

Draft Covid19 Code of Practice for commercial property (“the Code”)

Introduction

The purpose of this Code of Practice (“the Code”) is to impose a set of good faith leasing principles for application to commercial tenancies (including hospitality, retail, office and industrial) between owners / operators / other landlords and tenants, in response to the difficulties faced by both parties as a result of the Coronavirus (“COVID-19”) pandemic.

The Code will be given effect through relevant legislation or regulation as appropriate within the United Kingdom and Northern Ireland, including the devolved nations. The Code is not intended to supersede such legislation (and in particular it is not to be interpreted as a replacement for the Pubs Code Regulations 2016) but aims to complement it during the COVID-19 crisis period.

These principles will apply to negotiating amendments to existing leasing arrangements – to aid the management of cashflow for SME tenants and landlords on a proportionate basis – as a result of the impact and commercial disruption caused by the economic impacts of industry and government responses to the declared Coronavirus (“COVID-19”) pandemic, with the further aim of minimising any burden to the taxpayer.

This has been undertaken with the unanimous understanding that the effects of the coronavirus crisis, for which neither side is at fault, can only be overcome by a joint effort. These principles will apply to negotiating amendments in good faith to existing leasing arrangements

Through fair and cooperative dealings, on an equal footing, balanced sharing of burdens should always be pursued. With regard to discourse with political authorities, all parties should ensure that the entire value chain is always represented.

This Code of Practice seeks to safeguard the interests of both landlords and tenants and therefore protect the millions of people they employ and communities they serve.

Code Scope and Objectives

The Code is designed to set out principles of behaviour and responses to difficulties experienced by businesses in order to share the property-related costs and business risks of the COVID-19 crisis in a proportionate and measured way.

The Code seeks to set out principles and good practice in how to balance the interests of landlords and tenants reasonably and responsibly, through as swift and efficient means as possible.

The relationship between landlord and tenant is defined by law and it is not the intention of the Code to alter the basis of the legal relationship or the existing lease contracts, or override arrangements which have already been put in place (for example through side letters or deeds of variation). tenants remain liable for any rent arrears that have not been ameliorated under the provisions of the Code or otherwise, and must remain committed to the terms of their lease unless they are subject to other agreement with the landlord.

It is acknowledged that the Code is not the only government intervention in the commercial rental industry that either has been implemented or may be necessary going forward to support the financial health of the sector. The provisions of the Code will work in tandem with the provisions of the Corporate Governance and Insolvency Bill (when enacted) and The Coronavirus Act 2020 (including but not limited to the moratorium on forfeitures), the time limits on such provisions to be extended alongside this Code as required. The government continues to monitor the situation.

The impact that COVID-19 and the associated closure measures have had generally, and on the income of the hospitality, leisure and retail industries in particular, mean that landlords and tenants must work together collaboratively to find temporary, and where possible sustainable, agreements outside of the existing letter of their leases in order to create a shared recovery plan.

The aim of the Code is to facilitate those discussions by communicating best practice, presenting a unified approach for the industry and providing a framework by which those collaborative agreements can be implemented, monitored and, where necessary, enforced.

The Code applies to all commercial tenancies held by businesses which have been impacted by the COVID-19 crisis, whether in the hospitality, retail, leisure, hotel, offices, industrial and logistics sectors, ports, or agricultural sectors – but it is expected that the hospitality, leisure and retail sectors will have most need of it. Where the Code refers to “rent” this should be taken to refer to all rental elements of a lease or tenancy, including for instance “wet rent” as it applies to ‘tied’ public houses.

Where government support has been provided to businesses, whether landlord (e.g. employee schemes, loans and VAT deferrals) or tenant (e.g. loans and grants), this support is intended to help them meet the costs of maintaining their businesses. While it is recognised that rent is one of these costs, it is important that businesses do not incur unsustainable levels of borrowing in order to cover the costs arising from the pandemic.

The support granted by the government does not provide compensation for loss of income and does not restore either tenants or landlords to the financial position they would have expected to be in pre Covid19. Where support has been provided in the form of borrowing these loans are a financial burden on the recipient.

The Code supports protection for businesses adversely affected financially due to the impact of COVID-19. Protection should be proportionate to the effect, and targeted to benefit businesses in reasonable need of it.

