

# **Federal Commercial Rent Abatement Strategy – Mar. 30, 2020**

Prepared by: Save Small Business, a grassroots coalition of 20,000+ small businesses across Canada and the Toronto Association of Business Improvement Areas (TABIA), representing 40,000+ businesses

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## **Executive Summary**

Recent announcements by the Federal government to support small business have received significant praise. Increases to wage subsidies, more generous loans and deferral of sales tax collection will all help many companies. However, local small businesses – “main street” businesses – will likely not benefit from these supports. These businesses, forced in many cases to close in order to protect their communities from the COVID-19 public health crisis, have largely laid off their staff. They have also expressed limited interest in taking on additional debt, on any terms, as indicated by the almost 22,000 businesses who have signed the petition at [savesmallbusiness.ca](https://www.savesmallbusiness.ca), our survey results and those of the CFIB, as well as many media reports.

This paper describes in more detail the problems with a debt-based solution to the short-term cash flow needs of local small businesses, and offers a rent abatement strategy to address their largest remaining cost. This matter is urgent, as both our survey and other recent surveys suggest that at least 25% of local small businesses will not be able to pay rent on April 1st, and many more will fail to pay May rent. In the absence of a broad solution on rent, it is likely that many of our community businesses will close permanently over the next few months.

In summary, this paper recommends:

1. That the federal government directly provides aid to commercial landlords in order to provide a financial incentive for them to voluntarily reduce or waive rent for their tenants.
2. That Provinces be encouraged put a moratorium on commercial lease lockouts, preventing landlords from locking out tenants on April 1 while the implementation of this strategy is developed. (See Appendix C)
3. That all levels of governments put significant public pressure on banks to defer property debt principal payments without accruing interest. (See Appendix A)
4. That the Federal government works with provinces and municipalities to agree on a property tax and utilities abatement strategy for April, May and June.
5. That the federal government announces the framework of a rent abatement strategy prior to April 1 in order to avoid significant confusion and mass lock-outs of businesses on that date.

## **Rationale for recommended strategy**

### **1. Poor outlook for local small business**

- Many local small businesses have seen revenue declines over 80% and have already laid off most, if not all, of their staff. The little revenue they have left is often insufficient to pay fixed costs. Please see attached results from a survey of signatories to our petition.

- It is clear from our survey and that of others that there will be many permanent local small business closures after rent is due in April and then again in May. If economic recovery from the COVID-19 crisis is to be robust, it is critical for as many of these businesses as possible to be ready to re-open when social distancing is eased.
2. Discomfort with debt as a solution
    - Savesmallbusiness.ca was created in part because of a concern that debt would be used to support local small businesses. In the last week, almost 22,000 small businesses have signed our petition asking for non-debt solutions to their forced closure.
    - Our view is that there is a fundamental unfairness in asking businesses to close to protect the community, and then asking them to take on debt to make sure costs like rent, phone bills and debt payments are paid in full. This crisis calls for more equitable burden sharing.
    - Many media reports and our survey results support these concerns. (Media links: [1](#), [2](#), [3](#), [4](#))
  3. Impracticality of Canada Emergency Benefit Account (CEBA) loan roll-out to local small business
    - Owners are unlikely to be able to get the legal and financial advice they would require in order to take on loans given the current crisis.
    - Banks are currently struggling to manage requests for mortgage deferrals, and the Business Development Bank of Canada (BDC) has had significant challenges with demand for credit. It is unlikely that banks will be able to service the hundreds of thousands of local small businesses that would require loans to pay fixed costs. Given the number of businesses who will not be able to pay April 1st and May 1st rent, many businesses will be permanently closed by the time the program ramps up.
  4. Desire to include landlords in a solution to save local community businesses
    - Significant anecdotal evidence suggests that many landlords are offering interest-bearing deferrals to tenants, which will be hard to pay back once social distancing is eased.
    - Landlords and tenants want the same thing: for tenants to be successful. However, their relationship is likely to turn adversarial if businesses fail to pay April rent.
    - One rationale for current landlord behaviour is fear that leniency will set a standard they can't maintain if this crisis lasts longer than expected, and uncertainty about what other landlords are doing. A national strategy with a specific approach will relieve landlords of those concerns and makes it easier for them to work with their tenants to ensure their survival. As a matter of fairness and effectiveness, rent abatement in some form will be required to allow local small business to survive this crisis.

