

COVID-19: (AUSTRALIA) SOUTH AUSTRALIAN ACT AND REGULATIONS FOR COMMERCIAL LEASES

Date: 11 May 2020

Australia Real Estate Alert

By: Samuel Brown, Will Grinter, Karen Yuan, Elyse O'Hara

**This information is accurate as of 3:00 P.M. on Friday 8 May and is subject to change as this situation evolves.*

On 7 April 2020, the National Cabinet issued a Mandatory Code of Conduct (the Code), which imposes a set of good faith leasing principles that apply to certain commercial tenancies experiencing financial stress or hardship because of the COVID-19 pandemic. You can read more about the Code and the emergency powers provisions in other states in our previous alert which can be found [here](#).

Following the release of the Code, the South Australian Government has now introduced:

- the COVID-19 Emergency Response Act 2020 (the Act), and
- the COVID-19 Emergency Response (Commercial Leases) Regulations 2020 (the Regulations).

The Act, which was introduced on 9 April 2020, modifies the provisions of commercial leases to prohibit and regulate the exercise of certain landlord rights to enforce terms under these commercial leases.

The Regulations, which were introduced on 16 April 2020, detail the circumstances in which a tenant will be taken to be suffering financial hardship as a result of the COVID-19 pandemic.

In this article, we will discuss:

- When does the Act apply?
- Who is covered under the Act?
- What are the key provisions of the Act?
- Has the Act clarified the uncertainties from the Code?

WHEN DOES THE ACT AND THE REGULATIONS APPLY?

Section 7 of the Act, which contains the provisions relating to commercial leases, applies retrospectively from the period commencing on 30 March 2020 to the day fixed by the Minister, which must be the earlier of:

- the day on which all relevant declarations in relation to COVID-19 within South Australia have ceased, or
- six months after the commencement of the Act, (the Prescribed Period).

WHO IS COVERED UNDER THE ACT AND THE REGULATIONS?

Included commercial leases

The relevant provisions of the Act and Regulations regarding commercial leases apply to:

- a retail shop lease within the meaning of the *Retail and Commercial Leases Act 1995*,
- a lease under the *Landlord and Tenant Act 1936*, including a retail shop lease to which Part 4 of that Act applies, or
- any other agreement under which a person grants or agrees to grant another person for value a right to occupy premises for carrying on a business (whether or not the right is of exclusive occupation and whether or not the agreement is expressed or implied, oral or in writing.).

Unlike other States' legislation and the expressed purpose of the Code, the Act does not limit its application to commercial leases entered into prior to a specific date. The Act will apply to new commercial leases negotiated or entered into before and after the commencement of the Act.

The majority of the provisions of the Act apply to commercial leases where the tenant is suffering financial hardship as a result of the COVID-19 pandemic, as identified in detail below.

Pursuant to the Regulations, a tenant is taken to be suffering financial hardship as a result of the COVID-19 pandemic if the tenant is eligible for, or receiving, a JobKeeper payment in respect of the business of the tenant (whether in their capacity as an employer or on their own behalf). This is a further departure from other States' legislation and the Code, in that there is no additional turnover test applied for a tenant to benefit from the relieving provisions.

You can read more about eligibility for the JobKeeper payment in the K&L Gates tax team's Employer Guide to the JobKeeper Scheme which can be found [here](#).

Excluded Leases

The Act does not apply to:

- a lease under the *Pastoral Land Management and Conservation Act 1989*, or
- a lease under the *Crown Land Management Act 2009*.

WHAT ARE THE KEY PROVISIONS OF THE ACT AND THE REGULATIONS?

Prescribed Actions

If a tenant is suffering financial hardship as a result of the COVID-19 pandemic, a landlord cannot take any prescribed action against the tenant for a breach of the lease during the Prescribed Period due to any of the following:

- a failure to pay rent
- a failure to pay outgoings
- the business operating under the lease not being open during the hours specified in the lease, or
- another act or omission of a kind prescribed by regulations.

