

DISPUTES

COVID-19 and the resultant impact on rental payments: a practical analysis

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Introduction

The economic effects of the government-imposed lockdown (“**Lockdown**”) in order to contain and curb the spread of the Covid-19 pandemic have been widespread across all sectors of business in South Africa, including the retail property sector.

In terms of the regulations issued by the Minister of Cooperative Governance and Traditional Affairs on 25 March 2020, as amended (“**Lockdown Regulations**”), for the duration of the Lockdown (being, as at the date of publication of this article, from 27 March 2020 up to and including 30 April 2020), all business and other entities are obliged to cease operations, except for any business or entity involved in the manufacturing, supply, or provision of an essential good or service, save where operations are provided from outside of South Africa or can be provided remotely by a person from their normal place of residence.

One of the effects of the restrictions imposed by the Lockdown Regulations is that the majority of retail shops across the country are closed, with tenants receiving little to no income. As a result, some retail tenants have indicated to landlords that they will not be paying their rentals for the duration of the Lockdown. The non-payment of rental should be carefully weighed-up, as it constitutes non-performance on the part of the tenant to comply with its contractual obligations in terms of the lease agreement concluded with the landlord. This article explores the circumstances in which such non-performance may be permitted.

Although certain relief measures have been put in place, as discussed below, at present, none of these measures oblige landlords to suspend rental payments or to grant a remission of rental during the Lockdown Period. Accordingly, the starting point for both a tenant and a landlord should be the terms of their lease agreement.

The lease agreement

It has become standard practice for retail and commercial lease agreements to contain provisions dealing with an event of *force majeure* – being an unforeseeable event or circumstance which prevents a party from fulfilling its obligations under a contract. These clauses are often highly negotiated between the parties, and the manner in which an ‘event of *force majeure*’ has been defined in the particular lease agreement must be closely examined in order to assess whether a pandemic, such as Covid-19, meets the requirements. If this leg of the test is met, then in order for any non-performance by either party to be justified, the requirements set out for claiming an event of *force majeure* must be observed (for example, observing the requisite notice periods). However, we stress the importance of examining the definition of an ‘event of *force majeure*’ closely, as it may be the case that while a pandemic is encompassed by such definition, it may not excuse payment while the event of *force majeure* is continuing. As a result, any non-payment by the tenant will result in a breach under the lease agreement. In addition, a lease may also contain a term requiring the tenant to pay rental and other amounts due to the landlord in advance, without deduction or set-off. In these circumstances, the tenant will be required to pay such amounts monthly in advance (regardless of any right it may have to claim a remission of rental) and, thereafter, claim any such remitted rental from the landlord.

Another example of a clause which is often found in retail and commercial lease agreements, particularly where the tenant is a large retailer, is a ‘minimum occupancy’ clause. In these clauses, the landlord undertakes that, at all times, the relevant shopping centre will have a

minimum occupancy (often set out as a percentage), including occupancy by certain large retailers. A failure to meet this undertaking may entitle the tenant to cancel its lease agreement, depending on the terms of the clause. However, since cancellation is a drastic measure, the existence of such a clause may provide a tenant with significant leverage to negotiate with the landlord either a rental payment suspension or a rental remission for the duration of the Lockdown Period. Even if a rental suspension or remission is agreed, tenants should be aware that, in all likelihood, they will be obliged to continue paying operating costs, such as the rates, taxes and utilities associated with the leased premises and the common areas.

Insofar as there are any penalty stipulations in the lease agreement which may relate to non-performance, then the relevant legislation dealing with penalties will apply which, among other things, obliges a court to investigate the quantum of the penalty versus the prejudice suffered, and permits a court to reduce the penalty amount if it is out of proportion to the prejudice suffered. In addition, if a landlord claims under a penalty stipulation, then it is precluded from claiming damages for the same act/omission which gave rise to the penalty claim.

Common law principles

Where a lease agreement is silent as to the consequences of an event of *force majeure*, however, then either party may rely on the applicable South African common law principles. The principle set out by the common law doctrine of 'supervening impossibility of performance' is that each party's obligation to perform in terms of an agreement, and their respective rights to receive performance under that agreement, will be extinguished in the event that the performance by a party of its obligation becomes objectively impossible as a result of unforeseeable and unavoidable events – *vis maior* ("major force") or *casus fortuitous* ("accidental occurrence") – which are not the fault of any party to that agreement. Although absolute factual impossibility is not required, performance of an obligation will not be objectively impossible if that performance has merely become more onerous, difficult or costly.

