First court decision on rent reductions during covid-19 lockdown

03.12.2021

Introduction

Due to the emergency regulations issued by the Federal Council to combat the covid-19 pandemic, numerous businesses had to close their premises. This led to questions about whether the tenants of such premises are entitled to rent reductions. In December 2020, the draft for the Covid-19 Business Rental Act failed in Parliament (for further details, please see Legal uncertainty over rent reductions due to covid- 19 remains and Federal act on rent reductions during covid-19 lockdown fails in Parliament).

The Zurich Rental Court recently decided the first case regarding rent reductions for commercial leases. (Zürcher Mietgerichtspraxis, decisions of the Special Court fortenancy matters and the Conciliation Authority of the Zurich District, issue 2021, 31st edition.) Previous court cases did not address in depth the issue of rent reduction in connection with the covid-19 regulations. (Commercial Court Zurich, HE210052-O from 16 April 2021, consid 3.3, p 5; Appellate Court Basel-City, ZB.2020.36 from 2 November 2020, consid 4.2 et seq regarding issue of timely assertion of rent reduction and offset of claims; and Cantonal Court Basel-Landschaft, 410 20 173 from 22 September 2020, regarding adjustment of alimony.)

Background

The entitlement to rent reductions following covid-19 measures is controversial. The Rental Court addressed the possible avenues for the assertion of such a rent reduction, namely a reduction of rent according to article 259d of the Swiss Code of Obligations (CO/ CO, SR 220.), subsequent to objective impossibility (article 119 of the CO) and judicial adjustment (clausula rebus sic stantibus).

Rent reduction under CO

If a leased property is defective or the tenant is prevented from using it as contractually agreed, the tenant may require the landlord to reduce the rent proportionately under article 259d of the CO. Therefore, the decisive question is whether the covid-19 measures result in a defect of the leased property or whether the tenant is prevented from making the contractually agreed use.

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Part of the doctrine considers the impaired use of the leased business premises not as a defect but as a business risk of the tenant. For another part of the doctrine, it is decisive whether the landlord participates in the risk due to explicit contract clauses on the type of business for which the premises will be used, and whether there is an obligation of the tenant to use the premises. In the case of such clauses, this part of the doctrine supports a rent reduction because the actual use of the premises for a specific purpose is part of the performance owed by the landlord.

Impossibility of performance

According to the Swiss Federal Supreme Court, subsequent objective impossibility to perform only applies if the event causing it is permanent or at least its end is not foreseeable.

Part of the doctrine allows for partial impossibility where either quantitative impossibility or temporary impossibility applies. In the first case, it is impossible to make full use of the leased property. In the latter case, the impossibility is not permanent, and the leased property is only unusable for a limited amount of time. In this context, the Supreme Court distinguishes between the impossibility to perform a contractual obligation and the mere impossibility to use the rental property where the use is not part of the contract.

Clausula rebus sic stantibus

According to the principle of pacta sunt servanda, contracts are to be complied with according to the agreed terms. The judicial adjustment applies only if – due to a change in the contractual relationship – the fulfilment of the contract is no longer reasonable for at least one party. The assumption hereby is that the parties would not have agreed to the contract if they had known of the change beforehand.

According to the Supreme Court, the principle applies if:

- an unavoidable change in the contractual relationship has been unforeseeable upon conclusion of the contract;
- such change results in a serious equivalence disorder between the parties; and
- the parties did not fulfil the contract unconditionally.

Facts

In the case at hand, the parties concluded a lease agreement in early 2013 for a ground-floor shop and a basement warehouse in Zurich. The tenant stopped the rent payments due to the impairment of use of the shop that the pandemic caused for the months of April and May 2020. Subsequently, the tenant paid only a third of the monthly rent until January 2021. For February 2021, no rent was paid.

Arguments of tenant

Due to covid-19 measures, the shop only allowed one customer at a time, which reduced customer traffic by one-seventh. According to the tenant, the parties had agreed upon the use of the property as a shop, not only in the contract but also according to known intentions of usage. The tenant argued that, due to the oficial order to close the shop and the later limitation of customers, the rental property had suffered a defect. Furthermore, the tenant claimed that the impairment of use was suitable to prove a serious equivalence disorder between performance and consideration, which was why the clausula rebus sic stantibus applied. The tenant stated that she had done everything possible to mitigate the situation. However, she had not disclosed her accounts due to confidentiality reasons.

Arguments of landlady

The landlady argued that the use of the premises as a shop had not been part of the contract, and the impairment of use could not be considered a defect. She denied the applicability of article 119 of the CO, as the impossibility to use the premises was not a permanent one. She also disputed the application of the clausula rebus sic stantibus because there had been no serious equivalence disorder that would justify the adjustment of the contract. Finally, the landlady argued that the tenant had not substantiated the claim of a serious change in sales.

Decision

The Zurich Rental Court considered the contractual reference to the rental property as a shop and warehouse solely a description, not an agreement on the specific use of the property as a shop and warehouse. It also held that the clause in the general terms and conditions on the use of the property for the contractual purpose did not constitute an agreement on a specific use. According to the Court, the parties would normally stipulate a specific use in the contract itself, not in the general terms and conditions. Furthermore, the Court denied the permanence regarding the impossibility to perform under the contract, as the end of the measures was foreseeable.

Additionally, the Court held that the leased property had not suffered a defect, since the contract contained neither an assurance regarding the operation of the shop from the landlady nor an obligation to use the premises as a shop.

Finally, the Court acknowledged that there had been a change in circumstances, which could have been the basis for a clausula rebus sic stantibus case. However, the tenant had not disclosed information on the impact of the covid-19 measures on sales. Therefore, the Court denied the presence of a serious equivalence disorder with reference to the sales possibilities offered by internet shopping.

Comment

The Court concluded that the requirements of a rent reduction had not been fulfilled, mainly because the tenant had not disclosed details on the financial impact of the covid-19 measures. The Court did not generally rule out the application of the clausula rebus sic stantibus.

Accordingly, the Court's conclusion cannot be generalised. Rather, each lease agreement and each situation must be analysed individually, taking into account the financial impact of the

covid-19 measures and whether a specific use was agreed upon.

This article has been published by Michael Lips (Partner) and Melanie von Rickenbach (Associate) on 3 December 2021 at International Law Office (ILO), London.

No legal or tax advice

This legal update provides a high-level overview and does not claim to be comprehensive. It does not represent legal or tax advice. If you have any questions relating to this legal update or would like to have advice concerning your particular circumstances, please get in touch with your contact at Pestalozzi Attorneys at Law Ltd. or one of the contact persons mentioned in this legal update.

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