A "prescribed action" includes taking action under a commercial lease or seeking orders or issuing proceedings in a court for:

- eviction from the premises
- the exercise of a right of re-entry to the premises
- recovery of land
- distraint of goods (seizure of property in order to obtain payment of rent or other money)
- forfeiture
- damages
- a payment of interest on unpaid rent otherwise payable by the tenant
- recovery of a security bond (whole or part)
- performance of obligations by the tenant or any other person pursuant to a guarantee
- possession
- termination, or
- any other remedy available to the landlord against the tenant at common law or under the law of South Australia.

Additional Restrictions

In addition to the prohibition on prescribed actions, if a tenant is suffering financial hardship as a result of the COVID-19 pandemic, a landlord must not:

- unless otherwise agreed between the landlord and tenant, increase the rent payable under a commercial lease (other than rent or a component of rent determined by reference to turnover), or
- require a tenant to pay land tax or reimburse the landlord for the payment of land tax in respect of a commercial lease.

Future Law Protections

The Act provides that an act or omission of tenant, pursuant to a requirement under the laws of South Australia in response to the COVID-19 pandemic, will not:

- be taken to be a breach of the commercial lease, and
- constitute grounds for termination or the taking of any prescribed action by the landlord against the tenant.

This additional protection of tenants could have broad implications depending on what future laws relating to the COVID-19 pandemic are brought into place by the state of South Australia. Practically speaking, it is most likely to apply in any circumstances where premises are ordered to close and, as a result, tenants cannot trade or meet other obligations under their relevant commercial leases where physical access to premises is required.

Actions Taken Prior to 9 April 2020

The Act contains a provision that applies in circumstances where a landlord has sought to enforce its rights under a commercial lease during the period between 30 March 2020 and 9 April 2020 (Relevant Period), being the period of time between the commencement of the section and the day on which the Act was assented to.

If a tenant is suffering financial hardship as a result of the COVID-19 pandemic and during the Relevant Period:

- a landlord has taken or commenced, but not yet completed or finalised, a prescribed action
- a landlord has taken or commenced, but not yet completed or finalised, the performance of any other measure that the landlord would not have been permitted to undertake or commence during the Prescribed Period, or
- the operation of the terms of a commercial lease has had effect, or has a periodic or ongoing effect, contrary to the operation of section 7 of the Act,
- the action, operation or effect will, insofar as it remains incomplete or ongoing, or has a periodic or ongoing effect, be stayed or suspended until the end of the Prescribed Period.

HAS THE ACT CLARIFIED THE UNCERTAINTIES OF THE CODE?

As mentioned in our previous alert, which can be found [here](#), the Code contained several uncertainties regarding its application and implementation.

The Act does not make any mention of the Code and does not appear to have either implemented or clarified the provisions of the Code. As a result, many of the uncertainties of the Code remain unclarified. In this section we revisit the uncertainties of the Code and seek to set out some of the uncertainties of the Act.

What if a tenant has not suffered financial hardship as a result of the COVID-19 pandemic?

The provision that allows either party to apply to the Commissioner in respect of dispute resolution has been broadly drafted to apply to all commercial leases regardless of whether the tenant has suffered financial hardship as a result of the COVID-19 pandemic.

Any party to a commercial lease may apply to the Small Business Commissioner for either one or both of the following:

- mediation of a dispute in relation to whether or not a tenant is suffering financial hardship as a result of the COVID-19 pandemic; and
- a determination as to whether or not a tenant is suffering financial hardship as a result of the COVID-19 pandemic.

Any party to a commercial lease may also apply to the Small Business Commissioner for mediation of any other dispute in relation to issues that have arisen in relation to the COVID-19 pandemic. The issue may arise from, or relate to, the operation of the Act, a commercial lease or any other matter relating to the occupation of the premises or a business conducted at the premises.

The future law protections discussed above also broadly apply to all commercial leases regardless of whether the tenant has suffered financial hardship as a result of the COVID-19 pandemic.

Do the Act and Regulations apply to new leases entered into during the COVID-19 pandemic?

Yes, as outlined above, the Act and Regulations apply to existing commercial leases as well as new commercial leases negotiated or entered into after the commencement of the Act.

What evidence does a tenant have to provide to support financial hardship and how do they demonstrate it is a direct result of the COVID-19 pandemic?

The Regulations provide some clarity regarding the scope of information required.

