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**NEWS**

## **Queensland's new commercial leasing code for rent relief – tips and traps**

The Queensland Government has issued its long-awaited version of the National Cabinet's Mandatory Code of Conduct for commercial leasing (Queensland Code).

Housed in the *Retail Shop Leases and Other Commercial leases (COVID-19 Emergency Response) Regulation*, it impacts leases binding on or before 28 May 2020 and provides relief in relation to rent and lease obligations arising during the period 29 March 2020 to 30 September 2020 (known as the '*response period*').

Here, partner Kristy Dorney and senior associate Helen Wu provide a summary of what all parties to an '*affected lease*' should know about the Queensland Code.

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### **WHAT IS AN 'AFFECTED LEASE'?**

The Queensland Code applies to leases where the lessee is eligible for JobKeeper and is a small and medium-sized enterprise (SME entity).

If the lessee's staff are employed through another connected or affiliated entity, then it is sufficient if that entity is eligible for JobKeeper. There is no requirement for the lessee to participate in the JobKeeper scheme.

An SME entity has an annual turnover of less than \$50 million. This is demonstrated either by reference to the annual turnover in the 2018-2019 financial year or the likely annual turnover in the current financial year.

Where the lessee is connected with or an affiliate of another entity, the lessee's annual turnover is taken to be the aggregate turnover of all of the connected or affiliated entities. Otherwise, the relevant turnover is the turnover of the business carried on by the lessee at the leased premises.

When assessing the turnover of a lessee who is not connected or affiliated with other entities but operates its business at multiple premises, the reference to 'at the leased premises' in the turnover test may lead to the view turnover is to be assessed on a premises-by-premises basis. However, in our view, this is incorrect. The only sensible interpretation of this provision is 'business carried on by the lessee at the leased premises' is a means of identifying the relevant business. If the business itself is operated over multiple premises and online, then the turnover of the business includes the turnover from all of those operations.

If an agreement between a franchisee and franchisor includes a right to occupy premises which the franchisor has separately leased from the landowner, then that franchise agreement may qualify as an *affected lease*. If the franchise agreement qualifies, then the lease between the franchisor and the landowner will be deemed to be an *affected lease* and there is no need to assess whether the franchisor itself satisfies the above criteria.

Leases where the premises are used wholly or predominantly for farming business are excluded along with most leases over

State owned land.

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## RENT REVIEW CLAUSES

Rent under an *affected lease* must not be increased during the *response period*.

Rent reviews should be carried out pursuant to the terms of the lease. However, any resulting rent increase must not be applied until 1 October 2020 at the earliest if the lease is an *affected lease*.

If a lessee has not disclosed sufficient information for a lessor to determine whether the lease is an *unaffected lease* then it will fall to the lessor to make those enquiries of the lessee before any rent increase is applied.

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## RENT ARREARS

If a lessee owes rent for the period pre-29 March 2020, the Queensland Code does not apply, and the lessor is not restricted from acting on that breach such as by calling on security or terminating the lease.

However, if a lessee under an *affected lease* fails to pay rent or fails to open for business during the *response period*, the lessor is prevented from doing any of the following *prescribed actions*:

- terminating the lease
- seizing the lessee's property, including for the purpose of securing payment of rent owing by the lessee under the lease or other agreement relating to the leased premises
- seeking damages for the lessee's default
- requiring the lessee to pay interest, fees or charges on rent or outgoings owing by the lessee
- claiming on the security deposit, bank guarantee or indemnities provided by the lessee or its guarantors for rent or outgoings owing by the lessee
- requiring the lessee or a guarantor to perform their obligations under the lease
- exercising or enforcing another right of the lessor under the lease or other agreement relating to the leased premises.

