

# Rent relief for small businesses: COVID-19 and Canada's Emergency Commercial Rent Assistance Program

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On April 24, the federal government announced plans to partner with the provinces and territories to establish the Canada Emergency Commercial Rent Assistance program (CECRA) to provide rent relief for small businesses<sup>1</sup>. The initial announcement was short on specific details and raised many questions as to how the program would operate in practice. On May 14, Canada Mortgage and Housing Corporation (CMHC), which will administer CECRA on behalf of the Government of Canada and its provincial and territorial partners, released further details which clarify the program and the eligibility and application requirements<sup>2</sup>.

Under the CECRA, CMHC will provide forgivable loans to eligible commercial property owners who agree to reduce the monthly gross rent owed by their impacted small business tenants by a minimum of 75% for the months of April, May and June 2020. The loans are intended to cover two-thirds of the rent reduction (50% of the monthly gross rent owed by impacted tenants during the applicable 3-month period) while the property owner will bear not less than one-third of the rent reduction (not less than 25% of the monthly gross rent) as a reduction of its rental income. The tenant will remain responsible for paying no more than 25% of the monthly gross rent for the 3-month period. Loan funds will be deposited directly into the property owner's bank account.

Specific details concerning the application process and required documentation for CECRA loans are not yet available but CMHC has announced that an online application process for eligible property owners will open in the second half of May 2020. The application will include both fillable online forms and template forms of documents that will have to be submitted as proof of eligibility for the program. During the application process, property owners will need to provide evidence of an existing rent reduction agreement and attestations confirming eligibility for each impacted tenant asking for help. The deadline for applications will be August 31, 2020.

## Eligibility: property owners

To qualify for CECRA, a commercial property owner must:

- own or be the landlord of a “commercial real property” which is occupied by one or more “impacted small business tenants”;
- have entered into a rent reduction agreement with an impacted tenant which provides for a rent reduction of at least 75% for the period of April, May and June 2020, as well as a moratorium on evictions for that same period; and
- have declared rental income on its personal or corporate tax return for tax years 2018 and/or 2019

Helpfully, the criteria now include not only owners of freehold property, but also ground lessees who sublease commercial premises to impacted small business tenants. Landlords and tenants who are not at arm's length will be eligible to participate in CECRA so long as there was a valid and enforceable lease agreement in place prior to April 1, on no greater than market terms.

Previous confusion concerning references in the government's initial announcement to landlord "profit" and "costs" and what rent was to be reduced have now been clarified by the requirement for reductions of monthly gross rent which would include both monthly minimum or base rent and additional rent.

Commercial real property is defined as commercial properties with small business tenants. Commercial properties with a residential component and multi-unit residential mixed-use properties would also qualify for the program with respect to their small business tenants. However, CECRA loans are not available for tenants of any federal, provincial, or municipal-owned properties. CMHC has also confirmed that the program will apply regardless of whether or not the applicable commercial property is mortgaged. This clarifies previous announcements which suggested that only mortgaged properties would be eligible.

## Eligibility: impacted small businesses

Impacted small business tenants are businesses, including non-profit and charitable organizations, that:

- pay no more than \$50,000 in monthly gross rent per location pursuant to a valid and enforceable lease agreement in place prior to April 1;
- generate no more than \$20 million in gross annual revenues, calculated on a consolidated basis at the ultimate parent level; and
- have experienced at least a 70% decline in pre-COVID-19 revenues.

CMHC has specifically confirmed that eligible small business tenants who are in sublease arrangements are eligible for the CECRA program, if their subleases meet the foregoing program criteria.

For the purposes of calculating revenue losses, small businesses can either compare their revenues in April, May and June 2020 to the revenues earned in the corresponding period in 2019 or to the average of their revenues earned in January and February 2020. The tenant's revenues must be earned from ordinary activities in Canada calculated using its normal accounting methods and excluding revenues from extraordinary items. A question remains, however, as to whether the tenant's revenues are to be calculated on a location-by-location basis or a cumulative basis across all of the tenant's locations.