The Code reflects five fundamental principles **ensuring the payment burden is not shouldered by any one party:**

- That there is a broad common interest in ensuring business continuity, building back better, and facilitating the resumption of normal trading activities following a reasonable recovery period at the end of the COVID-19 pandemic, and that therefore the response to the pandemic will be consistent with the principle of fair and lawful dealing by landlords towards their tenants, and by tenants towards their landlords.
- Tenants whose businesses have been adversely affected by the Covid-19 pandemic and the public health response actioned by the government must receive support and concessions from landlords, in addition to government assistance, in order to survive the period of the pandemic and return to profitable trading after a recovery period.
- Where landlords themselves are adversely affected, either by the Covid-19 pandemic and the public health response, or by the level of support and concessions required by their tenants, they should have recourse to further support from the government to ensure their own financial commitments and fiduciary duties can be met.
- Any agreed arrangements will take into account the impact of the COVID-19 pandemic on the tenant, with specific regard to its revenue, expenses, and profitability. Such arrangements will be proportionate, fair and appropriate based on the impact of the COVID-19 pandemic plus a reasonable recovery period.
- The Parties will assist each other in their respective dealings with other stakeholders including insurance companies, governments, utility companies, and banks/other financial institutions in order to achieve outcomes consistent with the objectives of the Code.

The Code has been developed to enable both a consistent national approach and timely, efficient application given the rapid and severe commercial impact of official responses to the COVID-19 pandemic. Potential mechanisms for rent waivers and deferrals will be outlined by the code, but landlords and tenants are free to agree other arrangements as they see fit.

The code does not affect or attempt to invalidate any other offers already made by either landlord or tenant, and both parties may choose to opt out by agreement if they feel a more favourable solution has been found. Where agreements have already been signed prior to the publication of the Code either party may elect to renegotiate their agreement subject to the Code.

Code Time Period

The Code is intended to apply until 24 June 2021. Reviews of the working of the Code will be undertaken by the government at three monthly intervals, and they may decide to extend the code if trade in the relevant commercial sectors is still adversely affected by the Covid-19 pandemic.

The Code of Practice for commercial property

1. **Basis** - The Code does not change the underlying legal relationship or lease contracts between landlord and tenant.
2. **Transparency, Fairness and Partnership** - Landlords and tenants have a mutual interest in business continuity that reaches far beyond COVID-19. They are economic partners, not opponents. Therefore, in all dealings with each other, in relation to the Code and the COVID-19 crisis, they will act reasonably, fairly, transparently and in good faith, and will each provide sufficient and accurate information within the context of negotiations to achieve outcomes consistent with the Code.
3. **Unified Approach** - Both landlords and tenants will help and support each other in all of our dealings with other stakeholders including governments, utility companies, banks and financial institutions to achieve outcomes reflecting the Code's objectives, and to help manage COVID-19's economic and social consequences. Landlords and tenants will further help and support each other transparently in the pursuit of insurance claims arising from Covid19 and ensure that any successful claim will have a consequence on all other negotiations.
4. **Government support** - Where businesses (whether landlord or tenant) have received government COVID-19 related subsidies or reliefs, it is understood that this support has been provided to help businesses meet their commitments.
5. **Acting Reasonably and Responsibly** - Both landlords and tenants will operate reasonably, fairly and responsibly, recognising that everyone is impacted by COVID-19, in order to provide support where it is most needed. Where landlords and tenants, acting reasonably, fairly and responsibly, have been unable to reach a specific agreement a third party mediator could be employed by mutual agreement (if the cost of this is proportionate) to help facilitate negotiations.

In determining what reasonable payment may be made by tenants the following should be considered:

- ❑ Long term sustainability of business vs debt levels required to pay
- ❑ Closure period
- ❑ Duration and extent of restricted trading due to social distancing government requirements and consumer confidence
- ❑ Extra costs and obligations on landlords and occupiers through protecting customers
- ❑ Future cashflows and ability to carry on trading
- ❑ Needs of other stakeholders – banks, employees, suppliers
- ❑ Government support received

6. **Rental Payment or Waiver Plans** - It is recognised that every landlord and tenant relationship is different. As part of that, the rights of landlords and tenants to settle on the rental payment plan that suits them best are respected. However, in seeking a reasonable rental payment plan, both parties should act in good faith, reasonably and flexibly. Tenants seeking concessions should be prepared to provide justification for their request through a transparent approach to the properties in question. Landlords refusing concessions should be similarly transparent should they do so. In both cases this transparency should include financial information to the extent appropriate and relevant, which may differ from case to case.

