

COVID-19 impact on commercial leases

NOTE TO READER: This document is up-to-date as of April 24, 2020. The current unprecedented situation and the novelty of the statutory measures to neutralized certain contractual deadlines and/or other contractual sanctions in case of payment default from tenants imply clarifications from courts and daily reviews that may complete or change our analysis. We invite you to contact us for any questions regarding any potential rent suspension request.

1. LEGAL PROVISIONS IMPLEMENTED FOR VERY SMALL ENTERPRISES ("VSE")

1.01	Main eligibility criteria ¹	<ul style="list-style-type: none"> (i) activity having started prior to February 1, 2020; (ii) headcount not exceeding 10 employees; (iii) annual turnover of less than EUR 1,000,000 <u>or</u> average monthly turnover of less than EUR 83,333 (if the enterprise is less than one year old); (iv) not controlled by a commercial company within the meaning of Article L. 233-3 of the French Commercial Code; and (v) which is subject to the statutory prohibition of receiving public between March 1, 2020 and March 31, 2020 <u>or</u> which suffered a loss of turnover equal to or higher than 50% in March 2020 compared with March 2019.
1.02	Consequences ²	<ul style="list-style-type: none"> » contractual sanctions are neutralized (as well as legal sanctions in the context of insolvency proceedings) in case of default of a tenant to pay rent and rental charges relating to professional and commercial premises, due between March 12, 2020 and the expiry of a 2-month period after the end date of the state of health emergency, i.e., July 23, 2020 at midnight; » unpaid sums during the relevant period remain due and payable to the owner and shall be paid thereafter. Deferred payments shall be negotiated between owners and tenants.

¹ The conditions of eligibility to such legal measures are defined in article 1 of the Decree N°2020-378 dated March 31, 2020 which refers to paragraphs 1° and 3° to 8° of Article 1 and 1° and 2° of Article 2 of Decree No. 2020-371 of March 30, 2020.

² Article 4 of Ordinance No. 2020-316 of March 25, 2020.

2. COMMERCIAL MEASURES IMPLEMENTED BY CERTAIN OWNERS AND GOVERNMENTAL GUIDELINES

2.01	Main owners organization involved	<ul style="list-style-type: none"> » <i>Fédération des Sociétés Immobilières et Foncières (FSIF);</i> » <i>Association Française de la Gestion Financière (AFG);</i> » <i>Association Française des Sociétés de Placements Immobiliers (ASPIM);</i> » <i>Caisse des Dépôts et Consignations (CDC);</i> » <i>Conseil National des Centres Commerciaux (CNCC);</i> » <i>Union Nationale des Propriétaires Immobiliers (UNPI) ;</i> » <i>Fédération Française de l'Assurance (FFA).</i>
2.02	Targeted tenants	VSE and Small and medium-sized enterprises ("SME") whose activity has been interrupted pursuant to the Orders of March 14 and 15, 2020 and Decree No. 2020-293 of March 23, 2020 (" Mandatory Closure Orders ").
2.03	Suggested measures ³	<ul style="list-style-type: none"> » payments of rents and charges on a monthly basis; » suspension of the collection of rents and charges from April 1, 2020, and for subsequent periods of cessation of activity imposed by the French Government⁴; » implementation of payment rescheduling without penalty or interest; » cancellation of rents up to 3 months (excluding service charges) for VSE belonging to one of the sectors whose activity has been interrupted pursuant to Mandatory Closure Orders; and » for the other businesses affected by the Covid-19 crisis, discussions shall be initiated on a case-by-case basis.
2.04	Other owner's initiatives	Some owners, such as Icade, Ceetrus France or La Compagnie de Phalsbourg have announced a cancelation of 2 or 3-month rents for most of their tenants affected by the measures taken to fight Covid-19 epidemic.
2.05	Governmental guidelines ⁵	<p>The French Minister of the Economy:</p> <ul style="list-style-type: none"> » has urged major institutional real estate companies (i) to cancel 3-month rent due by VSE which have been forced to cease their activities to fight the Covid-19 epidemic and (ii) to initiate discussions with big retail networks to discuss any acceptable rent rescheduling. » appointed Jeanne-Marie Prost, a Cour des Comptes member, to organize a mediation between professional owners federations and trade federations to agree on framework agreements and a code of good conduct in order to allow owners and businesses to reach satisfactory solutions with respect to the rent issue.