### **Strategic considerations**

- Attempt to share burden between governments, landlords, banks and small business
- Target to commercial landlords as the most efficient point of contact to deliver support
- Avoid requirement for legislation, either Federal or Provincial
- Limit complexity in design, communication and implementation
- Allow for speed in execution
- Ensure that support applies to all business forms, and not just Canadian Controlled Private Corporations (CCPCs)

## **POLICY RECOMMENDATION: Pay landlords directly in exchange for waiving rent**

The goal of this strategy is to provide a framework and an incentive for commercial landlords to voluntarily reduce or waive rent for their tenants. The costs of evicting a tenant are significant, both in the form of legal costs and lost rent during vacancy. Given a compelling alternative, most landlords would choose to make it easy for their tenants to stay. Provinces may choose to add to this strategy by mandating that landlords accept these terms, but that is not essential for these strategies to succeed.

*Provinces should be encouraged to prevent landlords from locking out tenants while the details of this program are being developed.*

### **Cash payments directly to landlords**

- Federal government offers to pay 60% of any rent reduction offered by landlords to tenants, up to a maximum of \$6,000 per tenant per month
- To qualify, businesses need to have annual revenue less than \$5M
- Landlords would provide the following information along with a request for payment:
  - Proof of rent amount, either in the form of a returned rent cheque or bank statement
  - Business number of tenant and landlord
  - Commitment to reduce rent by either the entire amount owed, or \$10,000, whichever is lower, from April to June
  - Attestation by business that their revenue is less than \$5M
- Upon receipt of the above, payment would be made to landlords in a lump sum for three months in exchange for reduced rent as described above
- We suggest that cheques would be sent out upon receiving information from landlords, with audits to be performed at a later date
- Landlords would be required to show proof in their 2020 tax reporting that they reduced rent by the amount expected. Failure to show a reduction in income from these properties would result in significant penalties.
- The list of properties receiving payments from government, and the amount received, will be published in a searchable database, allowing tenants to ensure they received the appropriate abatement.
- Two examples of how this approach would work:
  - Rent is \$3,000 per month. Government pays landlord \$5,400 ( $\$3,000 \times 60\% \times 3 \text{ months}$ ), and tenant's rent is waived from April - June
  - Rent is \$15,000 per month. Government pays landlord \$18,000 (60% of first \$10K, for three months) and tenant's rent is reduced by \$10,000 to a total of \$5,000 per month from April to June
- The attached spreadsheet shows the financial result for landlords
- Appendix B describes another version of this strategy, using tax credits instead of cash and requiring the tenant to pay 25% of their rent costs

### **Benefits for tenants and landlords**

The benefits for tenants are obvious, but there are also significant benefits for landlords.

- Reasonable financial terms, as landlords will lose only the equivalent of approximately one month's rent with this strategy. The financial argument for landlords is significantly enhanced if banks were to take action as described below to defer mortgage principle interest-free.
- Clear framework for how to work with tenants who have been significantly affected by COVID19, and who express an inability to pay rent
- Better near-term cash flow, as the alternative for many is unpaid rent
- Administration required is significantly less than negotiating and executing rent deferrals
- More certainty about future income, as many fewer businesses will need to close

#### **Estimated cost to the Federal government of above strategies**

- Using Statistics Canada data, we calculated the total number of businesses with less than \$5M in revenue in five industries likely to be most affected by COVID-19 to get a rough estimate of cost
- For these nearly 500,000 businesses, the total monthly rent is approximately \$1B
- Therefore, covering 60% of rent would cost approximately \$600M per month, and \$1.8B total
- This is certainly an overestimation, as not all landlords would apply for this offer.
- \$1-1.5B is likely a better estimate for the total cost of this program.
- Please see simple spreadsheet attached.

#### **Associated Strategy for Taxes and Utilities**

After rent, the next largest category of fixed costs for most local small businesses are property taxes and utilities. The following policies would supplement the rent abatement strategy and ensure more small businesses will survive this crisis:

- We agree with the following recommendation from the CFIB on property tax relief:
  - "Provincial governments should provide substantial commercial property tax relief for the duration of the crisis. Specifically, we recommend:
    - Provinces cover property taxes for the duration of the COVID crisis (a minimum 25 per cent overall reduction in annual property taxes). British Columbia has already moved to cut its school taxes for commercial properties in half, which likely provides around 20 percent relief in overall property taxes for the year. Provinces could either significantly reduce property tax rates on their portion of property tax bills or provide money to municipalities so they can reduce their portion of the taxes.
    - Provisions for property tax relief should include that all property tax relief be passed on to tenants (this is automatic for triple-net leases)."
- The Federal government and the Provinces should work together on a cost-sharing agreement to reduce and defer utilities costs where possible.

