

Lease defaults

As New Zealand continues to navigate through a period of economic uncertainty, it is important for landlords and tenants to be vigilant of potential lease default risks and be mindful of different ways to respond to issues that may arise.

PLA cancellation provisions

Where a tenant has defaulted under a lease by an unremedied failure to pay rent or breach of any other covenant or lease condition, the Property Law Act 2007 (**PLA**) governs lease cancellation. Lease cancellation under the PLA is highly process and timeframe driven and requires accuracy to ensure that cancellation of the lease is effective, to prevent delays and to minimise litigation risk arising from improper cancellation of a lease and re-entry of premises.

At a high-level, a lease can be cancelled where:

- a tenant has breached a covenant or lease condition (including rental arrears for no less than 10 working days);
- the tenant has been served notice of the landlord's intention to cancel the lease (**PLA Notice**); and
- the breach has not been remedied by the end of the period specified in the PLA Notice.

PLA Notice

PLA Notices must strictly comply with the PLA and so accuracy in drafting and serving PLA Notices is critical. Failure to accurately draft and serve PLA Notices can result in the PLA Notice being ineffective which can potentially result in costly delays and expose a landlord to a risk of liability for improper cancellation of a lease.

Broadly, a PLA Notice must contain information about the breach, how the tenant needs to remedy the breach and the time period within which the tenant is required to remedy the breach. Additionally, a PLA Notice must be served on parties that have an interest in the lease - for example, mortgagees and receivers of the leasehold estate and any sublessees.

In addition to claims to remedy the lease breach, a landlord may also be able to claim additional monies owed related to any breaches that have occurred - for example, legal fees, default interest, marketing costs of re-marketing a premises and lease tail. Landlords should seek advice to determine what may be recovered.

Effective service of a PLA Notice is important. To avoid any issue of improper or ineffective service, best practice is to engage a process server as a means to provide certainty of service of the PLA Notice.

Guarantees and Security

Standard business practice is for a landlord to hold some form of lease security. If lease security is in place, then it is important to review the terms of the security at the time the PLA Notice is issued and have a clear path of how the security can be enforced. This is particularly relevant where a bank guarantee is in place as it will likely require the original to be produced with a specific form of notice provided to the bank in order to access the secured funds to remedy the claimed default.

Peaceable re-entry

If a tenant does not remedy the breach within the timeframe specified in the PLA Notice, a landlord may seek to regain possession of the leased premises.

Peaceable re-entry is a process by which possession of the premises is regained by the landlord without the use of force. Whilst exercising re-entry, a landlord must take reasonable care of the possessions of the tenant and provide the tenant the opportunity to collect them.

Given the potentially combustible circumstances where a landlord seeks to regain possession of the premises, it is advisable to keep accurate records of communications with the tenant and the re-entry process and, to the extent possible, ensure that both parties are in agreement on timeframes and appropriate times for repossession. Landlords need to be particularly mindful to ensure that re-entry is undertaken in a legal manner or risk a claim by the tenant or even criminal charges.

Alternative options

In a challenging leasing market, in some circumstances it may be preferable to take a longer view and maintain a relationship with a current tenant with future prospects, even in the face of lease defaults.

There are a number of ways to support tenants to avoid the cancellation of a lease. For example, a landlord may wish to offer temporary rent relief or deferral of the obligation to pay rent to enable a tenant to continue to trade and eventually re-pay rental arrears or remedy the breach of lease. Landlords can also facilitate or assist with an assignment of the lease, subletting part of a premises or even a surrender (or partial surrender) of the lease to allow a more liquid tenant to take over the lease obligations.

In addition to advising on lease defaults, we can assist with all aspects of leasing transactions so please contact us to discuss any queries you have.



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