³ In a press release dated April 10, 2020, FSIF announced that 9,000 tenants, mainly VSE-SME, have already benefitted from a rent suspension.

⁴ Measures announced in press releases dated March 20 and April 17, 2020, available on FSIF website (www.fsif.fr).

⁵ Such guidelines are not binding

3. LEGAL TOOLS INVOKED BY TENANTS TO SUSPEND THEIR RENTS

3.01 Force majeure⁶

(a)	Principles	<p>If the parties have not agreed any other specific definition of force majeure, force majeure will be qualified if the three following conditions are met:</p> <ul style="list-style-type: none"> » <u>exteriority</u>: the considered event shall be beyond the control of the person which intends to invoke the force majeure (in the case of a lease, the tenant); » <u>unpredictability</u>: the considered event shall not have been reasonably expected at the time of the conclusion of the contract. For leases entered into since the end of February/ beginning of March 2020, the predictability of the epidemic consequences is likely to arise; » <u>unavoidability</u>: consequences of the considered event were not avoidable through appropriate measures, i.e., for a lease, the tenant's rent payment obligation became <u>impossible</u> to perform (and not only more expensive). It implies that a tenant shall provide supporting documents and demonstrate that the effects induced by the administrative restrictions measures, put it in an unavoidable situation (<i>irresistible</i>). Such as, being deprived of any cash, it is unable to pay its rents and charges (evidencing the causal relationship). <p>At this stage, it is too early to determine whether courts will consider the Covid-19 epidemic as an event of force majeure in lease matters. Judges will assess the facts at their sole discretion, on a case-by-case basis. However, please note that case law of the last few decades:</p> <ul style="list-style-type: none"> » has not recognized force majeure for the dengue⁷ and chikungunya⁸ epidemics on the grounds that these epidemics were either predictable or surmountable; and » is generally reluctant to recognize force majeure to allow a debtor to avoid a monetary obligation⁹ and thus to avoid a tenant's obligation to pay its rent.
(b)	Consequences	<p>Benefits of force majeure qualification for tenants are still being discussed. Such benefits, depending on the legal ground invoked, could be the following:</p> <ul style="list-style-type: none"> » <u>suspension of the rents (and charges)</u>: in case of temporary and partial impediment of lease performance, in the light of case law which has so far been rather detrimental to tenants, the tenant would obtain a postponement of the payment of its rent, which would then remain due but would be rescheduled to the following monthly or quarterly instalments; or » <u>cancellation of the rent</u>: if the tenant is successful in demonstrating that during the period of closure, it faced a partial but definitive (and no longer temporary) impediment of the lease performance.

⁶ Article 1218 of the French Civil Code.

⁷ CA Nancy, November 22, 2010, N° 09/00003.

⁸ CA Basse-Terre, December 17, 2018 N° 17/00739.

⁹ Cass. com., September 16, 2014, N° 13-20.306.

(c)	Comments	<p>» For businesses whose closure has been decided by Mandatory Closure Orders (bars, restaurants, cinemas, retail clothing stores, etc.), tenants may attempt to invoke the benefit of force majeure to request a temporary suspension of rent payments.</p> <p>In the absence of clear provisions adopted by the legislator in this respect, we believe that judges should nevertheless (i) check whether, in the lease, as it is often the case, the parties did not intend to leave at the risk of the tenant any administrative closure measure not imputable to the owner and (ii) assess whether, notwithstanding this administrative closure, the activity and/or the financial health of the tenant did not allow it to carry on its activity (even partially) despite the administrative closure and to pay the rent and charges. Judges may therefore apply a different treatment based on the type of activity and financial strength of the tenant, on a case-by-case basis, even in the event of administrative closure of the premises.</p> <p>» For businesses whose administrative closure has not been decided by Mandatory Closure Orders but whose economic activity has been very seriously impacted by the various restrictions implemented to fight the Covid-19 epidemic (e.g., hotels) and tenants of office spaces, it seems that, in the light of case law and in the absence of clear provisions adopted by the legislator in their favor, it may be more difficult for them to justify their rent suspension on the ground of force majeure. They will need, in any case, to demonstrate that the consequences of the administrative measures taken to fight the Covid-19 epidemic, like in railways and airways sectors, put them in an unavoidable situation leading them to be deprived of any cash and therefore unable to pay their rents and charges (evidencing the causal relationship).</p>
3.02 Unpredictability (<i>Imprévision</i>) ¹⁰		
(a)	Criteria	<p>» occurrence of an unforeseeable event, assessed at the date of signing of the contract;</p> <p>» continuation of the lease - the payment of the rent - has become "<u>excessively onerous</u>" due to the occurrence of such event.</p>
(b)	Consequences	<p>» obligation for the owner to renegotiate the terms of the lease (this is an obligation of means and not of result);</p> <p>» if negotiations fail, tenant may request the judge to revise or terminate the contract.</p>

¹⁰ Article 1195 of the French Civil Code.

