

Corporate Real Estate

Code of Conduct for Leasing of Qualifying Retail Premises

Introduction

The Singapore Business Federation introduced a Code of Conduct for Leasing of Retail Premises in Singapore ("**COC**") on 26 March 2021. The COC was developed by the Fair Tenancy Pro Tem Committee ("**Committee**"), comprising of representatives of both landlord and tenant communities, members of government, industry experts and members of academia.

The COC aims to provide a set of guidelines for landlords and tenants of Qualifying Retail Premises to enable a fair and balanced position in lease negotiation, and to provide such landlords and tenants with a governance framework to ensure compliance with an accessible dispute resolution framework.

Qualifying Retail Premises ("**Qualifying Retail Premises**") are premises which are:

- (a) held under a lease agreement (which definition includes licence, sub-lease, agreement for lease and accepted letter of offer) entered into on or after 1 June 2021 with a tenure of more than one year; and
- (b) permitted to be used by the Urban Redevelopment Authority ("**URA**") and other relevant authorities for the uses more particularly specified in the COC, which include restaurant, shop, clinic, commercial school, sports and recreation and place of entertainment and even push carts and food kiosks.

The COC is effective from 1 June 2021. Members of the Committee have committed to abide and adopt the COC from 1 June 2021. The REIT Association of Singapore (REITAS) and the Real Estate Developers' Association of Singapore (REDAS) will also encourage their members to do their part as responsible landlords and comply with the spirit of the COC.

It is anticipated that the Government will work closely with the stakeholders, including landlords and tenants associations, to turn the code into legislation, and that Government landlords would also lead by complying with the COC unless there are other statutory obligations to abide by.

A Fair Tenancy Industry Committee ("**FTIC**") is expected to be formed by 1 June 2021 to serve as custodian of the COC and to monitor industry compliance.

This Update summarises the key features and principles of the COC.

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Conduct and Spirit of Negotiations

Part A of the COC sets out overarching principles in the conduct and spirit of lease negotiations. Landlords and tenants must adopt a consensual approach to negotiate in good faith, which includes acting honestly and fairly having regard to the legitimate interests of the other party and observing accepted or reasonable commercial standards of fair dealing in the performance of identified obligations. Nevertheless, they are entitled to have regard to their own commercial self-interest as long as they do not act in bad faith. They can take the position that certain provisions are not acceptable for commercial, business or risk allocation reasons.

Leasing Principles

Part B of the COC sets out 11 Leasing Principles, which include mandatory requirements as well as best practices. Any deviation from mandatory requirements cannot be made unless the Leasing Principle expressly allows for such deviation with mutual agreement. The Leasing Principles cover: (1) exclusivity; (2) cost to prepare lease agreement and third party costs; (3) advertising and promotion charge and service charge; (4) pre-termination by landlord due to landlord's redevelopments works; (5) sales performance; (6) material adverse change; (7) pre-termination by tenants; (8) security deposit; (9) floor area alterations; (10) building maintenance; and (11) rental structure.

If the tenant requests for a Leasing Principle from the COC to be included in the lease agreement, the landlord must include such Leasing Principle.

(1) Exclusivity

As a general rule, provisions preventing a tenant from having another branch or franchise within a certain radius or preventing a landlord from leasing premises for similar trade or business in the same building must not be included whether during or after the end of the lease term. On an exceptional basis, if both parties agree to such provision, a joint declaration must be made to the FTIC within 14 days of the signing of the lease agreement.

(2) Costs to Prepare the Lease Agreement and Third Party Costs

There should be transparency on costs (i.e. upfront disclosure), fees must be legitimate and justifiable, and there must be no profiteering.

Point-of-Sales System ("POS system"): Each party must pay for its own costs for regular maintenance of its own POS system. If the tenant's existing POS is compatible for integration with the landlord's POS system, the cost of integration must be borne on an equal 50:50 cost sharing basis but if the tenant's

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existing POS system is not compatible and has to purchase a new POS system, the additional cost for the new POS system and the cost of the integration must be borne on an equal 50:50 cost sharing basis.

Cost to Prepare the Lease Agreement: If there are no amendments to the landlord's standard lease template (where such template is compliant with the COC), no legal or administrative fees shall be payable by the tenant to the landlord for the preparation of lease agreement. If the tenant requests for amendments to the landlord's standard lease template (where such template is compliant with the COC), the tenant must bear either the legal costs or administrative costs (but not both) of the landlord. If the tenant requests for amendments to the landlord's standard lease template (where such template is not compliant with the COC) to address any deviation from the COC, the landlord must bear the legal costs or administrative costs (but not both) of the tenant. These provisions would require landlords to review their own standard lease templates upfront to ensure that they are COC compliant. In this respect, the COC contains sample clauses for redevelopment, termination under exceptional conditions and determination of floor area.

