

9 June 2020



Authors

COVID-19: Is there a right to a rent reduction?

Since the Federal Council ordered the closure of a large part of the shops in Switzerland in mid-March to counteract the spread of the COVID-19 virus, a dispute has raged between business tenants and landlords as to whether this extraordinary situation entitles business tenants to a rent reduction and, if so, to what extent. This article is intended to provide a summary of the questions in dispute.

1. Starting position

As ordered by the Federal Council on 16 March 2020, numerous businesses in Switzerland had to cease operations. Restaurants, hairdressing salons, fitness studios and clothing stores were particularly affected. The Federal Council relaxed its measures in 3 stages (27 April, 11 May and 8 June). Currently, all shops can open (in some cases with certain restrictions).

However, it cannot be ruled out that, depending on the course of the pandemic, a closure or restriction of shops will be re-ordered.

In the context of these officially ordered closures of the shops, the discussion flared up as to whether and, if so, to what extent a business tenant can demand a reduction in the rent he owes.

2. Intervention by the legislator

In order to settle the above-mentioned dispute and create legal certainty, the Swiss legislator decided to settle this controversy by law.

In the summer session, both the Council of States and the National Council adopted a compromise regarding the partial remission of commercial rents. The Federal Council is thus instructed to take the following legislative measures:

- Businesses that had to close down in accordance with Art. 6 para. 2 of COVID-19-Ordinance 2 (version of 19 March 2020) only owe their landlord 40 % of the rent for the period of closure ordered by the authorities.
- This regulation applies for a maximum of two months to businesses that had to reduce their operations in accordance with Art. 10a para. 2 of COVID-19-Regulation 2 (version of 19 March 2020).
- There is an upper limit of CHF 20,000 per month and per rental property.
- If the rent is between CHF 15,000 and CHF 20,000, both tenant and landlord have the option of waiving this rule (so-called opt-out clause).
- The Federal Council should provide for a hardship fund of CHF 20 million for landlords.
- Agreements already made between the rental parties remain valid.

For businesses which are not covered by this compromise, the question remains whether they can apply for a reduction in rent as a result of the closure ordered by the authorities and - if so - to what extent.



Peter Haas
Partner



Dr. Martin Rauber
Legal Director

3. Legal basis

According to Swiss tenancy law, the tenant can demand a rent reduction from the landlord if "the object is rendered unfit or less fit for its designated use". The claim shall arise from the time when the tenant becomes aware of the defect and shall end when the defect is remedied.

The question therefore arises whether the closure by the authorities as a result of the COVID-19 pandemic constitutes a defect within the meaning of tenancy law and whether this entitles the tenant to a rent reduction.

4. What is a defect in terms of Swiss tenancy law?

According to the Swiss Federal Supreme Court's case law, the demised property is defective if it is not (anymore) suitable for the intended use. This is primarily determined by the contractual purpose of the premises. A defect may exist where the property lacks a characteristic which is guaranteed under the contract or is required with regard to the contractual purpose, thus impairing its utility value. It is therefore a matter of comparison between the contractually owed condition and the actual condition of the premises.

It is irrelevant to the existence of a defect, whether the missing characteristic is tangible or intangible, if the characteristic has been agreed for suitability or for other reasons, or who or what has caused this contractual deviation. Rather, the existence of defect is assessed in a value-neutral manner based on the rental agreement.

Whether the demised property is (still) suitable for the implied, agreed or usual customary use is assessed according to objective criteria. The typical use has to be taken into account. For instance, the surroundings of a rental property can undergo various changes over the course of time, which have a more or less strong impact on the property. Such general changes (e.g. development of the neighboring land, increase in traffic etc.) - apart from extreme cases - cannot amount to a defect in the rented property.

5. Does the COVID-19-related closure of business premises qualify as a defect in terms of Swiss tenancy law?

There is lack of precedent in relation to the question whether COVID-19-related closures constitute a defect in terms of Swiss tenancy law. Depending on the interests involved, different opinions are suggested.

The Swiss Association of Business Tenants takes the view that no rent is due for the period of the closure ordered by the authorities. This association argues that the landlord is unable to fulfil his contractual obligation to provide usable premises for the contractually agreed purpose, such as the operation of a restaurant.

The Swiss Homeowners' Association argues the exact opposite. The demised property itself is, despite the ordered closure, still fully usable. Thus, the landlord fully meets his obligation to perform, which also means that the rent is still due unabated.

In fact, it seems debatable whether the rented property lacks a contractually guaranteed or required characteristic impairing its value due to the COVID-19-related closure. Although the property may no longer (temporarily) be used, it is still free of defects and is still available to the tenant. The nature and condition of the leased property remains unchanged. It is, therefore, controversial whether the landlord owes the business tenant commercial premises accessible to the public.

In addition, in the case of commercial property, the rental objects are often let in the shell of the building, meaning that the interior fittings are carried out by the business tenant himself. It is therefore up to the tenants to decide what kind of business operations they will set up and carry out within the premises provided by the landlord. The business tenant agrees with the landlord on the business use of premises, but not the actual business operations.

It can be assumed that, in future, court practice will show whether the officially ordered COVID-19 closure constitutes a defect in the demised property which may give rise to a claim to a reduction in rent.

