

Rt Hon Jacinda Ardern, Prime Minister
Hon Kris Faafoi
Hon Stuart Nash
Hon Grant Robertson
Hon Simon Bridges
Hon Paul Goldsmith
Hon Todd McClay
Parliament Building
Wellington, 6160

2 April 2020

Dear Prime Minister, Government Ministers and Opposition Members of Parliament

COVID-19 effect on small business leases – call for urgent action to be taken to prevent business closures

We are an industry association that represents New Zealand franchisors and affiliated service providers.

There are over 630 franchised brands in New Zealand, operating around 37,000 individual franchise businesses. The latest statistics we have available show that turnover within the sector amounts to \$27.6 billion, equivalent to 11% of New Zealand's GDP.

A very large proportion of New Zealand's retail and service brands are franchises. Approximately 56% of New Zealand franchises systems are in the retail, food retail, accommodation, real estate and support service sectors. We expect the large majority of these businesses would be premises based. Most franchise businesses are small to medium enterprises, that is, businesses employing 20 people or less.

The income of many franchisors is based on a percentage of sales made by their franchisees. Hence the current market conditions threaten not only franchisee incomes but also franchisors. If a franchisor fails, the entire network of franchisee businesses is also likely to fail (even those who may otherwise have survived the effects of COVID-19).

The Government has instigated the wage subsidy scheme, and other forms of relief to help mitigate the effects of COVID-19. The wage subsidy will certainly go some way to alleviating the financial stress franchisees and franchisors are suffering, but it will still be very difficult for many to stay in business through the period of lockdown and beyond while the market slowly recovers. In order to do that, they need to be able to pay their other significant expenses.

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One highly significant difficulty the franchise sector is now confronting is the inability to make lease payments and the oppressive demands of many landlords. In many businesses rent accounts for one of their largest expense items. Our members are reporting to us is that even where there is a 6th edition ADLS lease (which contains clause 27.5 requiring a 'fair proportion' of rent and outgoings to cease to be payable for the duration of the lockdown), landlords are offering rent rebates that vary from 70% down to as low as 20%. However, where there is no similar clause (which is often the case with older leases and the larger institutional landlords and landlords of large malls), landlords are refusing to do any deals at all. We are receiving regular reports that even the largest and highest profile shopping centre landlords, who have charged very high rent for years, are threatening legal action for unpaid rent as soon as the next day after the rent was due.

Many franchisees have no ability to generate income while their premises are inaccessible. They are simply unable to afford to pay. In a very short period of time, this will lead to mass cancellations of leases and loss of businesses as well as other assets owned personally by franchisees, such as the family home.

In some cases, the franchisor holds all head leases and then sub-leases to franchises. The refusal of landlords to negotiate will also lead to the closure of some key New Zealand franchised brands with an enormous cost to the thousands of families who rely on their franchisees' businesses for employment.

It is acknowledged that banks are offering friendly terms for business loans, but those loans will still need to be repaid on top of existing indebtedness. In many cases the repayments will prevent franchisees from drawing any income from the business. In other words, in many cases, this form of relief is nowhere near enough. With respect, we simply do not think it is realistic to expect that even reduced-interest terms of borrowing from a bank will be enough to see franchise businesses who have commercial leases through this very difficult time. Franchisees must be able to further reduce their costs – a large part of that is obtaining relief from their rental obligations.

We acknowledge that landlords are also victims of this crisis and many have responded well to the call to share loss between themselves and their tenants. However, we are gravely concerned about the behavior of some who have generated healthy profits for years and whose attitude to this situation affects a very wide range and number of tenant businesses.

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One landlord has said:

“Since you are our valuable tenant, we are happy to provide 30% rent relief for April to help you with cashflow conditional that those 30% will be paid one month after Alert level 4 is removed.

At the end of the day we are all waiting for the Government response and package about rents during lockdown, it will clear situations and obligations for the Landlords, Tenants and Banks.

Once the Government package is out, we will all adjust according to the government rules, atm is business as usual”

Our urgent requests of you

We understand you are currently considering some form of intervention in commercial leasing. This is very welcome news.

We urge you to grant a form of rent relief to all tenants of commercial leases.

We believe this could take a variety of forms, including:

- a) compulsory requirement for all landlords and tenants, regardless of whether there is a ‘no access’ clause 27.5 in their lease, to negotiate a fair rent and outgoing reduction, to apply for the duration of the lockdown (and perhaps longer, noting that it will take some time for economic activity to recover),
- b) because there is no legal precedent as to what factors are relevant when assessing a ‘fair proportion’, clarify that a ‘fair proportion’ is to be assessed by reference to all factors bearing upon the parties’ relative capacity to absorb the losses caused by the closedown (these may include the relative economic strength of the parties, the extent to which a party can continue to generate income despite the lockdown – whether by remote working or due to part or all of its business being an ‘essential business’, the likelihood of a party benefiting from a rebound in its demand for its products and services after the lockdown and whether the premises continues to have any benefit to the tenant despite the lockdown (perhaps for storage of imperishable stock or location of a server enabling remote working),



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- c) clarify that the 'fair proportion' of rent and outgoings which shall cease to be payable is to be a rent *abatement* rather than *deferral*. Many landlords are taking the view that while a portion of the rent can be suspended during the lockdown, it must be repaid afterwards. This of course is just another form of credit and creates debt that is simply unsustainable for most tenants,
- d) grant immediate jurisdiction to the Tenancy Tribunal to resolve – online if need be – any disputes between landlords and tenants of commercial leases that arise out of determining what amounts to a fair rent and outgoing reduction,
- e) full or partial lease subsidies provided by the government (subject to fiscal responsibility),
- f) interest free loans (less desirable, given our comments above), and
- g) a freeze on any eviction processes for the duration of the lockdown and a period afterwards – noting that tenants will not have funds to pay rental arrears immediately upon the lifting of the lockdown.

There are no doubt many other solutions and as well we note that the Australian Government¹ has already intervened in relation to commercial leasing concerns.

We would be happy to discuss our views further with you and share with you some real-life examples of the difficulties that commercial leases are presenting for franchised – and many other – businesses.

Yours faithfully,

Robyn Pickerill
CEO

¹ <https://www.business.gov.au/risk-management/emergency-management/coronavirus-information-and-support-for-business/a-hold-on-evictions-for-renters>

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