

### Effects of COVID-19 on Commercial Leases in Germany

by Marc Bohne, Peter Junghänel, Matthias Rüdert von Collenberg

The COVID-19 pandemic is causing massive disruption to landlords and tenants of commercially used spaces. Many tenants are affected by reduced customer frequency, supply bottlenecks or staff illnesses. Also, the German federal states' legal regulations on infection protection, which restrict or prohibit the opening of many shops and restaurants (and, in the future, possibly offices), often cause massive losses for tenants. Against this backdrop, the question inevitably arises: what will be COVID-19's effects on commercial lease agreements? This alert provides an initial overview of the potential effects, and assumes that such commercial lease agreements contain no mention of the impairments that are now occurring.

#### THE CONSEQUENCES OF THE PANDEMIC AS A DEFICIENCY OF THE RENTAL OBJECT?

If the consequences of the COVID-19 pandemic were to constitute a deficiency of the rental object, the tenants could potentially reduce rents, or, in extreme cases, even terminate their lease extraordinarily. When considering this, however, a distinction must be made in separate circumstances.

Cases in which the landlord is no longer able to provide the tenant with contractually owed services (apart from the provision of the rental object itself) are relatively clear. If, for example, the landlord owes the option of co-using a canteen under the lease agreement and can no longer maintain the operation of the canteen, this is likely to constitute a deficiency of the rental object (unless otherwise contractually agreed), which entitles the tenant to a reasonable rent reduction.

However, the question of whether reduced customer frequency in the course of the COVID-19 pandemic or restrictions imposed on tenants due to legal regulations issued in response to the pandemic could lead to a deficiency in the rented property appears to be of much greater significance at present.

The reduced customer frequency alone typically would not lead to a deficiency of the leased object, because the risk of use, including the risk of generating a profit with the leased object, is generally borne by the tenant in the case of commercial leases.

More difficult to assess is the question of whether there is a deficiency of the leased object if the tenant is no longer allowed to operate its business at all or only with limited operating hours due to new legal regulations. According to established case law of the German Federal Court of Justice, legislative measures can only lead to a deficiency in rented property if the restriction of use is directly related to the specific nature, condition or location of the rented property. It is precisely this, however, that is likely lacking in the legal regulations issued in response to the COVID-19 pandemic. If the Federal Court of Justice consistently adheres to the above-mentioned case law, the restrictions imposed by the ordinances issued during the COVID-19 pandemic are therefore unlikely to constitute a deficiency of the rental object.

#### DEFAULT OF THE TENANT - DESPITE A FORCE MAJEURE CRISIS

If a tenant wrongfully does not pay rent in full when due, it is in default. Yet, what may seem obvious is not necessarily self-evident in times of COVID-19: Since default requires fault under German law, a tenant could argue that fault does not exist in case of *force majeure*. In principle, it cannot be dismissed that the COVID-19 crisis in other contractual relationships constitutes cases of *force majeure*, especially in connection with collapsing supply chains. With regard to the obligation to pay rent, however, this argument is generally unlikely

to be effective, as it is a simple obligation to pay in cash. According to the German Civil Code, a creditor cannot argue that it does not have cash. Of course, rental agreements may contain specific provisions on *force majeure*, but in German practice this is usually not the case.

## **RIGHTS OF THE TENANT UNDER THE ASPECT OF DISTURBANCE OF THE BASIS OF THE BUSINESS**

In individual cases, however, even if there is no deficiency in the rental object, tenants may demand an adjustment of the rental agreement under the principle of "disruption of the business basis" (*Störung der Geschäftsgrundlage*) or, if an adjustment is not possible or cannot reasonably be expected of a contractual partner, a termination of the rental agreement. The legal institution of disruption of the business basis takes into account, as a consequence of the principle of good faith, circumstances which have become the basis of the contract but which have changed seriously after the conclusion of the contract.

Also, in tenant claims focused on disruption of the business basis, contractual and statutory distribution of risk must be considered. Since the tenant generally bears the risk of use under commercial leases, claims based on the disruption of the business basis of the transaction would also be excluded.

However, the German Federal Court of Justice has emphasized that in exceptional cases, in which an unforeseen development with potentially existential consequences for one party occurs, the contractual and statutory distribution of risk with regard to a possible disruption of the basis of the business could be disregarded as an exception. Although we are currently inclined to deny that there is a disruption of the basis of business due to the temporary restrictions on business, this assessment may change in the wake of the COVID-19 pandemic – especially considering that courts will retrospectively consider any possible disruption of the current crisis. Against this background, we do not rule out the possibility that the institution of disruption of the business basis may become a gateway for possible rights and claims of tenants.

## **OUTLOOK**

The consequences of the COVID-19 pandemic still cannot be conclusively assessed. It should be clear, however, that the massive loss of revenue and restrictions on tenants will lead to a multitude of disputes between landlords and tenants.

Goodwin [real estate lawyers](#) can help clients navigate the economic and legal uncertainty affecting commercial lease agreements.

Please contact us to review or continue the discussion.

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Please visit Goodwin's [Coronavirus Knowledge Center](#), where firm lawyers from across the globe are issuing new guidance and insights to help clients fully understand and assess the ramifications of COVID-19 and navigate the potential effects of the outbreak on their businesses.

## CONTACTS:

**Marc Bohne**

Partner

+49 (0)69 6677 38511

mbohne@goodwinlaw.com

**Peter Junghänel**

Partner

+49 (0)69 6677 38533

pjunghanel@goodwinlaw.com

**Matthias Rüdt von Collenberg**

Associate

+49 (0)69 6677 38606

mcollenberg@goodwinlaw.com

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