6. Which contracting party bears the COVID-19 risk?

If the defectiveness of a rented property due to a COVID-19-related closure is affirmed, the question arises as to which contracting party must bear this risk.

There are no extraordinary situations comparable to the current COVID-19 pandemic in Swiss legal practice. The current situation is that, depending on the type of business, the business may not be operated or may only be operated to a limited extent. And this is due to a situation that is neither within the sphere of influence of the tenant nor within the landlord's.

There is at least some case law where certain immissions (for example construction or aircraft noise) affecting the use of a leased property were deemed to be beyond the control of the parties to the lease. In such cases, it is disputed whether the tenant is entitled to a rent reduction. According to one view, a claim exists because the defectiveness causes a disruption of the performance owed, which must be rebalanced. This is independent of whether the landlord would have an influence on the disruption and whether the defect can be repaired at all. On the other hand, a dismissal of the tenant's claim is justified precisely by the fact that the landlord has no influence on the disruption and thus has no possibility to remedy the defect.

As mentioned above, there is no legal practice as to what view a court would follow in a case-by-case situation. Nevertheless, it should be pointed out that several other rights of a tenant only come into play if the landlord does not remedy a defect reported to him within a reasonable period of time.

In principle, it is understandable that ordered operating restrictions or closures fall within the operating risk of the entrepreneur, i.e. the tenant. The same applies to the landlord: despite the COVID-19-related closure of entire business areas, the landlord is still obliged to fulfil his various payment obligations (e.g. mortgage interest, maintenance, heating, general electricity etc.).

It is therefore arguable that the COVID-19 closure would justify modifying the risk allocation under Swiss tenancy law. The landlord bears the risk of the usability of the rented property and the tenant bears the risk of its use - in particular the risk of making a profit with the rented property. The downturn in business, which has materialized in many business units due to the COVID-19-related closure, is thus generally considered to be one of the operator risks that should be borne by the business tenant. If the landlord were to be held liable for all malfunctions outside his sphere of influence, including those that he is unable to remedy, this would be tantamount to strict liability. Accordingly, the corresponding risk would have to be reflected in the rent; a risk surcharge - difficult to calculate in advance - would therefore have to be added.

7. Conclusion and recommendation

For businesses covered by the compromise proposal, the legal situation is clear. They are entitled to a rent waiver, provided that the opt-out clause is not applied and individual agreements have not already been made.

In addition, precisely because of the lack of precedent, it is currently impossible to estimate whether a court would see a defect in a COVID-19-related closure of a business operation and over which party to the contract it will place the burden of risk. Various scenarios are conceivable.

In view of this uncertainty, the parties to a commercial lease are well advised to talk to each other and find a practical solution. This can be a deferral or a partial reduction of the rent. Taking all opinions into account, it cannot be ruled out that a court will consider COVID-19 closures to be a defect and that a rent reduction will be granted. However, a complete reduction of the rent, as it is sometimes demanded, might not be realistic even in such a case.

In addition, landlords generally have no interest in a tenant going bankrupt, especially in the current situation, when the financial problems are not the fault of the tenant. Bankruptcy means that in any case no more rent payments will be due and that the premises will not be available for a long time. It is unlikely that it will be possible to find new tenants within a reasonable period of time. Tenants and landlords are business partners who are often bound together by long-term contracts. Accordingly, the problem should also be solved in partnership.

Your contacts for contract and tenancy law



Peter Haas
Partner

T: +41 31 328 75 75
peter.haas@eversheds-sutherland.ch



Oliver Beldi
Partner

T: +41 31 328 75 75
oliver.beldi@eversheds-sutherland.ch



Olivier Dunant
Partner

T: +41 22 818 45 00
olivier.dunant@eversheds-sutherland.ch



Marc Nufer
Partner

T: +41 31 328 75 75
marc.nufer@eversheds-sutherland.ch



Dr. Martin Rauber
Legal Director

T: +41 44 204 90 90
martin.rauber@eversheds-sutherland.ch

eversheds-sutherland.ch

The information contained in this document is intended for informational purposes only and cannot replace an appropriate legal advice. Eversheds Sutherland Ltd., with its legal domicile in Zurich (Switzerland), can take no responsibility for actions taken based on the information contained in this document.

© Eversheds Sutherland 2020. All rights reserved. Eversheds Sutherland is a global provider of legal services operating through various separate and distinct legal entities. Eversheds Sutherland is the name and brand under which the members of Eversheds Sutherland Limited (Eversheds Sutherland (International) LLP and Eversheds Sutherland (US) LLP) and their respective controlled, managed and affiliated firms and the members of Eversheds Sutherland (Europe) Limited (each an "Eversheds Sutherland Entity" and together the "Eversheds Sutherland Entities") provide legal or other services to clients around the world. Eversheds Sutherland Entities are constituted and regulated in accordance with relevant local regulatory and legal requirements and operate in accordance with their locally registered names. The use of the name Eversheds Sutherland is for description purposes only and does not imply that the Eversheds Sutherland Entities are in a partnership or are part of a global LLP. The responsibility for the provision of services to the client is defined in the terms of engagement between the instructed firm and the client. Eversheds Sutherland Ltd., with its legal domicile in Zurich (Switzerland), is a member firm of Eversheds Sutherland (Europe) Ltd.