

BRIEFING NOTE

The COVID-19 Virus and The Future of Retail Leases – Exploring Co-Tenancy Clauses in the Context of Singapore

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Introduction

As Singapore steps into its sixth week of Circuit Breaker to limit the transmission of COVID-19 within the community, many sectors of the Singapore economy are affected negatively by this prolonged shut down. Perhaps one of the hardest hit sectors is the retail sector, where physical retail shops are not permitted to operate although rental obligations remain.

In this briefing note, we will look at co-tenancy clauses common in retail leases in the United States of America (the “USA”) but less common in Southeast Asia. We will discuss how parties may negotiate for co-tenancy clauses moving forward from this pandemic.

Overview of Co-Tenancy Clauses

In retail leases, co-tenancy clauses typically allow tenants to reduce their rental obligations if one of the following occurs:

- specifically-named tenants (usually the anchor tenant(s)) exit the mall or remain closed for a certain period of time; or
- certain percentage of the gross leasable retail area remains vacant or closed for a certain period of time.

The rationale of co-tenancy clauses is that anchor tenants or a highly occupied mall draws foot traffic, which is usually the reason a tenant elects to locate in a specific mall. When these factors become absent, foot traffic falls. To protect tenants from the negative impact of reduced foot traffic, co-tenancy clauses often provide for some form of rent reduction.

On the flip side, landlords who agree to the inclusion of co-tenancy clauses create risk for themselves. Landlords may not be able to control tenants’ decisions to close or exit. Yet, when tenants do so, landlords face a ‘domino’ effect of rent reductions from remaining tenants.

Application of Co-Tenancy Clauses in Singapore

In recent headlines, Robinsons department store has announced its exit from Jem shopping mall. Whilst this is the first report of one major retailer exiting from one shopping centre, given the soft market and weak sentiments, it may very well not be the last report. Further, the dampened consumer confidence may make it challenging to replace tenants (especially

larger tenants). If noticeable retail areas are unoccupied, remaining tenants may experience reduced footfall. What then happens to the rental obligations of the remaining tenants?

Adopting the experience in the USA, one way of addressing this in new or renewed tenancy agreements would be to include a co-tenancy clause. If this is done, then there are a number of issues that landlords and tenants should consider:

- Whether the co-tenancy clause may be triggered when: (a) named anchor tenants exit; (b) certain proportion of the leasable retail area remains empty; or (c) a combination of (a) and (b) above?
- Whether landlords must replace a departing anchor tenant with another anchor tenant or whether multiple co-tenants are acceptable? Also, whether the replacement tenant(s) must be in the same trade sector as the departing anchor tenant?
- Whether the landlord is allowed a grace period for filling the departed or vacant space? If so, how long should this period of time be?
- Whether the remaining co-tenants are obliged to remain opened whilst replacement tenant(s) are being sought?
- Whether the remaining co-tenants are obliged to show that sales have actually decreased following the departure and/or vacancy?

How We Can Help

During such tumultuous times, we appreciate that there are concerns about the long-term prospects of the retail sector. We have a strong background advising on commercial contracts, whether on contractual negotiations or assisting with contentious issues. We remain on hand to assist parties through this difficult period.

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