

Article

Bermuda Commercial Leases and COVID-19

Authors: Francesca S. Fox, Director | Oliver Goodwin, Associate

Covid-19 has clearly had a huge impact on both landlords and tenants of commercial premises. In this article we aim to deal with queries that both landlords and tenants may have in respect of their obligations and liabilities under their leases and related insurance claims. This is intended as general advice only since, as with any contract, it will be necessary to review the terms of the lease or insurance policy before giving specific advice.

Does the pandemic change the tenant’s contractual obligation to pay rent?

No. The majority of leases require tenants to pay a fixed annual rent by equal monthly instalments. Many landlords rely on the rent to pay their mortgage. Any failure by the tenant to pay rent on time and in full will be a breach of the terms of the lease allowing the landlord to take enforcement action and (subject to obtaining a Court Order) terminate the lease.

Many leases contain provisions under which rent may be reduced or suspended in certain circumstances. However, these provisions generally only apply when premises cannot be occupied as a result of physical damage caused by an insured risk (such as storm damage or flooding). Otherwise, rent can only be changed by agreement and so any tenants who are having difficulties paying their rent should speak to their landlords as soon as possible with a view to negotiating a reduction or suspension of rent.

Does a landlord have to act in good faith when tenants ask for rent concessions or variations to lease terms as a result of Covid-19?

No, unless there is an unusual term in the lease specifically obligating good faith in these circumstances. Despite there being no legal requirement for landlords to act in good faith there may be wider commercial or reputational reasons, avoiding tenant insolvency for example, as to why landlords may entertain a collaborative approach to agreeing temporary rent concessions or amendments to the terms of the lease.

Considerations when documenting rent concessions and variations to the lease

Where landlords are willing to agree temporary rent concessions or more substantial lease variations it is important that the agreed amended terms are clearly documented and signed by both parties to avoid any future disputes. Following completion, the document must be stamped with \$100 since otherwise it will not be capable of being used in any court proceedings. The parties should consider the following non-exhaustive list of considerations:

- Over what period will the rent concession be applicable? Can this period be extended and if so, how is any extension to be agreed?
- Over what period will the amended terms be enforceable? How is the agreed concession to be documented – by side letter or by deed of variation? Should the new term(s) be personal to the tenant or bind any successors in title of the tenant?
- Has the guarantor to the lease (if any) been party to the discussions and also agreed to the new terms or rent concession?
- Will the tenant be obliged to repay the discounted rent sums in the future or will the agreed rent concession sum be final?

We would always advise parties to seek legal representation to review and formalise any proposed side letter or agreement before any action is taken.

Can a tenant terminate the lease as a result of Covid-19?

The majority of commercial leases are for fixed terms. However it is always important to check whether the tenant has any right to terminate at any time before the end of the contractual term.

If a tenant has remained in occupation following the expiry of a lease term, it will be occupying as a “periodic tenant” and either party will be entitled to terminate the arrangement by giving the other notice (one month’s notice where the rent is paid monthly).

Leases do not generally contain “act of God” or “force majeure” provisions which would entitle either party to terminate or suspend rent as a result of a catastrophic events outside their control. However, if such a provision is included, it would need to be reviewed carefully to see whether or not it covers Covid-19.

Some contracts can be set aside as a result of “frustration” following a force majeure event that makes it physically or commercially impossible for a contract to be fulfilled, or which would result in the performance of the obligation being radically different from that which was anticipated when the parties entered into contract. This is a common law remedy that applies in fairly limited circumstances and generally the courts have been reluctant to apply it to leases. A lease is a contract that is performed over a period of time and, whilst the effects of Covid-19 have been severe and the Government’s Shelter in Place Regulations have prevented tenants from using their premises, it is for a temporary period only. The fact that the economic impact on a tenant may result in the premises being surplus to its requirements does not mean that the performance of the lease obligations has been frustrated.

Are there any potential insurance claims which may assist the parties?

A landlord’s building insurance policy generally covers a landlord against loss of rent for a specified period of time. However, cover is generally only available in respect of losses arising from the suspension or reduction of rent following physical damage to premises caused by an insured risk. Such insurance will not therefore be available to a landlord who agrees a rent reduction with a tenant as a result of Covid-19.

Many tenants will have business interruption insurance but, again, this is intended to provide cover for a tenant who has to relocate or suffers loss as a result of damage to its premises.

Is there any impact on the maintenance obligations and fees?

In multi-let buildings, landlords retain responsibility for the maintenance and upkeep of the common parts of the building. These obligations should be reviewed carefully to see whether the landlord is required to take measures to protect its tenants against Covid-19, for example enhanced cleaning of the common parts. Any failure to comply with such obligations would give rise to potential claims by its tenants for breach of contract.

Many leases provide for tenants to pay a maintenance fee or service charge based on the actual costs incurred by the landlord in respect of its maintenance obligations. In such cases, any increased costs are recoverable from the tenants.

Does the tenant have to allow the landlord access?

Most leases require tenants to allow their landlords access to the premises for inspection purposes and to undertake repairs to the building. This may create issues for tenants both in terms of ensuring that their employees’ exposure to visitors and workmen is limited and, during any periods of lockdown or office closure, providing access in accordance with their obligations. Landlords and tenants should discuss any hygiene protocols in advance and where the tenant is only required to give access at “reasonable times” consider whether, in the current circumstances, the tenant would be justified in limiting the landlord’s access to after normal working hours.

Authors:

Francesca S. Fox
 Director
 francesca.fox@conyers.com
 +1 441 278 7989

Oliver Goodwin
 Associate
 oliver.goodwin@conyers.com
 +1 441 278 7996

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For further information please contact: media@conyers.com