(c)	Limits	<ul style="list-style-type: none"> » article 1195 of the French Civil Code does not apply to commercial leases entered into prior to October 1, 2016¹¹; » as Article 1195 of the French Civil Code is not of public policy (<i>ordre public</i>), a large majority of commercial leases entered into after October 1, 2016 expressly excludes the benefit of unpredictability; » for leases entered into after October 1, 2016 that do not exclude the benefit of Article 1195 of the French Civil Code, a tenant willing to invoke unpredictability to renegotiate the terms of its lease will have, in addition, to demonstrate that on the signing date of the lease, the Covid-19 epidemic was unpredictable.
(d)	Comments	<p>Even if the tenant may validly invoke the benefit of Article 1195 of the French Civil Code, it will nevertheless remain liable for the payment of rent until an agreement is found with the owner or until judicial revision of the lease. This reduces the practical short-term interest to invoke unpredictability for a tenant facing immediate economic difficulties.</p>
3.03 The obligation to deliver ¹² , and the exception of non-performance ¹³		
(a)	Criteria / Principles	<ul style="list-style-type: none"> » the owner's obligation to deliver premises - which is the rent consideration - requires the owner to make available and maintain throughout the term of the lease, premises that are available and in a condition to be used for the purpose for which they have been leased; » the exception of non-performance (<i>exception d'inexécution</i>) is a threatening tool allowing a party to invoke a significant default (or a threat of such default) of the other party to justify its own default, until the other party executes its obligation; » businesses subject to Mandatory Closure Orders may attempt to invoke default of their owners' obligations to deliver and, as a result, in response, on the basis of the exception of non-performance, decide to stop paying their rent.
(b)	Effects	<p>If the default of the owner's obligation to deliver the premises is recognized (which he may contest on the ground of force majeure), the tenant will be definitely exempted from its own obligation to pay the rent during the relevant period.</p>
(c)	Limits	<p>Article 1219 of the French civil Code, which is the legal ground of the exception of non-performance, is not qualified as public policy (<i>ordre public</i>). A careful review of the lease will be necessary to determine if the parties have excluded such provisions.</p>

11 Date of entry into force of Ordinance No. 2016-131 dated February 10, 2016 reforming the law of contracts. For such leases, the old case law which denies the benefit of unpredictability to private law contracts should therefore continue to apply (Cass. Civ. 6 mars 1876, *Canal de Craonne – C. Appel Chambéry, Ch. civ., 1ère section, 13 mai 2014, n° 13/01212*).

12 Article 1719 of the French Civil Code.

13 Article 1219 of the French Civil Code.

(d)	Comments	<ul style="list-style-type: none"> » Mandatory Closure Orders can be viewed as targeting the activity carried out by the tenant rather than to the premises themselves. As a result, the owner has not ceased to make the premises available and cannot be held liable for the consequences of a measure that has affected the tenant's activity; » in addition, a large number of leases provides that administrative closures which are not due to the owner shall be at tenant's risks. In such case, the lease will continue and the rent will be fully due; » then, even if the Mandatory Closure Orders affects the premises, such measures are the result of the "<i>Fait du Prince</i>" and as such, this situation constitutes for the owner a case of force majeure exempting it from any failure¹⁴. The owner would then be exempted from any liability.
4. OWNERS' LEGAL TOOLS TO FORCE RENTS PAYMENT		
(a)	Guarantees	<p>If, following a rent payment default decided by a tenant on the ground of force majeure, unpredictability or exception of non-performance, the parties fail to reach an agreement on a rent suspension, the owner may seek to call the guarantees granted by the tenant to secure its obligations (i.e. deposit or guarantees granted by third parties).</p>
(b)	Termination clause and its limits within the state of health emergency	<p><u>Principles:</u></p> <ul style="list-style-type: none"> » It is only in a final phase, once all other remedies have been exhausted (i.e., guarantees drawn down and contractual sanctions applied (interest for late payment, compensation, etc.)), that the owner may decide to issue an order to pay (<i>commandement de payer</i>) to its tenant, under the threat, if not executed within one month, to invoke the benefit of the termination clause (Article L. 145-41 of the French Commercial Code)¹⁵. » The judge of urgent matters (<i>juge des référés</i>) may then confirm that the termination clause has been validly triggered, unless there is a serious dispute, in which case the dispute will be referred back to the merits. It may also decide to suspend the effects of the termination clause by granting the tenant a payment rescheduling.