Third-Party Costs: "Catch-all" provisions requiring tenants to pay all unspecified and generic third-party costs are not permitted, and all third-party costs (e.g. consultant fees, vetting fees) which are to be borne by the tenant need to be communicated upfront to the tenant and set out clearly in the lease agreement, save that the landlord is entitled to charge the tenant either administrative fees or legal fees (but not both) for preparation of ancillary documents arising from tenant-initiated requests, such as side letters.

Sales Audit Fees: Landlords would only be allowed to require sales audit where the rent includes a gross turnover component. Where the tenant's POS system is integrated with the landlord's POS system, in place of an annual audit sales report submission, tenants must be allowed to provide an upfront monthly undertaking by their director or certified public accountant on the accuracy of sales submission concurrently with the tenant's monthly sales submission and annual statutory declaration by director. Any right for the landlord to request the tenant to submit an annual audited sales report must be set out in the lease agreement with the requirement for the landlord and tenant to share the cost of such annual audited sales report on a 50:50 basis.

Where the tenant's POS system is not integrated with the landlord's POS system, the tenant would need to comply with the landlord's requirement for sales verification as set out in the lease agreement. In such event, if the landlord requires annual sales audit and annual audited sales report, the tenant would have to bear the full cost of such audit.

Public Liability Insurance: Where the Qualifying Retail Premises has a floor area of 15,000 square feet or less, the landlord cannot require tenant's public liability insurance coverage to be more than S\$3 million or the public liability insurance coverage limit in the landlord's public liability insurance policy, whichever is lower.

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Electricity Charges: In cases where the landlord is on the En-bloc Contestability Scheme and the landlord arranges for purchase of electricity for the building for an electricity retailer of its choice, the costs charged by the landlord to the tenant must be on a pass-through basis without mark-up or price discrimination among tenants of the same building but the landlord may charge reasonable administrative costs (but not infrastructure costs) if communicated upfront to the tenants.

(3) Advertising and Promotion ("A&P") Charge and Service Charge

While the landlord may adjust the service charge and A&P charge during the lease term, the overall gross rent after such adjustment must not increase.

(4) Pre-termination by Landlord due to Landlord's Redevelopment Works

Landlords would only be entitled to pre-terminate if they intend to carry out substantial redevelopment, asset enhancement or reconfiguration works to the building or part of building where the premises are located ("**redevelopment works**") and require vacant possession for such works. The landlord would not be able to pre-terminate purely to change the tenant mix in the building without carrying on redevelopment works or if the landlord is able to carry out such redevelopment works without requiring vacant possession of the premises. At least six months' prior written notice would be required, but if such redevelopment works are required to be carried out by law or authorities' requirements ("**Requirements**") and the time period given to the landlord does not permit the requisite six months' notice, the landlord must give such notice to the tenant promptly upon being aware of such Requirements.

If the initial lease term is pre-terminated due to the redevelopment works, the landlord must pay the tenant a compensation sum calculated based on the agreed declared value of the tenant's fit out capex works less depreciation on such agreed declared value amortised on a straight-line basis across the initial lease term. Where the tenant has carried out renewal capex works as agreed between landlord and tenant, and the renewal term is pre-terminated due to redevelopment works, the landlord must pay the tenant a compensation sum calculated based on the agreed declared value of the tenant's renewal capex works less depreciation amortised on a straight line basis across the renewal term. Prior to entry into a binding lease agreement, the landlord and tenant, acting reasonably, shall discuss in good faith on items to be included as tenant's capex works and the estimated value for computation of the agreed declared value.

Where the landlord has obtained URA Written Permission for any asset enhancement initiative works, the landlord must inform the tenant of the same before signing the lease agreement. Otherwise, in addition to the capex compensation sum (as set out above), a further compensation sum would be payable by the landlord. In the event the landlord and the tenant are unable to agree on the additional compensation sum, either party may escalate the matter to the Singapore Mediation Centre ("**SMC**").

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(5) Sales Performance

As a general rule, clauses which allows the landlord to pre-terminate if a specified sales target is not met must not be included in the lease agreement. However, on an exceptional basis, if both parties agree to include such provision, they must make a joint declaration to FTIC within 14 days after the signing of the lease agreement.

