

The impact of COVID-19 on commercial lease agreements

The closure of many companies since the first lockdown in March 2020 and the resulting economic slowdown have caused high tensions between lessors and lessees of commercial premises. Some tensions escalated to disputes, some of which have already been brought before French courts. Law No. 2020-1379 of November 14, 2020 authorizing the extension of the state of health emergency and introducing various measures to manage the health crisis (the “Law”) has supplemented the measures taken as early as in March 2020 by the French Government concerning the performance of commercial leases agreements.

The adoption of the Law provides the opportunity to address the issue of commercial leases in the context of the health emergency measures that have been taken, as well as the options currently available to lessees and lessors to overcome this unprecedented crisis.

Understanding the health measures taken in relation to commercial leases agreements

1. In order to provide support to the economy to deal with the serious repercussions of the health crisis, the French Government had been empowered – pursuant to Law No. 2020-290 of March 23, 2020^[1] – to take, by way of Ordinances, any measures to postpone in full or spread out the payment of rents relating to business and commercial premises and to waive financial penalties and suspensions that may be applied in case of non-payment by lessees.

2. Under the terms of two Ordinances dated March 25, 2020^[2], the French Government has set up a mechanism to protect commercial lessees against the risk of rescission of the lease agreement in the event of non-payment of rents during the health crisis.

Ordinance No. 2020-306 of March 25, 2020 applies to all contracts and temporarily renders termination clauses ineffective for a legally protected period between March 12 and June 23, 2020.

Ordinance No. 2020-316 of March 25, 2020 prohibits the application of penalties or termination clauses in case of non-payment of rents and service charges that fall due during a protected period running from March 12 to September 11, 2020 (two months after the end of the state of health emergency). However, it can only be invoked by natural persons and private law legal entities who/which carry out an economic activity and are eligible for the solidarity fund mentioned in Article 1 of Decree 2020-371 of March 30, 2020.

As a result of the successive restatements of the provisions governing the solidarity fund, the protective measures provided for under (Article 4 of) Decree 2020-316 should now apply to any and all private law entities not controlled by a holding company, having been subject to an administrative ban on receiving the public in March 2020 or having lost more than 50% of their turnover, employing no more than 10 people and with a turnover of less than 1,000,000 euros for the last ended financial year.

These two statutes freeze some of the penalties incurred by the lessee in case of non-payment of the rent during the health crisis, but do not, however, suspend the payment of such rent.

3. In the fall, the French Government imposed new lockdown measures and extended the state of health emergency for one month, effective from October 17, 2020.

4. **The Law of November 14, 2020** authorized the extension of the state of health emergency until February 16, 2021 and introduced various measures to manage the health crisis, including concerning the relationships between lessors and lessees^[3].

The scheme applies to: natural persons and private law legal entities who/which carry out an economic activity affected by an administrative police measure taken because of the epidemic (in particular curfews, regulations concerning the opening to the public, meetings and activities on public highways and public spaces, establishments that have been subject to a temporary closure or regulated opening).

The closure of the business does not appear to be required as long as it is sufficient that the activity has been affected by an administrative police measure. On the other hand, if a company has several establishments, it will only be entitled to benefit from the scheme for the premises affected by said administrative police measure.

The Law also specifies that, in addition to this requirement, additional eligibility criteria (in particular, number of employees, turnover and loss of turnover) will be set forth in a forthcoming Decree.

Regarding the measures adopted with a view to alleviating the financial penalties and other sanctions

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incurred by defaulting lessees, the rents and service charges remain due but the payment default will not be (immediately) sanctioned.

As such, the relevant companies may not (i) be charged interest or financial penalties (ii) or incur any actions, sanctions, interim measures or enforcement measures for late payment or non-payment of rents or service charges relating to premises that are subject to an administrative police measure.

The Law also specifies that personal sureties and liens that guarantee the payment of the relevant rents and service charges may not be enforced.

Lessors eligible for the scheme may benefit from these protection measures until the expiry of a period of two months from the date on which their activity ceases to be affected by an administrative police measure.