The lessor may take a *prescribed action* if it has first done one of the following:

- Reached an agreement to reduce the rent payable during the *response period* in accordance with the rent relief provisions of the Queensland Code, and the prescribed action is being taken in response to a breach of that rent relief agreement.
  - Reached an alternative settlement agreement with the lessee where the lessee has expressly agreed to allow the lessor to take the *prescribed action*.
  - Secured an order of a court or tribunal authorising the *prescribed action*.
  - Made a genuine attempt to reach an agreement with the lessee to vary the lease in accordance with the rent relief provisions of the Queensland Code but has not reached an agreement because the lessee has substantially failed to comply with its obligation to negotiate (this includes obligations to give true, accurate and not misleading information sufficient to enable the parties to negotiate in a fair and transparent way).
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## RENT RELIEF NEGOTIATION

A party to an *affected lease* can give notice in writing to the other party to negotiate the rent payable under the lease and other lease provisions.

In practice, the lessee is likely to be the one giving this notice. However, a lessor may consider giving the notice if the lessee has simply stopped paying rent and is not otherwise negotiating or communicating with the lessor.

After the notice is given, the parties are required to exchange relevant information to support the negotiation process.

30 days after sufficient information has been exchanged, the lessor must make an offer to the lessee to reduce the amount of rent payable during the *response period* along with any proposed changes to the lease the lessee asked to be negotiated.

In making the offer, the lessor must have regard to *all the circumstances of the lessee and the affected lease*. This includes, but is not limited to, the reduction in turnover of the business carried on at the leased premises during the *response period*. The following are also to be considered:

- The extent to which a failure to reduce the rent would compromise the lessee's capacity to fulfil their ongoing obligations under the lease.
- The lessor's own financial position and ability to offer rent relief.

Any reduction or waiver of outgoings ordinarily passed on to the lessee under the lease such as land tax, rates, and insurance premiums.

This assessment is important and is discussed in more detail below because once the lessor determines the appropriate rent reduction to be offered, 50 percent of that rent relief must be in the form of a waiver (ie a complete write off of that rent, never to be recovered by the lessor).

Where a lessor wishes to offer a lessee something that may be more generous than what the Queensland Code would otherwise require, the lessor should be careful to explain its reasoning to avoid the lessee later insisting on the 50 percent waiver rule for this relief.

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## DISCLOSURE OF FINANCIAL INFORMATION

There are no limits in the Queensland Code about what information a lessor may ask its lessee to provide to support the rent relief negotiations. However, the lessor would need to explain how the requested document was relevant to enable the parties to negotiate in a fair and transparent way.

Guidance as to what is 'sufficient information' is set out in the Queensland Code and expanded on the Queensland Governments' [business.qld.gov.au website](https://business.qld.gov.au). The guidance reflects the intention of the Queensland Code is to allow consideration of the full economic impact of the COVID-19 pandemic on both parties, not just the decline in turnover.

Examples given of sufficient information include the following:

### From the lessee

- A statement detailing why the lease is an *affected lease*.
- Information demonstrating the lessee is an SME entity (as explained above).
- Evidence of the lessee's eligibility for, or participation in, the JobKeeper scheme
- Accurate financial information or statements about turnover, including:
  - a statement of COVID-19 restrictions imposed on the business that reasonably affected, or will affect, turnover in 2019—20 financial year
  - extractions from an accounting system or lodged business activity statement (BAS) or tax returns
  - information provided to a financial institution
  - expenses that have substantially increased (or have been deferred, waived or suspended) due to COVID-19

- Information about what steps the lessee has taken to mitigate or alleviate the financial impact of COVID-19:
  - Summary of government financial assistance sought and the outcome (including land tax relief for landlords).
  - Material provided by a government agency in relation to financial assistance package availability, eligibility, or acceptance.

### **From the lessor**

- A statement explaining the costs of owning and maintaining the property.
- Extractions from an accounting system or lodged business activity statement (BAS) or tax returns.
- A statement of COVID-19 restrictions (if any) imposed on the landlord that reasonably affected, or will affect, their financial position in 2019-20 financial year.
- Information provided to a financial institution.
- Details of expenses that have substantially increased (or have been deferred, waived or suspended) due to COVID-19.

