COVID-19 in Singapore: What can Commercial Tenants Do?

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COVID-19 RESOURCES

The global outbreak of the novel coronavirus (COVID-19) is the most critical problem facing the world now. The Singapore government has acted swiftly to reduce the risks of local transmission. At the time of publication of this article, all bars and entertainment venues such as nightclubs, cinemas, and games centres have been prohibited from operating. In addition, all gatherings involving more than ten (10) persons have been prohibited. F&B, retail, and health and fitness businesses have been allowed to continue their operations (but with further precautionary measures)– for now. It is certain that these regulations will, and must, be tightened, if the health situation continues on its current trajectory.

To help businesses affected by these measures, the Singapore government has introduced property tax reductions for landlords, and rental waivers for its tenants. However, landlords in the private sector have not been as quick to pass these savings on to their tenants. On 1 April 2020, the Singapore government announced that it will introduce a bill to suspend enforcement actions by commercial landlords against tenants who are unable to pay their rent as a result of COVID-19, for up to six (6) months. However, this is just a deferral, and not a waiver, of the tenant's obligation to pay rent. It appears that rental payments will continue to accrue for these tenants and will still have to be paid after the suspension period is over.

It remains to be seen when, and to what extent, the Singapore government will step in, to force landlords to reduce rents. In the meantime, tenants whose businesses are affected by COVID-19 may wish to terminate or vary the terms of their tenancies in order to avoid their debts from accruing. This article considers their ability to do so, and seeks to give practical recommendations.

Impact of COVID-19

The most important step for any tenant is to review its tenancy agreement (which would have been difficult for a tenant to negotiate against the large landlords at the outset) to understand the full impact of COVID-19 on their businesses.

Commercial tenancy agreements for the large malls typically require the tenant to open for trade or business every day of the term, and impose liquidated damages for failure to do so. Other obligations include maintaining an illuminated display, keeping the premises secure, and paying for insurance.

These obligations continue to run even if the tenant cannot carry on business as usual, although the landlords may not enforce them in view of the current spotlight on them, coupled with consistent pleas for rental rebates from the Restaurant Association of Singapore (RAS), Singapore Retailers Association and an informal grouping called Singapore Tenants United for Fairness.

Force Majeure

Some, but not all, tenancy contracts contain a 'Force Majeure', clause. This is a common name for a clause that excuses the tenant from strict performance of its obligations, when some supervening event prevents or delays performance.

The effect of a Force Majeure clause depends on the words in the clause, which will vary from agreement to agreement. The key aspects of the clause are as follows:

a) **Scope**: Most clauses will list specific situations that can trigger the clause, such as fire, war, supervening laws and regulations, or a pandemic (usually by reference to the World Health Organization). Other contracts may not list specific examples, but use terms like "act of god" or "force majeure event". These terms are usually interpreted to mean supervening events that are both unforeseeable and unavoidable.

b) **Effect**: Some clauses come into effect if the supervening event prevents, hinders, or delays, performance. However, if there is no such allowance, then the supervening event must make performance impossible, or illegal.

c) **Consequences**: The clause may provide for termination of the agreement at the option of one party. More typically, a clause may entitle one party to suspend performance, or extend deadlines for performance, while the supervening event continues.

The Singapore courts will interpret a Force Majeure clause strictly. This means that the tenant must satisfy the courts that the words in the clause are wide enough to cover the tenant's specific situation. In addition, the tenant must show that it has taken all possible steps to avoid the event or the impact of its consequences.

In Singapore, the large landlords often hold a much stronger bargaining position when negotiating a lease. As such, many commercial tenancy agreements do not contain Force Majeure clauses that would be helpful to a tenant in a COVID-19 situation.

From experience, most tenancy agreements only provide for termination of the lease where the property has been destroyed by fire, or other natural causes. It is uncommon for a tenancy agreement to provide for the waiver, deferment, or suspension of monthly rental in the event of a Force Majeure event. In fact, certain tenancy agreements expressly exclude the payment of monthly rent from the effect of a Force Majeure clause.

In the absence of a Force Majeure clause, the tenant must then consider whether it can seek to argue the termination of the lease on the basis of frustration.