At the end of this period, the lessor will regain its rights and may sue the defaulting lessee and any guarantors, or resume suspended enforcement proceedings.

Means of action available to lessors and lessees

Like the March 2020 Ordinances, the provisions of the Law concerning commercial leases do not suspend the payability of the rent and do not, therefore, exempt the lessee from paying it.

This issue of the payment of rent has already given rise to a substantial amount of litigation.

Many practitioners consider that the lessee's obligation to pay the rent could be undermined under ordinary contract law. This concerns in particular arguments based on force majeure, unforeseeability (a French law concept close to that of hardship), non-performance, deprivation of enjoyment resulting from the closure of businesses or the requirement according to which contracts must be performed in good faith.

To date, the decisions issued on this matter were handed down in relation to the March 23, 2020 Ordinance, but they do give an initial indication of how judges reacted to these arguments.

In two cases adjudicated on the same day, two lessors applied to the summary judge to obtain payment of the rents due for the second quarter of 2020^[4].

In both cases, the judge, to deny the requests of the plaintiffs, considered not only that these requests were seriously disputed but also dismissed a certain number of arguments put forward by the lessees.

As the two cases concerned the obligation to pay a sum of money, the judge dismissed the plea of force majeure as being ineffective in these circumstances. He also considered that it had not been demonstrated that the lessor had failed to fulfill its obligation to deliver the premises, since the health context, which was not attributable to it, could not in itself constitute such a failure on the part of the lessor.

Although the judge did not rule on the merits in these two cases, he nevertheless recalled that contracts must

be performed in good faith, which means that the parties are required, in exceptional circumstances, to check whether such circumstances do not make it necessary to adapt the terms and conditions governing the performance of their respective obligations. In both cases, in order to hold that the lessors' claims were seriously disputable, the judge recalled that the lessee's business sector had been harshly affected and that the lessee had brought evidence – by producing exchanged letters – that it had approached its lessor to try and find an amicable solution.

However, it all depends on the circumstances.

In another decision handed down this summer^[5], the summary judge of the Paris Judicial Court, relying on the same rationale, granted a request for payment made by a lessor on the ground, in particular, that the tenant had never formalized a clear request for the remission of its debt or requested an adaptation of its obligations.

Given the variety of situations that may exist (e.g. closure of a restaurant in accordance with applicable legal provisions vs. closure of a retail business pursuant to a decision of the operator itself because of its inability to guarantee to its employees that applicable hygiene standards will be complied with), it seems essential to remain pragmatic in order to avoid, as far as possible, the implementation of lengthy and costly legal proceedings at a time when both lessors and lessees are encountering financial difficulties.

Therefore, even if the interests of the two parties are diverging, dialogue and the search for an amicable outcome should, in certain circumstances, definitively be favored.

In order to encourage lessors to make a move in this direction, Mr. Bruno Lemaire, French Minister of the Economy, Finance and the Recovery, specified on October 30 that a tax credit would be introduced in the 2021 Finance Bill to prompt lessors to cancel part of their rents. This measure should benefit companies with less than 250 employees, subject to an administrative ban on receiving the public or operating in the restaurant and hotel industry. Any lessor which, over the last quarter of 2020, agrees to waive at least one month's rent could benefit from a tax credit of 50% of the amount of rent waived, up to a maximum of 800,000 euros. To date, this draft measure has been adopted on first reading by the French National Assembly as part of the vote on the first part of the 2021 Finance Bill.

^[1] Emergency Law No. 2020-290 of March 23, 2020 to deal with the Covid-19 epidemic

^[2] Ordinance No. 2020-316 of March 25, 2020 relating to the payment of rent, water, gas and electricity bills for the business premises of companies, the activity of which is affected by the spread of the COVID-19 epidemic, and Ordinance No. 2020-306 of March 25, 2020 on the extension of deadlines expiring during the state of health emergency and on the adaptation of procedures during that same period

^[3] Article 14 of the Law

^[4] Paris Judicial Court, October 26, 2020 No. 20/53713 and No. 22/55901

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[5] Paris Judicial Court, July 10, 2020, No. 20/04516

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