In making a determination as to whether or not a tenant is suffering financial hardship as a result of the COVID-19 pandemic, the Small Business Commissioner must have regard to:

- whether or not the tenant is eligible for, or is receiving, a JobKeeper payment in respect of the business of the tenant (whether in their capacity as an employer or on their own behalf)
- any reduction in turnover of the business of the tenant (as verified by financial records or statements provided by the tenant) during a specified period as compared with another specified period determined by the Commissioner as being relevant to the circumstances of whether or not the tenant is suffering financial hardship as a result of COVID-19.

This ultimately allows the Small Business Commissioner to determine the scope of the financial records or statements to be provided by the tenant and what "specified periods" are appropriate for conducting a comparison of the business' turnover.

How is turnover determined?

Turnover is not defined in the Act. While the Act does not impose a turnover threshold, the Act still relies on the concept of turnover for other purposes. For example:

- rent payable under a commercial lease must not be increased during the Prescribed Period (other than rent or a component of rent determined by reference to *turnover*); and
- any reduction in *turnover* of the business of the tenant is considered in determining whether or not a tenant is suffering financial hardship as a result of the COVID-19 pandemic.

Given the absence of a definition of turnover, we expect that parties seeking to apply the Act will have regard to the determination of turnover under the Code.

Under the Code, turnover is defined by reference to assessments undertaken for eligibility for the Commonwealth's JobKeeper programme. It appears that turnover must therefore be determined by reference to the activities of the tenant and not the relevant premises. This will mean that where a tenant experiences a significant "bricks and mortar" trading impact, but potentially stable or even increased online turnover, the online turnover must be allowed for in the determination of turnover.

How does turnover apply to tenants that are part of corporate group or a franchise structure?

The Act does not clarify how the concept of turnover will be applied to tenants that are part of a corporate group or a franchise structure.

Under the Code, turnover is applied in respect of franchises at the franchisee level, and in respect of retail corporate groups at the group level (rather than the individual retail outlet level).

This gives rise to considerable uncertainty and it is likely that this will give rise to disputes. It is not clear how turnover will be determined in circumstances where:

- a tenant under the lease is a franchisor but the business at the premises is that of the franchisee and their eligibility for the JobKeeper Scheme differs, or
- the group business of a tenant is undertaken through various entities.

Are tenants entitled to a reduction in rent due to COVID-19? For how long?

The Act does not require landlords to provide any reduction in rent.

While the Code requires landlords to offer a rent reduction that is proportionate to the amount of the reduction in the tenant's turnover during the COVID-19 crisis period and subsequent recovery phase, the Act does not prescribe this. Accordingly, any reduction in rent will be subject to negotiation between the parties.

However, if a tenant is suffering financial hardship as a result of the COVID-19 pandemic, the Act prevents a landlord from taking any prescribed action against a tenant on grounds of a breach of the lease during the Prescribed Period consisting of a failure to pay rent.

What happens to rent reviews during the Prescribed Period?

If, during the Prescribed Period, a tenant is suffering financial hardship as a result of the COVID-19 pandemic, the Act provides that rent payable must not be increased other than by reference to turnover (unless otherwise agreed between the landlord and the tenant).

The wording of this provision is unclear as to whether rent reviews can be applied for the balance of the lease year, once the Prescribed Period has elapsed.

The lack of clarity arises because the provision does not expressly state that rent reviews must not occur during the Prescribed Period. The provision states that rent must not be increased if during the Prescribed Period the tenant is suffering financial hardship as a result of the COVID-19 pandemic. The restriction on rent reviews is not a broad ban on rent reviews during the Prescribed Period, it only applies where the tenant is also suffering financial hardship.

However, once the Prescribed Period elapses, the Act will no longer apply. On this basis, there is a strong argument that rent reviews can take place after the expiry of the Prescribed Period.

What about outgoings?

The Act only prevents a landlord from requiring a tenant who is suffering financial hardship as a result of the COVID-19 pandemic to pay land tax or reimburse the landlord for the payment of land tax during the Prescribed Period.

While the Code requires landlords to pass on any reductions in statutory charges, as well as the benefit of any deferral of loan repayments on a proportionate basis, the Act does not prescribe this. Accordingly, the passing on

of any reduction in statutory charges and any deferral of loan payments will be subject to negotiation between the parties.