Agreeing and adhering to a formal written rent payment plan should protect against forfeiture for non-payment of rent under the previous lease terms (to the extent that the rent has been amended by the rent payment plan) after the Coronavirus Act 2020 moratorium on forfeiture is lifted or for leases not covered by the moratorium (e.g. agricultural), for so long as the rent payment plan applies. To help the parties in those discussions rental payment plans should take into account the extent of the impact on the tenant business during the lockdown period and the following period where trade is restricted by social distancing rules and low consumer confidence, and also any product ties. They may include (but will not be limited to) any one or more of the following options:

- a. a deferral of the whole or part of the rent for one or more payment periods, to be paid back over a reasonable period of no less than 24 months to be agreed having regard to the circumstances of the case, up to the remaining payment periods of the lease or whichever is earliest;
- b. a full or partial rent-free period for a set number of payment periods – for example the period of forced closure of a retail unit - which may be in return for a number of measures such as a reversionary lease on reasonable terms, the removal of a break right in favour of the tenant, extension of the lease by a period longer than the closed period, or other agreement with the landlord;
- c. the payment of the rents over shorter payment periods for a set time (e.g. weekly or monthly rather than quarterly) including provision for their payment in arrears. Any arrears payments should be paid back over a period of no less than 24 months or the expiry of the agreement if earlier;

- d. rental variations to reduce ongoing payments to a market rate and/or to provide for all or part of the rent to be paid as a proportion of turnover of the site, incorporating any period during which the site was closed, in return for a reversionary lease on reasonable terms, the removal of a break right in favour of the tenant, or an extension of the lease;
- e. landlords drawing from rent deposits on the basis that the landlord will not then require that the deposits be "topped up" by the tenant before it is realistic and reasonable to do so and over a period no shorter than 24 months from the commencement of the agreement to draw down;
- f. reductions in rent, either in whole or part, across other units occupied by the tenant and owned by the landlord, in return for concessions to the landlord, as part of a negotiated agreement applying to a portfolio of units;
- g. landlords waiving contractual interest rates on unpaid rents to make payment plans more affordable for tenants;
- h. tenants and landlords agreeing to split the cost of the rent for the unoccupied period between them;
- i. any of the above in return for e.g. a reversionary lease on reasonable terms, the removal of a break right in favour of the tenant, or an extension of the lease.

Both parties should seek to avoid unnecessary legal costs and expect that each party should bear their own costs.

Where the agreed arrangements include the deferral of rent, payment of such rental deferrals by the tenant must be amortised over the balance of the lease term and for a period of no less than 24 months, whichever is the greater, unless otherwise agreed by the parties.

7. **Service and Insurance Charge** - In so far as possible, any service charge and insurance charge payable under the Lease should continue to be paid in full. Tenants should prioritise payment of service charge and insurance charges ahead of payments of rent, to ensure that buildings can continue to be insured and safely maintained so that they are ready to support the economy's recovery after the COVID-19 crisis. In relation to service charges:

- a. these should be reduced accordingly where the lack of use of a property has lowered the service charge costs incurred;
- b. conversely, it is acknowledged that in some cases there may be additional service costs required, e.g. in order to operate a building which complies with health and safety requirements in the context of COVID-19, or recommissioning where buildings are reopened

c. landlords should ensure that service charge costs are reduced where reasonably possible and frequency of payment should be spread over shorter periods.

d. where there is a known net reduction in overall service charge due to lack of use of a property (taking into account any additional COVID-19 related costs), this reduction should be passed on to tenants ahead of the end of year reconciliation;

e. landlords should ensure that all management fees reflect any reduced levels of expenditure.

Any solution the parties reach in relation to service charge should take account of the RICS Professional Statement Service Charges in Commercial Property, 1st edition, and of all RICS guidance in relation to service charges and COVID-19.

8. Lender engagement - Landlords and tenants are expected to engage with their lenders and financial providers to seek flexible support in relation to their existing financial arrangements where this is needed.

9. Binding mediation - Where landlords and tenants cannot reach agreement on arrangements under the Code, the matter may be referred by either party to applicable retail / commercial leasing dispute resolution processes for binding mediation, including Small Business Commissioners / Ombudsmen where applicable.

Landlords and tenants must not use mediation processes to prolong or frustrate the facilitation of amicable resolution outcomes.

If at this point, one party refuses to engage with the process, mediation will proceed without their involvement. The mediator and the other party will determine a suitable outcome, which will be treated as an outcome agreed under the Code.