

Legal uncertainty over rent reductions due to COVID-19 remains



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Real Estate, Switzerland

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Introduction

From 17 March 2020, numerous shops, restaurants and other facilities throughout Switzerland had to close their businesses due to emergency regulations issued by the Federal Council to combat COVID-19.**(1)**

This has led to the question of whether the tenants of such premises are still obliged to pay rent or whether they are entitled to a full or partial rent reduction.

While the Federal Council started to gradually lift the lockdown on 11 May 2020, and despite many opinions having been expressed in the legal community and by politicians, this question remains as unanswered as it was at the beginning of the lockdown.

Legal framework

Where a rented object is defective or a tenant is prevented from using a rented object as contractually agreed, the tenant may require that the landlord reduce the rent proportionately (Article 259a of the Code of Obligations).**(2)** Such reduction applies from the date on which the landlord learns of the defect until it is remedied (Article 259d of the Code of Obligations).

The right of rent reduction does not require that the defect or cause of the tenant's prevention from using the leased object can be eliminated by the landlord or that the landlord is at fault. Pursuant to settled case law, tenants may be entitled to a rent reduction if use of the rented premises is affected by a third party – for instance, if a neighbour's construction site prevents customers from accessing a shop or restaurant.

No relevant case law expressly addresses rent reductions where a tenant cannot conduct business in rented premises due to compulsory measures introduced to combat a pandemic or comparable event. Whether the Swiss authorities' closure of businesses due to COVID-19 constitutes a prevention in the use of a leased object in the sense of Article 259a of the Code of Obligations is thus subject to ongoing dispute.

If a tenant stops paying rent because it assumes that it is entitled to a rent reduction, it runs the risk of the landlord terminating the lease on short notice (after having set a 30-day payment deadline). Notably, during the COVID-19 lockdown, the Federal Council invoked emergency law to temporarily extend the 30-day payment deadline to 90 days.

(3) The extension applies only if a tenant defaults on rental payments that are due between 13 March 2020 and 31 May 2020 and if such default was caused by the governmental measures to combat COVID-19.

Even if not explicitly stated by the Swiss Federal Council, the above extension of the payment deadline has no impact on potential rent reductions. In particular, it provides no ground to claim that no right to a rent reduction exists and that only the postponement of rental payments should be considered. Such an extensive rule would require a clear legal basis.

Federal Council's input

From the start of the lockdown, the Federal Council has, without taking a stand, urged parties to rental agreements to find a solution by negotiation.

Moreover, a task force was set up to address the impact of COVID-19 on rental agreements and explore potential solutions to the question on rent reductions. So far, no substantial contribution from the task force has been reported.

Federal Parliament's efforts

In early May 2020, the Federal Parliament held an extraordinary session to address COVID-19-related topics, including the question of rent reductions for tenants affected by the lockdown.

While a majority of both the National Council and the Council of States agreed that a regulation on rent reductions is required, no agreement on how to resolve certain questions could be reached. Therefore, no regulation has been issued to date.

In particular, the two chambers disagreed on whether the proposed regulation should apply to all rental agreements or only to rental agreements which provide for a maximum monthly rent (eg, Sfr8,000). Moreover, the chambers disagreed on the level of reduction.

However, revised proposals are under discussion by the parliamentary commissions and the Federal Parliament is expected to address the question again in its next session.

Landlords' reactions

A handful of landlords – including private individuals, communities and institutional investors – have granted their tenants substantial rent reductions on a voluntary basis. This is remarkable, but has not inspired others to do the same, even though a distressed tenant could prove to be a bigger issue for a landlord than a temporary rent reduction.

What's next?

The Federal Parliament will likely implement an emergency federal act on the disputed rent reduction in the upcoming summer session. Such act will hopefully provide legal certainty on the following questions:

- To which rental agreements does the regulation apply?
- Is there an opt-out option for tenants?
- Does the regulation allow or require the circumstances of a particular case to be taken into account?
- Does a rent reduction depend on certain conditions?
- Is there any risk of abuse and how will this be mitigated?
- Will landlords receive any form of compensation for loss of rent?

Irrespective of the above, court proceedings are expected since the act is unlikely to clarify all areas of uncertainty. Further, it cannot be assumed that all rent reduction disputes will be settled. Hence, the courts will likely have the final say on this matter.

Comment

Against this background and in view of prospective regulations under preparation by the Federal Parliament, parties to lease agreements should be cautious when considering settlement proposals. This is because both landlords and tenants, being corporate bodies, may encounter liability risks if they hastily conclude settlement agreements which

later prove to have unfavourable terms or terms that do not appropriately reflect the specific circumstances of the individual case.

Should a tenant suffer from financial hardship due to the COVID-19 crisis and become bankrupt, the risk is that its creditors challenge the payment of full rent. The same applies to a bankrupt landlord, whose creditors could proceed against granted rent reductions through an action for annulment or claw-back action.

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Endnotes

(1) Ordinance on Measures to Combat the Coronavirus (COVID-19) (COVID-19 Ordinance 2), SR 818.101.24.

(2) SR 220.

(3) Ordinance on Mitigating the Effects of the Coronavirus Pandemic on Leases (COVID-19 Ordinance Leases), SR 221.213.4.

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