Similarly, while the Code requires landlords to waive the recovery of outgoings or other expenses under a lease during the period that the tenant is unable to trade from the premises, the Act does not impose such an obligation. A waiver of outgoings or other charges during a period where the tenant is unable to trade will be subject to negotiation between the parties.

What about landlords who are facing financial hardship due to COVID-19?

The Act does not contemplate circumstances where the landlord is facing financial hardship due to the COVID-19 pandemic. However, as the Act does not strictly require a landlord to offer a rent reduction, the landlord's financial ability to offer a rent reduction may be considered during any voluntary negotiations between the parties.

What about shopping centres? Do landlords need to offer the same deal for all tenants within the same shopping centre or building?

No, the economic impacts of the COVID-19 pandemic will be different for each tenant of shopping centres.

While landlords are not strictly required to provide rent relief under the Act, where a landlord agrees to negotiate rent relief, the temporary arrangement may be based on the circumstances of the particular tenant. In accordance with the Code, rent relief may be a "tailored, bespoke and appropriate temporary arrangement" for each tenant on a case-by-case basis.

If only a few tenants are left trading in a shopping centre or building, can the landlord close the building or shopping centre to reduce costs without incurring compensation claims from the remaining tenants?

The Act has not clarified this issue. Unless the Government issues a direction requiring closure, then it is likely that the landlord may be exposed to claims in the event of closure.

Is there a right for tenants to terminate the lease agreement due to COVID-19?

In the absence of a right of termination under a lease, no. However, the parties may separately negotiate and agree to a surrender of the lease.

Can a landlord call on security during COVID-19?

If a tenant is suffering financial hardship as a result of the COVID-19 pandemic, a landlord cannot take action for recovery of a security bond or performance of obligations pursuant to a guarantee, on grounds of a breach of the lease during the Prescribed Period due to:

- a failure to pay rent; or
- a failure to pay outgoings; or
- the business operating under the lease not being open for business during the hours specified in the lease.

However, the Act does not prevent the landlord from calling on security for other reasons, where permitted under the lease.

Can a landlord terminate a lease during COVID-19?

If a tenant is suffering financial hardship as a result of the COVID-19 pandemic, a landlord cannot take action to terminate the lease, on grounds of a breach of the lease during the Prescribed Period that consists of:

- a failure to pay rent; or
- a failure to pay outgoings; or
- the business operating under the lease not being open for business during the hours specified in the lease.

The Act does not prevent the termination of a lease in circumstances where a tenant has breached the lease and the breach consists of matters unrelated to the COVID-19 pandemic (i.e. a breach that does not consist of a failure to pay rent, outgoings or operating the business during the hours specified under the lease).

What happens if the parties can't agree?

A party to a commercial lease may apply to the Small Business Commissioner for either one or both of the following:

- mediation of a dispute in relation to whether or not a tenant is suffering financial hardship as a result of the COVID-19 pandemic; and
- a determination as to whether or not a tenant is suffering financial hardship as a result of the COVID-19 pandemic.

Parties may appeal a determination of the Small Business Commissioner to the Magistrates Court.

Any party to a commercial lease may also apply to the Small Business Commissioner for mediation of any other dispute in relation to issues that have arisen in relation to the COVID-19 pandemic. The issue may arise from, or relate to, the operation of the Act, a commercial lease or any other matter relating to the occupation of the premises or a business conducted at the premises.

The Act does not impose a timeframe within which a dispute must be resolved. It is possible that rent relief arrangements to apply during the crisis period will still be unresolved well after the end of the pandemic.

KEY CONTACTS



SAMUEL BROWN
PARTNER

SYDNEY
+61.2.9513.2466
SAMUEL.BROWN@KLGATES.COM



WILL GRINTER
PARTNER

MELBOURNE
+61.3.9640.4411
WILL.GRINTER@KLGATES.COM



KAREN YUAN
SPECIAL COUNSEL

SYDNEY
+61.2.9513.2467
KAREN.YUAN@KLGATES.COM

This publication/newsletter is for informational purposes and does not contain or convey legal advice. The information herein should not be used or relied upon in regard to any particular facts or circumstances without first consulting a lawyer. Any views expressed herein are those of the author(s) and not necessarily those of the law firm's clients.