Supervening impossibility of performance can occur due to *vis maior* or *casus fortuitous*. These concepts have been described as events emanating from "nature", or from man, which are irresistible and outside the control of the ordinary person, and may be unforeseen or unforeseeable. They include acts of State. *Casus fortuitous*, it has been said, "*is a species of vis maior, and imports something exceptional, extraordinary or unforeseen, and which human foresight cannot be expected to anticipate or which, if it can be foreseen, cannot be avoided by the exercise of reasonable care or caution*". Accordingly, there is a strong argument to be made that Covid-19 falls into the category of *casus fortuitous*.

Another common law principle which may be applicable is that relating to beneficial occupation. If a tenant is prevented, as a result of *vis maior*, from making beneficial use of the leased premises ("*commodus usus*") then the tenant is excused from paying rent (either wholly or partially), provided that the tenant's loss of beneficial occupation is a direct and immediate result of the *vis maior*, and not merely indirectly or remotely connected with it. We draw a distinction here between retail tenants who do not provide essential goods and services, and those who do. In respect of the latter, these retail tenants are permitted in terms of the Lockdown Regulations to continue trading throughout the Lockdown. Even if such 'essential' retail tenants were to argue that they have suffered a decrease in earnings, this is an indirect result of the Lockdown Regulations, as they continue to enjoy beneficial occupation of their leased premise and are able to continue trading. Accordingly, we do not think that any claims for a remission in rental by such 'essential' tenants would be successful.

As mentioned above, it is only in the absence of a *force majeure* clause in the relevant lease agreement that the common law position will apply. The common law principles are all contingent on whether a landlord and a tenant have agreed in their lease agreement to alter the common law consequences of both *vis maior* and supervening impossibility of performance. In considering whether the parties to a lease agreement have sought to alter these common principles, a Court will scrutinise the terms of the lease agreement carefully, because it is not presumed that the parties intended to alter the common law.

Relief measures

Certain relief measures have been already been implemented by the government, in an attempt to alleviate the economic impact of the Lockdown. This includes a competition law exemption, in terms of which agreements relating to (i) rental payment suspensions and/or rental discounts; (ii) limitations on the eviction of tenants; and (iii) the suspension of or adjustment to lease agreement clauses which restrict such tenants from undertaking reasonable measures to protect their viability during the Lockdown, between designated retail tenants and retail property landlords, are exempt from the prohibition against certain restrictive horizontal and restrictive vertical practices. The relevant tenants are those in the clothing industry, the footwear and home textile industry, the personal care service industry and the restaurant industry. However, the exemption does not mean that rental landlords are obliged to grant any relief to the relevant category of retail

tenants, but rather that such tenants and landlords are free to negotiate the aforementioned category of agreements without breaching the competition laws of South Africa (and provided that they adhere to the terms of such exemption).

Another initiative which has been put forward is by a newly-constituted body, the Property Industry Group, which comprises the South African Real Estate Investment Trust Association, the South African Property Owners' Association and the South African Council of Shopping Centres. The purpose of the initiative is to provide guidelines to landlords, which are members of the bodies comprising the Property Industry Group, for nationwide assistance, in the form of a proposed relief package, for retail tenants and which are hardest hit by the Lockdown. The relief package aims to primarily support SMMEs and as a qualifying factor, among other things, tenants who were in good standing as at 29 February 2020 will not be evicted for the next two months and must undertake to not retrench staff during the relief period. However, at this stage, the relief package is still in the form of a proposal, and landlords and tenants should take note of any official reprieve which may be announced in this regard, whether during or after the Lockdown and whether pursuant to amendment of the Lockdown Regulations or otherwise.

Conclusion

Any failure by a tenant to comply with its rental payment obligations under a lease agreement, which failure is not justified in terms of either the agreement itself or at law, will be regarded as a breach by the tenant. Accordingly, in order to assess whether or not a tenant may legitimately suspend its rental payment and/or claim a remission in rental as a result of the Lockdown, we recommend that, in each particular case, the relevant facts and remedies should be considered, namely the terms of the lease agreement, the applicability of any common law principles and the imposition of any official relief measures. Regard must also be had to the Lockdown Regulations, which are amended on an almost-daily basis, as the government considers new ways to alleviate the impact of Covid-19 on the economy.



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