(6) Material Adverse Change

Landlords and tenants are encouraged, but it is not mandatory, to re-negotiate the lease agreement where the tenant is prevented, obstructed or hindered from performing its typical business activity due to events beyond its control (e.g. store closure due to public health interest).

(7) Pre-termination by Tenants

Tenants may require a right to pre-terminate the lease with six months' notice or six months' gross rent in lieu, upon either of the following exceptional conditions:

- (a) the business principal of the goods and/or services from which the tenant has obtained the right to sell such goods and/or provide the services being retailed in the premises is insolvent; or
- (b) the tenant loses the distributorship or franchise rights to sell the goods and/or provide the services being retailed in the premises for reasons not due to the non-performance or breach by the tenant of the distributorship or franchise agreement.

A compensation sum equivalent to the security deposit would be payable by the tenant to the landlord for such pre-termination and the landlord may apply the security deposit towards such compensation sum. While the COC specifies that any shortfall in the security deposit must be made good by the tenant, such application of the security deposit by the landlord would effectively leave the landlord without security for other breaches or outstandings.

(8) Security Deposit

Security deposit for Qualifying Retail Premises with floor area of up to 5,000 square feet and lease term of up to three years shall not exceed three months' gross rent. Where the parties mutually agree to an alternative security deposit amount, they must make a joint declaration to FTIC within 14 days of the signing of the lease agreement.

If the tenant does not wish to provide cash security deposit, the tenant needs to notify the landlord before signing the lease agreement and the landlord must accept up to 50% of the security deposit by a non-cash mode (e.g. "on demand" bank guarantee) based on landlord's prescribed format. Subject to the

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landlord's acceptance, the tenant may choose to provide the security deposit by way of a personal guarantee (e.g. from their director) in lieu of cash or bank guarantee.

A cover-all guarantee clause stating that the tenant's directors, shareholders, employees or any person are personally liable in cases of default by the tenant must not be included in the lease agreement.

(9) Floor Area Alterations

For each new letting, the landlord must provide a registered surveyor's certificate confirming the surveyed area before handover or by such later date as the parties may agree. If the surveyed floor area is larger than the floor area specified in the lease, there would be a corresponding upward adjustment of gross rent and security deposit subject to a 5% cap. If the surveyed floor area is smaller than the area specified in the lease, there would be a corresponding downward adjustment of gross rent and security deposit provided that if the difference is more than 10%, each party has the right to terminate the lease without liability by giving notice within one month of the landlord's provision of the surveyor's certificate.

All adjustments shall be with effect from the commencement date of the lease.

(10) Building Maintenance

The landlord must be responsible for any loss or damage suffered by the tenant due to the gross negligence or wilful default on the part of the landlord to maintain the building.

(11) Rental Structure

As a general rule, rental formula must be based on a single rental computation throughout the lease term and must not have an "either/or, whichever is higher" formula. On an exceptional basis, if both parties agree to an alternative rental structure, a joint declaration must be made to FTIC within 14 days of the signing of the lease agreement.

Data Transparency

Part C of the COC deals with data transparency. Landlords who collect sales data from tenants as part of the Gross Turn Over rent structure must share sales data metrics by trade category (i.e. total monthly sales and total floor area) on a one-on-one basis before signing the lease agreement, and bi-annually for existing tenants. For reasons of confidentiality, sales data would not be shared where the number of tenants for the relevant trade category is less than three.

If a confidentiality clause is included in the lease agreement, it needs to mutually apply to both landlord and tenant.

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Checklist, Dispute Resolution and Enforcement of Code of Conduct

Landlords are required to provide a completed checklist in the form set out in the COC when the landlord sends the first draft lease agreement to the tenant. The checklist must indicate any deviation from Leasing Principles or whether such Leasing Principle is not applicable. Nevertheless, the tenant must conduct its own due diligence to review the lease agreement. Once the lease agreement is signed by both parties, it is binding on them.

For incidents of non-compliance during lease negotiations, either party may refer non-compliance to the FTIC. If many reports are made against a particular party, FTIC may name and shame such party. If the signed lease agreement is not compliant with the COC, either party may escalate the non-compliance as regards Leasing Principles and Data Transparency to the SMC within 14 days of signing the lease agreement. In such event, the parties must attend mediation sessions and comply with the resolutions of the SMC.

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