. In most states this mediation service will be available through the Small Business Commissioner. Parties also have the option of choosing a private mediator.



Preparing for your Negotiation

Importantly, the Code provides that landlords and tenants will act in an open, honest and transparent manner, and will each provide sufficient and accurate information within the context of negotiations to achieve outcomes consistent with the Code. For many tenants, relationships with the landlord in the past may not have facilitated this open, honest communication and negotiations may prove challenging.

There are several areas which tenants can take time to prepare, which will facilitate this more open negotiation and several tips which can be implemented to deliver the best result.

Tip 1: Think about what's important

As you prepare for the negotiation, it will be easy to focus on short-term cash flow issues. These are important, no doubt. You also need to consider longer-term interests and issues so that you have more room to build creative solutions into the negotiations.

Some things you may want to consider are as follows.

- What are the longer term prospects for your business? Is continuation of the business in its current location essential, nice to have or not necessary?
- What would be the costs involved or the impact on revenue of having to find new premises if you are evicted at the end of the moratorium period or if your lease is not renewed.
- How important is this particular location to my business. Does it rely on neighbouring businesses to generate foot traffic for example.



- How long do I expect of COVID-19 to impact on my business to last? How quickly do I expect my business to recover?

Having thought about your own perspective, it is important to think about the perspective of the landlord. You will need to consider certain factors, but you will then need to check these through discussion with the landlord.

Examples of questions you should consider are:

- Is the landlord keen to maintain the lease over the longer term?
- Is my landlord an individual investor, small business, corporate etc.? Who are the other stakeholders impacted by non-payment of rental?
- What is the landlord's financial position and how has it been impacted by COVID-19?
- Does the landlord have mortgage repayments on the property?



Tip 2: Plan possible agreements

Once you have an idea of what both parties are trying to achieve in the negotiation and what their key concerns and objectives are, it is the right time to start brainstorming the kind of agreements that could be reached.

While you will obviously have an ideal outcome that you are looking for, it is also helpful to think more broadly than this and also to get a little bit creative. Think not only of the scenarios that work for you but think about scenarios that may be put forward by the landlord. It is important to have thought of these in advance so that when they are raised in the negotiation, you know how to respond to them appropriately.

While rent reductions, either in the forms of waiver or deferral, are obvious options (and are in fact mandated by the Code), there may be other options possible to help out in the negotiation.

Examples of other things that could be agreed are:

- Timing and terms of the rent deferral
- Lease extensions or additional options
- Rent reductions that are lower than the revenue reduction but are available for a guaranteed period
- Reduction in outgoings
- Contribution to fitout or improvements
- Waiver of make-good costs at the end of the lease
- Consent to sub-lease

Tip 3: Get your data

The most effective way to deliver an outcome that works for you is to be as transparent as possible regarding your situation.

While the Code requires the tenant's financial position to be considered, it does not specifically refer to the landlord's financial position being an issue.

While your initial instinct may be to withhold financial information from the tenant on the grounds that it is confidential, you will have much more success at your negotiation if you are willing to provide solid evidence to the tenant of your own difficulties as a result of the situation.

Human nature is such that the mere act of providing some justification for what you are asking for increases the likelihood of getting what you want – or something close to it at least.

Evidence that you might need to bring to the negotiations includes:

- Documentation of your turnover for the current period and the comparative period. If you are only seeking a 30% reduction, the confirmation of your eligibility may be sufficient. If you are seeking a larger reduction, you will probably need to provide more detailed sales figures.
- Evidence of reduction in trading capacity or hours. Were these due to government regulations compared or more "voluntary" closures based on your own or your staff's requirements?
- If you are also claiming increased costs due to COVID-19 you should provide the landlord with evidence to of how costs have increased for your business. This may include things like additional cleaning costs. While the Code does not specifically require increased costs to be considered by landlords there is no reason you can't bring it to the table.

- Any modelling or industry information that supports how long the recovery period may be for your business.

You will also be able to ask the landlord for information to help you understand their situation. In particular, if the landlord claims that they have financially been impacted by COVID-19 you may justifiably ask them to provide evidence of the financial impact.

Useful information may include:

- Their personal situation – eg. The landlord may be a self-funded retiree who relies on the rent for their income.
- Additional interest costs relating to the deferral of loan payments
- Costs attributed to having withdrawn superannuation balances early to finance mortgage repayments during this situation.
- Information about other stakeholders



Tip 4: Be aware what happens if no agreement is reached

It is absolutely critical that you consider what will happen if you are not able to reach an amicable outcome with the landlord. In most cases this will mean mandatory mediation. Mediation can be a helpful process, but it is possible that there may be fairly long delays in getting to mediation. A successful mediation will provide you with a binding agreement.

If an outcome is not successfully achieved at mediation, then it is likely that the landlord will take legal action against you to recover outstanding rent. You would need to consider:

- What impact would a judgement against you have on your financial status?
- What additional costs would be incurred? These will include your legal costs in defending the proceedings but possibly also statutory interest costs and the legal costs of the landlord?
- Are you at risk of eviction at the end of the moratorium period? How would this impact you? Are you likely to find cheaper premises? Would alternative premises suit you as well as the current ones? What costs would you incur in moving?

You should also consider what happens from the **landlord's perspective** if no agreement is reached. For example:

- What would be the cost of proceedings against you compared to the likely hold of getting a cash return from those proceedings?
- If the landlord evicts you at the end of the moratorium period, what will that mean for them? Will they easily be able to relet the premises? What kind of rental may be achieved in that situation?



Where can I get help?

For many tenants, this will be one of the most challenging financial negotiations they have ever had to undertake. In situations where parties are under financial and emotional stress, managing a negotiation effectively can be very challenging and you may benefit from third party assistance. There are several places you can go for assistance:

- The Small Business Commissioner in your state will have a help line where you can talk to someone for some guidance
- A leasing specialist will have a good understanding of the market and plenty of experience of dealing with tenants
- A negotiation specialist can assist you in preparing for your discussions or can act as an independent facilitator to assist the conversation. They will add particular value in managing the emotional aspects of the negotiation and helping both parties step back to focus on realistic goals.

Resources

Australian Small Business and Family Enterprise Ombudsman

<https://www.asbfeo.gov.au/>

Victorian Small Business Commissioner

<https://www.vsbvc.vic.gov.au/>

NSW Small Business Commissioner

<https://www.smallbusiness.nsw.gov.au/>

Queensland Small Business Champion

<https://desbt.qld.gov.au>

South Australian Small Business Commissioner

<https://business.sa.gov.au>

Western Australian Small Business Commissioner

<https://www.smallbusiness.wa.gov.au/>

Tasmanian Small Business Council

<https://www.tsbc.org.au/>



What to do next

Overall, there are many things that you can prepare before your discussions with the tenant that will help you navigate this difficult situation. At the very heart of this process, however, needs to be an understanding that neither landlords nor tenants are to blame for the current situation, and neither party will be held 100% accountable for the financial impacts.

In order to work towards a viable outcome, both parties will need to be prepared to accept an outcome that is less than ideal - but is better than a worst case scenario.

For guidance on how to navigate these and for information regarding your specific circumstances, please **contact Nicole Davidson** for a **confidential and complimentary initial discussion**.



The contents do not constitute legal advice, are not intended to be a substitute for legal advice and should not be relied upon as such. You should seek legal advice or other professional advice in relation to any particular matters you or your organisation may have.

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