

# Intelligence MEMOS



From: Michael J. O'Connor

To: Bill Morneau, Minister of Finance

Date: May 22, 2020

Re: **COMMERCIAL RENT PART 3: LEVELLING THE PLAYING FIELD**

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Final details of the commercial rent relief program for small businesses announced in April emerged this week. That they arrived more than half-way into the eligibility period is just one signal that the [Canada Emergency Commercial Rent Assistance \(CECRA\)](#) risks missing the mark in providing the necessary support to salvage such businesses shuttered by the pandemic lockdown.

Time will tell if landlords realize the important burden placed on them to ensure qualifying tenants have the opportunity to re-open and boost Canada's economic growth in the aftermath of the pandemic. The Canadian Federation of Independent Business estimates that following the COVID-19 lockdown, 42 percent of small businesses will close permanently, and that 58 percent will not be able to pay their May 2020 rent. With an August 31 deadline to apply, there is a limited amount of time to implement a solution that fits small business tenants, landlords and lenders alike if CECRA is to have any positive impact on the economic recovery.

CECRA lacks the precision, debate and transparency of the legislative process that the [CERB](#), [CEWS](#) and [CESB](#) programs have benefitted from. However, the CECRA funding remains a significant financial incentive for a landlord to reduce a tenant's rent by at least 75 percent and participate in the program administered by the Canada Mortgage and Housing Corporation (CMHC). This model should attract landlords to participate since the alternative for many small businesses may result in no rent at all.

However, CECRA misses the mark in two fundamental ways. First, it does nothing to level the playing field between landlord and tenant. In fact, it puts the decision to participate squarely in the hands of the landlord, exacerbating the existing power imbalance. Second, it originally introduced a [secured mortgage lender](#) into the equation, but placed no burden on them. In fact, it in effect collateralizes the lender's interest by making debt service payments (principal and interest) one of the eligible uses of the funds. Absent debt service payments, landlords now seem to have the flexibility to cover other running costs.

Here are some ideas to deal with these issues:

To put the landlord and the tenant on a level playing field, the federal and provincial governments would have to provide an unconditional prohibition or suspension of a landlord's eviction and other customary rights in the event of a failure to pay rent. CECRA restricts evicting affected tenants during April, May and June 2020 (the Target Period), but only with the landlord's consent. Restricting the prohibited evictions period to the three-month period of the COVID-19 lockdown is insufficient time to see how businesses will perform following the re-opening. [Australia](#), [New Zealand](#) and the [U.K.](#) have all made efforts to level the playing field between landlords and tenants with a moratorium on commercial evictions; none have committed to fund a portion of tenants' rent. If commercial evictions rise above historical levels, the federal government should encourage all provinces to bring in a moratorium until at least September 2020.

Participation in CECRA should be made mandatory so that small business tenants can seek the protection and reliefs offered; with an opt-out by otherwise eligible business tenants and landlords acting in good faith. This would go a long way towards bringing reluctant landlords into a reconsideration of the lease agreements for the period of the COVID-19 lockdown and re-opening.

CECRA appears designed to protect lenders' interests as much as to provide support for tenants. Lenders are however not required to fund any portion of the program. While there are a number of programs available to support lenders such as the Insured Mortgage Purchase Program, much more can be done to encourage secured mortgage lenders in providing additional relief to small business landlords.

For example, lenders could be encouraged by the federal government to waive a borrower's requirement to pay or accrue interest on debt of properties premised by small businesses eligible for the CECRA program during the Target Period. Instead the mortgage payments would be regarded for those three months as payments of principal only. Normally the Canada Revenue Agency will accept a waiver that would otherwise give rise to taxable income between arm's length parties and should be prepared to do so in these circumstances without there being any negative tax consequences to either the borrower or lender. The reduction in the lender's interest income would reduce their current tax bill. The income tax saved on the three months of interest waived could be reinvested by the lender in new investments, with the yield over the remaining term of the mortgage going a significant way towards compensating lenders for the interest waivers but otherwise preserving their cash flow.

Given the reported reluctance of some landlords to participate in CECRA, landlords and tenants should as a minimum seek to involve the lenders in the renegotiations of lease terms by considering the feasibility of a waiver of the landlord's interest during the three months covered by CECRA. Obviously, if there is no lender, then it simplifies the situation and such landlords are better positioned to participate in the CECRA on their own account.

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