¹⁴ Cass. 3ème civ., 9 octobre 1974, n°73-11721 and Cass. 3ème civ., 23 janvier 2008, n° 06-19520.

¹⁵ Any exercise of this termination clause will have to be done in good faith, which will be assessed at the time of the delivery of the order to pay (Cass. civ., 3ème, 1er févr. 2018, n° 16-28.684).

		<p><u>Limits:</u></p> <ul style="list-style-type: none"> » Pursuant to Article 4 of Ordinance No. 2020-306 of March 25, 2020 as amended, “When their purpose is to sanction the default of an obligation within a specified period, any penalty payments, damage clauses, termination clauses as well as the clauses providing for a forfeiture, are deemed not to have taken effect or to be effective, if this period has expired during the period defined in I of article 1. [i.e. between March 12 and June 23, 2020 at midnight] <p><i>In case of default, effectiveness of such penalty payments and clauses are postponed for a duration calculated after the expiry of this period equal to the time elapsed between (i) March 12, 2020 or, if later, the date on which the obligation is born and (ii) the date on which it should have been performed.”</i></p> <ul style="list-style-type: none"> » Accordingly, if a tenant is in default of the payment of rent and charges, and if the owner decides to trigger the termination clause in the absence of an amicable agreement, the lease may not be terminated during the “protected period” (i.e., between March 12 and June 23, 2020, at midnight) and until the expiry of an additional postponement period starting on June 24, 2020 and determined as mentioned above¹⁶. » In addition, and insofar as a termination clause can be effective after the “protected period” for a breach occurring during such period, a judicial uncertainty remains on the success of an action before a court by the owner in obtaining the termination of the lease; the risk being that the judge of urgent matters (<i>juge des référés</i>), rather than imposing the ultimate sanction, will prefer, depending on the type of defaulting tenant, to grant the tenant a payment grace period and therefore a rescheduling of the unpaid rent and charges over the following installments.
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16 Examples:

Case 1 : Monthly rent is due on May 1, 2020. The tenant fails to pay such rent. An order to pay is notified to it on May 15, 2020. The tenant should benefit in principle of a grace period of 1 month to pay such rent (i.e., until June 15, 2020)

=>Postponement on the ground of Article 4 of the Ordinance: the outstanding obligation to pay is effective on May 1, during the protected period. The deadline of the order to pay is June 15 at the latest, during the protected period. The Ordinance will then apply. If the tenant does not pay its rent by June 15, it will benefit from a grace period corresponding to the time elapsed between (i) the date on which the obligation is born (May 1) and (ii) the date on which it should have been performed (June 15), i.e., a duration of one month and 15 days, starting on June 24.

Case 2 : Monthly rent is due on June 1, 2020. The tenant fails to pay such rent. An order to pay is notified to it on June 15, 2020. The tenant should benefit in principle of a grace period of 1 month to pay such rent (i.e., until July 15, 2020)

=>Postponement on the ground of Article 4 of the Ordinance: the obligation to pay is effective on June 1, during the protected period. The deadline of the order to pay is July 15 at the latest, after the protected period. No postponement mechanism will apply to such monetary obligation and the termination clause will be effective on July 15 if the tenant has not paid its rent by that time.

Case 3 : Quarterly rent (Q2 2020) is due on April 1, 2020. The tenant fails to pay such rent. An order to pay is notified to it on April 22, 2020. The tenant should benefit in principle of a grace period of 1 month to pay such rent (i.e., until May 22, 2020)

=>Postponement on the ground of Article 4 of the Ordinance: the obligation to pay is effective on April 1, during the protected period. The deadline of the order to pay is May 22 at the latest, during the protected period. The Ordinance will then apply. If the tenant does not pay its rent by May 22, it will benefit from a grace period corresponding to the time elapsed between (i) the date on which the obligation is born (April 1) and (ii) the date on which it should have been performed (May 22), i.e., a duration of one month and 22 days, starting on June 24.

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