This is not an exhaustive list and if there is additional information a lessor can explain as being relevant then it can be requested.

If the lessor is *not* relying on its own financial position in making an offer then disclosure of additional information by the lessor is not required.

There is some guidance at [business.qld.gov.au](https://business.qld.gov.au) as to what a lessor should not request. However, there is no explanation for why that information is not considered relevant. Again, if the lessor can explain a valid reason for requiring it, then the request is not prohibited by the Queensland Code.

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## **DEFERRED RENT**

Where the lessor's rent reduction offer includes deferred payment of a portion of the rent, the lessee does not have to start paying this deferred rent until 1 October 2020. The deferred rent is then to be repaid over a period of at least two years but no more than three.

In practice, this might mean a lessee is still paying off the deferred rent after its lease expires. In effect, the deferred rent will operate as a simple debt to be paid off over the agreed period with no interest able to be charged. Bearing this in mind, the Queensland Code allows the lessor to continue to hold any 'security deposit' given to the lessor until the deferred rent has been paid. Although security deposit is not defined, we expect it will include bank guarantees.

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## **LEASE EXTENSION**

In addition to offering a rent reduction, the lessor is required to offer to extend the term of the lease for the same length of time the rent reduction is offered and on the same terms as the existing lease. However, the rent payable during the extension is required to be 'adjusted for the waiver or deferral'.

Although the drafting is unclear, the requirement to adjust the rent 'for the waiver or deferral' during the extension period in our view can only sensibly mean the rent payable during the extension is as per the terms of the lease. However, if the extension falls within a period of time the parties have agreed the rent is to be waived and deferred, then the rent is adjusted to reflect that agreement.

The obligation to offer an extension does not apply where the lessor has already entered into another agreement in relation to the premises which will not accommodate the lease extension. This would include a new lease to a third party or an agreement to commence redevelopment or renovation works to the premises or property.

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## FURTHER RENT NEGOTIATIONS

Most rent relief agreements reached will involve some level of assumption or forecast. Although an agreement may be reached under the Queensland Code, the regulations allow lessees to request further reductions in the rent if assumptions on which the original agreement were made turn out to be materially different.

The same negotiation and document disclosure obligations apply. However, in making the new rent reduction offer, the lessor is not bound to ensure 50 percent of it is new rent reduction includes a waiver.

The section only mentions a further reduction to the rent and not an increase. So, if the actual decline in turnover turns out to be not as bad as forecasted, there is no opportunity for the lessor to require the lessee to pay the waived or deferred rent.

Lessors who would prefer to ensure the rent reduction offered is based on an actual decline in turnover should consider making an offer which requires an end of month or end of quarter reconciliation with the rent reduction, waiver and deferral to be calculated on actual turnover figures.

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## LESSEE NOT COOPERATING

A practical issue arises for lessors in that the Queensland Code restricts lessors from increasing rent and taking prescribed actions against the lessee where the lease is an affected lease. However, the lessor cannot determine whether it is an *affected lease* without certain information from the lessee and will risk breaching the Queensland Code if they increase the rent or take a *prescribed action* if the lessee later shows it was an *unaffected lessee*.

In so far as increasing the rent is concerned, there is no solution for this issue in the Queensland Code.

For *prescribed actions*, protection is afforded under the Queensland Code. However, it requires the lessor to assume the lessee is subject to an *affected lessee* and move forward to make a genuine attempt to negotiate a rent reduction.