Frustration

Frustration occurs when, due to an unforeseen event which is not the fault of either party, the obligations under the lease are radically different from those the parties contemplated at the point of signing, and can no longer be performed.

The outbreak of COVID-19, and the subsequent regulations that were issued by the Singapore government are clearly events that were no anticipated, and cannot be said to be the fault of either party.

Nevertheless, it will be an uphill task for a tenant to persuade the Singapore courts that the lease has been frustrated. The tenant must establish that it has become impossible to perform the lease, and not merely more expensive or less profitable.

The tenant would be in a better position to establish frustration if the tenant is operating a business which is prohibited by the COVID-19 regulations. For example, a cinema. However, even in such cases, many tenants have tried and failed, as can be seen from the following cases in the UK and Hong Kong:

a) during the 2003 SARS epidemic, a tenant argued that the lease had been frustrated by an isolation order by the Department Health, which meant that it could not be inhabited for 10 days. The Hong Kong court held that a 10-day period was insignificant in view of the 2 year duration of the lease, and therefore did not "significantly change the nature of the outstanding contractual rights or obligations" of the parties (Li Ching Wing v Xuan Yi Xiong);

b) more recently, European Medicines Agency (EMA), an agency of the EU, sought to frustrate its lease of premises in Canary Wharf, UK, when the UK invoked Article 50, triggering its exit from the EU. EMA argued that since it was required by law to be located in an EU country, it would no longer be able lawfully enjoy the lease. The English judge rejected this argument and held that the UK's transition to a non-EU member state did not constitute a "frustrating event", since, following Brexit, the EMA would have legal capacity to deal with, and sublet, the premises in a non-EU country and so it could continue to perform its obligations under the lease.

Based on the above, there is a possibility that the Singapore courts may find that a long-term lease would not be frustrated by a mere closure of malls even for a month. The outcome in each case will be highly dependent on the specific facts of the case.

When a contract is frustrated, it is essentially cancelled. Neither party needs to do anything more for the other. There is no need to pay any sums set out in the contract. If deposits have already been paid, a refund or partial refund may be obtainable.

Negotiations for suspension / holiday / deferment

For the majority of tenants, the most practical route out of the immediate difficulties thrown up by the current crisis, particularly for more established businesses, is to negotiate for a (temporary) adjustment to the rent payable under the lease.

This can take the form of a full-blown rent-free period, or a temporary reduction. However, most of the large shopping malls are owned by REITs, which are hesitant to reduce rents, as they have to take into account the interests of its unitholders. Any significant rental rebates would certainly affect the distribution per unit of these REITs and also further impact on their traded prices, which have already been battered down in recent weeks.

For landlords, there are number of reasons to agree to a reduction in rent during this period, before the Singapore government further intervenes to regulate rent.

If, even after taking into account the deferral provided for in the Singapore government's proposed bill, a tenant is still unable to pay its accrued rent at the end of the deferral period, the tenant may take the view that it should make plans to cease business completely.

With the latest Singapore government measures, the landlords may be unable to commence enforcement actions to recover rental payments, until the suspension period is over. There is certainly no guarantee that the tenant would still be solvent (on a cash-flow basis) by the time the landlord enforces the judgment against the tenant. The landlord may then be left with a judgment that has little economic value. The landlords would then still have to do an impairment of these accrued rent at that stage.

In the meantime, if the landlord loses a tenant, there is no guarantee that a replacement tenant can be easily found, in this current recessionary economic climate. It may therefore be best for the landlord to work towards a solution where all parties can survive the oncoming storm. The landlords must always remember that even for listed tenants in their malls, such tenants may also not survive based on their cash-flow if the precautionary measures imposed on the malls are for a protracted period or more stringent measures are imposed.

Conclusion

The doctrines of frustration and force majeure are complex, and there are serious consequences if misapplied. We recommend that tenants and landlord work towards a sensible compromise that would benefit all parties.

However, if no compromise can be reached, we recommend tenants obtaining legal advice immediately on whether the current COVID-19 situation constitutes a Force Majeure event within the scope and ambit of the relevant clause in the tenancy agreement, or alternatively, a frustrating event given the tenant's circumstances. There may also be other legal arguments that could be mounted depending on the actual factual scenarios.

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