## Retroactive application

While CECRA offers assistance only for the 3-month period of April, May and June 2020, property owners will be permitted to apply for assistance once the 3-month period has ended if they can prove eligibility during those months. If rent for the 3-month period has been collected at the time a CECRA loan is approved, the property owner will be required to either refund amounts paid by the applicable tenant or, if agreed between the parties, give the tenant a credit for rent payable in a future 3-month period.

## Forgiveness of rent and CECRA loans

The CECRA loan agreement and the rent reduction agreement will each include a covenant by the property owner not to recover forgiven rents when the program is over, including by way of future rent increases. CECRA loans will be forgiven if the property owner complies with all applicable program terms and conditions, including the covenant not

to recover forgiven rents. This effectively prohibits the use of CECRA loans to fund rent deferral arrangements. The terms of the forgivable loans and the timing of that forgiveness are not set out in the details published by CMHC to-date.

## Analysis

CMHC's most recent program update has responded to some of the initial questions and criticisms that arose out of the federal government's initial announcement of CECRA – particularly those relating to what rent is covered, whether landlords who are ground lessees can participate and initial suggestions that only mortgaged properties were eligible. However, concerns remain as to how effective the program will be in practice.

The program does not afford relief directly to impacted tenants. Tenants needing assistance must rely on the co-operation of their landlords to provide a rent reduction and apply for a CECRA loan. Will landlords participate in the program? There is no mechanism to force landlords to do so. To the extent that landlords are required to provide a rent reduction and to bear at least one third of the cost of such rent reduction (i.e., not less than 25% of the monthly gross rent), there is a disincentive for landlords to participate. Most landlords would prefer a rent deferral arrangement to an outright rent reduction and, in practice, most rent deferral arrangements apply only to base rents, not to gross rents (unlike the CECRA program which requires forgiveness of gross rents). In addition, landlords of mortgaged properties may have given negative covenants to their lenders which prohibit lease amendments that waive or reduce rent obligations without lender consent.

Furthermore, the application process requires landlords to attest as to the qualification of each impacted tenant as part of the application process. In practice, we expect that this will necessitate a fair bit of financial disclosure being made by tenants (on an individual and consolidated basis) to their landlords which may be a disincentive for tenants themselves to ask their landlords to participate. It also suggests that landlords will need to consider a reasonable degree of diligence in respect of their tenants' (and their parent entity's) finances, which many landlords may not be willing or able to do.

On the other hand, the program is only available to certain qualifying tenants. Tenants who pay more than \$50,000 per month in gross rent for any particular location, whose gross annual consolidated revenues (at the ultimate "parent" level) is more than \$20 million or whose revenues for the period April to June 2020 have declined by less than 70% will not be eligible for relief. While the program appears to be available on a location-by-location basis, more clarity is required concerning whether the tenant's revenue decline is to be determined on a location-by-location basis or on a cumulative basis across all locations. Impacted tenants will need to seek the co-operation of their landlords to apply for CECRA relief and may only receive partial relief depending on which of their landlords are willing to participate in the program.

There is also a question for real estate investment trusts whether the forgiven loan is "bad income" for specified investment flow-through (SIFT) tax purposes that remains to be answered.

Finally, only minimal details concerning the application requirements and the terms and conditions applicable to the CECRA loans have been released to date. It remains to be seen whether CMHC will establish a standard set of specific terms and conditions for such loans or leave it to the discretion of CMHC approved lenders to establish market loan terms within CMHC directed parameters as is done for CMHC insured residential mortgages.

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<sup>1</sup> <https://pm.gc.ca/en/news/news-releases/2020/04/24/prime-minister-announces-partnerships-provinces-and-territories>. See also: <https://news.ontario.ca/opo/en/2020/04/ontario-canada-emergency-commercial-rent-assistance-program.html>

<sup>2</sup> <https://www.cmhc-schl.gc.ca/en/finance-and-investing/covid19-cecra-small-business>

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