Where a lessee fails to provide sufficient information to prove they are subject to an *affected lease*, we recommend the lessor undertakes the following processes to best mitigate against this risk:

- Write to the lessee acknowledging the Queensland Code and each parties' obligations. Include in the letter a list of the questions and information required to determine if the lease is an *affected lease* and the details of the economic impact (if any) on the lessee's business, including turnover. Be precise by listing the information you require or consider attaching a formal questionnaire setting out the information you consider appropriate.
- If the lessee does not respond, we recommend one to two written follow ups.
- If the lessee has still not responded and you intend to apply a rent increase clause or take any of the *prescribed actions*, then write to the lessee advising they have failed to provide information to confirm it is subject to an *affected lease* so you cannot apply the Queensland Code to the lease. Reference the past requests for information that have gone unanswered. Outline in this letter the action you intend to take and the date on which you intend to take it and invite the lessee to contact you prior to that date if it believes it is subject to an *affected lease*.
- If the lessee still does not establish it is subject to an *affected lease*, then proceed with the rent increase or *prescribed action* as foreshadowed in the letter.

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## DISPUTE RESOLUTION

If an agreement cannot be reached in relation to the appropriate level of rent reduction to offer, then either party can bring the matter to a head under the dispute resolution provisions.

The first step is to apply to the Queensland Small Business Commissioner to have the dispute mediated. At the mediation, the parties are required to cooperate and act reasonably and in good faith. If the dispute cannot be resolved at mediation, then either party can apply to the Queensland Commercial and Civil Tribunal (QCAT) to have the dispute determined.

The lessee can also apply to QCAT for orders if the lessor increases rent or takes *prescribed action* in breach of the Queensland Code.

QCAT has wide powers to make orders, including orders about rent payable for the *response period* or how the rent is to be worked out (eg by reference to the turnover of the lessee's business).

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## LAND TAX RELIEF

The Queensland Government is offering rebates and waivers of land tax for eligible properties.

The two percent foreign surcharge on land tax will be automatically waived as will a three-month deferral of land tax liabilities for the 2020-21 assessment.

A 25 percent rebate for the 2019/20 land tax liability is available for properties affected by the COVID-19 pandemic on application only.

Application must be made by 30 June 2020. In making the application, the landowner must agree to provide rent relief to affected tenants 'of an amount at least commensurate with the land tax rebate' and comply with the six leasing principles published by the Queensland Government even if the 'relevant lease' is not regulated. QLD leasing principles

The leasing principles are similar to but not identical to the Queensland Code. They include limits on increasing rent and claiming on bank guarantees and a general obligation to negotiate in good faith with a tenant if their ability to pay rent is impacted by COVID-19. There is no obligation to give a mandatory waiver of rent.

The guidance is unclear as to whether the principles are only applied to affected tenants or all tenants at the building (eg is the rent increase prohibition only for the affected tenant or all tenants in the building?). Further, as the applications for land tax relief are made on a property-by-property basis, it is unclear whether the principles are only required to be applied at the building in question or across the entire property portfolio even if a claim for land tax rebate is not made on the other properties.

With respect to the obligation to pass on the rebate of an amount *at least commensurate with the land tax rebate* it is also unclear how this is to be achieved. For example, if only some of the tenants are affected tenants, is it sufficient to provide relief to the affected tenants proportionate to their share of the overall lettable area and the lessor retains the balance for its own use? Or, must the entire rebate be applied to rent relief to affected lessees? Further, where a lessee would ordinarily pay the land tax liability, is the fact it will now receive a reduction on that liability sufficient to satisfy the obligation to provide rent relief?

Until further guidance is issued, we recommend a common sense approach be adopted by landowners to ensure at least affected lessees receive the benefit of their proportion of the relief either through an outgoings reduction or rent relief. We also consider it reasonable to treat the leasing principles as applying only to affected lessees and only to the property the subject of a rebate application.

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## WHAT SHOULD YOU DO?

Both landlords and tenants need to understand the new regulations and assess the requirements and what their position is.

Our Real Estate lawyers continue to advise landlords and tenants as they navigate the COVID crisis and are readily available to help you work through the new complex requirements imposed by the Code.

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