

# The Code of Practice for Commercial Property Relationships Following the COVID-19 Pandemic

## The Beginning of the End of Pandemic Rent Arrears?

UK – November 2021

Since March 2020, an unprecedented number of tenants have withheld rent because of the impact that COVID-19 has had on their cash flow, given the inability of many to trade due to various government restrictions. There are also an unprecedented number of landlords facing financial difficulty and pressure from investors as a result of reduced rental income.

This tension between landlords and tenants has been exacerbated by repeated lockdowns and restrictions on certain sectors since the beginning of the pandemic. Coupled with the seemingly endless extensions to the moratoriums introduced to protect tenants, the struggle by both landlords and tenants to protect their business interests has framed the rental market throughout the past 18 months.

The significant changes to the Code of Practice for commercial property relationships following the COVID-19 pandemic (the Code of Practice), published on 9 November 2021, provides an introduction to the purpose, scope and application of the draft Commercial Rent (Coronavirus) Bill (the Bill).

### Considerations When Negotiating Under the Code of Practice

The Code of Practice sets a framework for landlords and tenants to consider and apply in negotiating the payment of rent arrears that have accrued as a consequence of the COVID-19 pandemic. It emphasises that tenants will be expected to pay their debts if they can afford to do so, and that they shall not automatically be entitled to a concession. For those who are unable to pay their debts, the Code of Practice supports tenants in trying to agree relief with their landlords. At the same time, it makes it clear that landlords should not be left to bear the burden of the COVID-19 pandemic if granting relief would impact their own solvency.

This alert sets out the behaviours and principles expected of landlords and tenants involved in rent arrears negotiations and answers key questions relevant to both parties.

### Behaviour

Landlords and tenants need to display four behaviours when negotiating under the Code of Practice. These behaviours will also apply to the arbitration scheme.

Landlords and tenants have a relationship that is mutually beneficial and essential for business continuity. The behaviours required under the Code of Practice are centred on this founding principle and expect the parties to act transparently, collaboratively, reasonably, responsibly and swiftly.

### Principles

The following principles should be considered by parties negotiating rent arrears:

- The preservation of viable businesses
- The preservation of the viability of the tenant should not be at the expense of the solvency of the landlord
- The relief agreed should be no more than the tenant requires to afford the repayments and if the tenant can pay in full, they should





## Approaching Rent Negotiations Under the Code of Practice – FAQs

### Is the code compulsory?

No, the code is voluntary.

### Do landlords have to agree a concession?

No, but the UK government expects landlords and tenants to negotiate to resolve disputes about unpaid arrears accrued as a consequence of the COVID-19 pandemic. The code says that a tenant should pay rent in full if it can afford to do so, but if they cannot, the parties should try to negotiate with an expectation that the landlord should share the burden – but not at the expense of the landlord's solvency.

### What type of tenancy does the code apply to?

All commercial leases, unlike the draft Bill, which only applies to business tenancies under Part II of the Landlord and Tenant Act 1954.

### What debts does the code apply to?

Rent arrears payable under a commercial lease (including service charge and insurance payments) accrued because of the COVID-19 pandemic. This appears to be wider in scope than the Bill, which applies solely to arrears incurred during specified periods of lockdown/restrictions.

### What if an agreement has already been reached?

Landlords and tenants should honour outstanding agreements. If a tenant makes payments towards arrears without having an agreement in place, they should make it clear what period the payments relate to.

### The tenant occupies a number of properties owned by the landlord – do they need to be considered individually?

No, in these circumstances, a commercial approach would be to consolidate rent negotiations. Notably, the Bill does not appear to allow consolidation of rent arbitration proceedings where there are multiple tenancies with the same landlord, which could make resolving a rent dispute through the arbitration process unnecessarily expensive and time consuming, particularly for landlords with large, extensive leasehold portfolios.

### Is there a time limit on when the arrears need to be paid?

Not where payment of arrears is negotiated under the Code of Practice. However, the Bill envisages a period of no more than two years, which landlords and tenants might sensibly apply to negotiations under the Code of Practice.

### How much rent should a tenant pay?

This will depend on a number of factors, namely:

- If the tenant can pay in full, they should pay in full
- If the tenant cannot pay in full, they will need to demonstrate to their landlord why they need assistance

The Code of Practice envisages taking into account points that will be considered in the arbitration process (once that becomes law) – namely, the viability of the tenant and its ability to pay. This will require the parties to balance the question of how much the tenant can afford to pay against the impact on the landlord's solvency if the debt is compromised or written off.

### How should a landlord assess its tenant's viability and what it can afford to pay?

The Code of Practice sets out a non-exhaustive list of information that a landlord might want to take into account (which will also be relevant to considerations under the rent arbitration regime once implemented) – see the below box. The key point for landlords is that the UK government expects landlords to shoulder some of the burden caused by COVID-19, but not if that might adversely impact the landlord.

In reaching an agreement, a landlord may wish to (if appropriate) provide evidence to show the impact of the tenant's proposals on its own solvency, to ensure that any agreement is fair. However, this may require the landlord to share sensitive information that it may not be willing to (and is not obliged to) share.

### Is the tenant obliged to provide information to its landlord on its financial position?

If a tenant wants to reach an agreement with the landlord, they should be willing to provide evidence to show their financial position. The risk of this is that the landlord will be entitled to scrutinise potentially sensitive company information. It also means that tenants who do not want to pay arrears (rather than cannot pay arrears) will not be able to provide supporting evidence and, therefore, may not be able to reach an agreement with the landlord to reduce their rental liability.

### What is the impact of reaching an agreement on rent arrears on the rent arbitration scheme?

If parties reach a legally binding agreement governing the payment of arrears, neither party can apply for rent to be determined under the proposed rent arbitration scheme.

## What kind of evidence might be helpful when considering viability and affordability?

- Existing and anticipated credit/debit balance
- Assets and liabilities
- Business performance and the impact of COVID-19 on the tenant's business
- Government assistance received and assistance from other parties such as lenders
- Dividend payments to shareholders
- Status of other tenancies within the tenant's portfolio
- Status of the tenant's overdraft limit
- Loss of important contracts or the insolvency of a key customer

The Code of Practice is not designed to keep otherwise insolvent companies solvent. It is designed for companies that cannot afford to pay their arrears or in the case of landlords, grant a concession, but whose business is otherwise viable.

There is no "one-size-fits-all" solution for demonstrating the viability of a business or the affordability of certain proposals. An important part of negotiating under the Code of Practice will be the use of evidence. Tenants will inevitably need to provide more information than the landlord when negotiating. In particular, tenants will be expected to demonstrate why the payment is unaffordable and provide details of what payment and/or payment period would be affordable. Landlords, on the other hand, will be considered to be solvent unless they currently, or are likely to soon be, unable to pay their debts as they fall due.

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