## **Appendix A: Role of Banks in success of strategy**

In the discussion about abatement or waiving of rent, landlords often raise the issue of their own expenses. If they were to waive rent, how would they pay their mortgage? It's a reasonable question. Anecdotal evidence and media reports to date suggest that landlords are having a hard time deferring their mortgages, and when they do they are being asked to pay interest on the deferral. This provides limited incentive to pass along reductions in cash outflows to tenants, and encourages landlords to suggest deferrals instead of abatements.

A broader, easier and more generous approach to commercial property debt by banks would significantly increase the likelihood of the success of this policy. It is strongly urged that the federal government and the banks come to an agreement that allows for the deferment of principal, without interest, and the waiving of interest payments for the three months addressed by this strategy. Banks should apply this more generous approach automatically for landlords with property debt on fewer properties, who are less likely to be able to afford an abatement strategy.

There is significant dissatisfaction among the respondents to our survey of [savesmallbusiness.com](https://www.savesmallbusiness.com) signatories about the role that banks have played to date. Significant pressure on banks by all levels of government would be seen positively by the small business community as the current belief is that the needs of banks take precedence.

The participation of banks is also critical for small businesses who also own their properties. The proposals in this document are targeted at rent abatement and as a result will not benefit any business owner who has purchased their property.

## **Appendix B: Tax Credits for Landlords in exchange for waiving rent**

If paying in cash is deemed too complicated, or too slow, a similar outcome could be achieved with tax credits. This approach benefits significantly from better support from the banks as described above, as current cash flow for landlords would be worse. It also works well in conjunction with the Canada Emergency Business Account, as landlords would be able to repay loans when tax refunds are issued. They are also receiving HST deferrals, easing cash flow concerns in the short-term. In this example, we show an approach that includes some rent contribution from tenants, again to help with short-term cash flow. The approach would be the same as cash payments, with the following modifications:

- Refundable tax credit offered on 60% of reduction of rent, as long as rent is reduced by at least 75% of the total amount of the rent or \$10,000, whichever is lower.
- Administration would largely occur when reviewing 2020 tax returns, as landlords would be asked to submit an additional form outlining the reduction in rent with associated proof that the rent reduction occurred.
- Three examples of how this approach would work:
  - Rent is \$3,000 per month. Rent is reduced by \$2,250. Tenant pays \$750 and government provides \$1,125 per month in refundable tax credits. Proceeds to landlord are \$1,875
  - Rent is \$10,000 per month. Rent is reduced by \$7,500. Tenant pays \$2,500 and government provide \$3,750 in refundable tax credits. Proceeds to landlord are \$6,250
  - Rent is \$15,000 per month. Rent is reduced by \$10,000. Tenant pays \$5,000 and government provides \$5,000 in refundable tax credits. Proceeds to landlord are \$10,000
- This approach is likely administratively easier for government, especially in the short-term, but the lack of up-front cash may reduce uptake by landlords
- The attached spreadsheet shows the financial result for landlords

## **Appendix C: Suggested Announcement Strategy**

It is advised to announce this strategy prior to April 1 in order to avoid significant confusion and mass lock-outs of businesses on that date. Studies show that 25% of small businesses have less than two week's cash on hand, meaning it is likely that at least 25% will not be able to make April rent. Our survey suggests the number is somewhat higher, as nearly 40% of respondents indicated they would not be able to make April rent. An announcement should cover the following points:

- It is a priority for the federal government to reduce the rent of small businesses over the next three months
- Over the weeks to come, a strategy will be announced that will help landlords reduce and waive rent for their tenants, funded by the federal government
- It is highly recommended that Provinces to not allow commercial landlords to lock out businesses for non-payment of April rent
- The government will be working closely with Canada's banks to enhance the offering to reduce and defer mortgage payments for commercial properties, as it believes the approach to date does not meet the requirement to help businesses and landlords survive this crisis