

## **CORONAVIRUS: IMPACT OF OPERATIONAL RESTRICTIONS ON COMMERCIAL AND RESIDENTIAL LEASES IN THE CZECH REPUBLIC**

Due to SARS CoV-2 coronavirus, the operation of retail shopping facilities in the Czech Republic is affected by operational restrictions imposed by the public authorities from 12 March 2020 to protect public health and safety. As a result, new acts prohibiting the termination of leases due to non-payment of the rent (provided it is caused by restrictions imposed by the public authorities in relation to the SARS CoV-2 coronavirus pandemic) have been adopted.

### **ANALYSIS OF THE OPERATIONAL RESTRICTIONS AND THEIR IMPACT ON OBLIGATION TO PAY THE RENT**

#### **Operational restrictions**

Presently, landlords are not obliged to close entire buildings. However, certain extraordinary measures have been adopted, including closure of restaurants and pubs (with only take-away services being retained) and closure of all retail shopping facilities with the exception of certain stores (e.g. stores selling food, groceries, pharmaceutical products or medicines). The restrictions above have been imposed on the operators of these facilities (i.e. tenants if the relevant facility is located in the leased premises). The Czech Government declared that the list of exceptions will be extended weekly as the pandemic situation is expected to improve.

The restrictions referred to above were in place from 12 March 2020 to 23 March 2020 under the Czech Government crises measures issued pursuant to the Crisis Act and from 24 March 2020 under the Czech Ministry of Health extraordinary measures. However, the relevant Czech Ministry of Health extraordinary measures have been revoked by a decision of the Municipal Court in Prague dated 23 April 2020 (file no. 14 A 41/2020) due to non-compliance with the law. As a reaction to that, the Czech Government issued on 23 April 2020 resolution no. 454 under which the restrictions referred to above were in place for a period from 24 April 2020 to 27 April 2020 and resolution no. 453 under which the restrictions will be in place from 27 April 2020 onwards pursuant to the Crisis Act. Currently, the restrictions for various retail operations are gradually lifted, depending on the type and size of the retail operation.

#### **Tenants' obligation to pay rent under the Lease Agreements**

We are of the view that the current operational restriction of some retail shopping facilities is a legal requirement on tenants' side. Tenants forced to close their business are relieved from the performance of their respective contractual obligations (e.g. obligation to keep their business open during opening hours) and landlords are not entitled to the related damages and contractual penalties as closures of the premises are direct result of the legal requirement.

Given that landlords are still able to perform all of their obligations under the lease agreements as the building operation remains unaffected (i.e. tenants are still able to access the leased premises, store goods in there and landlord still provides services under the lease agreement), we are of the view that tenants are not released from their obligation to

pay rent and/or service charges (unless the lease agreement provides otherwise), despite being effectively prevented from using the leased premises.

## **Potential claims against the Czech Republic for compensation of loss**

Section 36 (1) of the Crisis Act stipulates that the state has an obligation to compensate loss caused to natural and legal persons as a result of crisis measures carried out under the Crisis Act. Therefore, tenants and landlords may be entitled to claim damages from the state for loss caused by the restrictions imposed in respect to the SARS CoV-2 coronavirus crisis under the Crisis Act. In order to establish a claim for compensation under the Crisis Act, there must be a causal link between the state's crisis measure and the suffered loss. The amount of compensation is not limited by the Crisis Act, but the claim must be submitted within six months from ascertaining (realizing) the loss (subjective limit) and maximum within five years from the occurrence of the loss (objective limit).

However, given the vast amounts of compensation that the state would be obliged to pay to all the persons affected by the same, we would be reluctant to conclude that the provisions of the Crisis Act will, in practice, be applied in their full extent. It is not entirely clear whether the compensation under the Crisis Act might be claimed with respect to the loss caused by the Czech Ministry of Health extraordinary measures as they have not been issued pursuant to the Crisis Act. Given the fact that certain Czech Ministry of Health extraordinary measures were revoked by the Municipal Court in Prague due to non-compliance with the law, another option to claim compensation would be a compensation claim pursuant the Act no. 82/1998 Coll. (Act on liability for the loss caused by public authorities) due to incorrect administrative procedure applied by the Czech Ministry of Health.

## **ANALYSIS OF THE GOVERNMENTAL ACTS RESTRICTING TERMINATION OF LEASES**

### **Commercial leases**

The Commercial Leases Covid Act aims to support tenants affected by the current restrictions imposed by the public authorities. Please find below summary of the main aspects of the Commercial Leases Covid Act including our critical analysis.

- Section 3 (1) of the Commercial Leases Covid Act stipulates that the landlord is prohibited from unilateral termination of the lease due the tenant's default with payment of the rent related to the lease, provided such default (i) occurs during period from 12 March 2020 to 30 June 2020 (the "relevant period") and (ii) is caused by the SARS CoV-2 coronavirus related restrictions imposed by the public authorities preventing or substantially hindering business activity of the tenant. The prohibition protects tenants until end of the "protection period" (i.e. period from date of effectiveness of the act till 31 December 2020). Please note that the Commercial Leases Covid Act contains wrong reference in the definition of restrictions imposed by the Czech Ministry of Health extraordinary measures. By a strict interpretation it could be concluded that the operational restrictions imposed by the Czech Ministry of Health extraordinary measures do not fall within the scope of the Commercial Leases Covid Act and tenants affected by these restrictions cannot seek protection under the Commercial Leases Covid Act. However, the explanatory note to the Commercial Leases Covid Act indicates that the reference is legislative error. Therefore, the courts might interpret this provision extensively in order that its interpretation would correspond to the purpose of the Commercial Leases Covid Act – protection of tenants affected by restrictions.
- The tenant is obliged to provide the landlord with documents evidencing a causal link between the payment default and the SARS CoV-2 coronavirus related restrictions within fifteen (15) days from the first day of the delay with the rent payment. However, should the tenant fail to fulfil this obligation, the Commercial Leases Covid Act does not explicitly provide any sanction. Therefore, we are of the view that even if the evidencing documents are not provided to the landlord within the period above, the tenant would benefit from the termination moratorium, should these documents be delivered to the landlord by the time the landlord would be otherwise able to (i) terminate the lease (under the lease agreement or general law) and (ii) effectively issue the termination notice to the tenant.
- The Government declared that the Commercial Leases Covid Act entitles tenants to postpone payment of the rent until June 2020. However, the wording of the Commercial Leases Covid Act does not really entitle the tenant to such

postponement as it only stipulates that non-payment of the rent cannot be the termination reason (subject to conditions thereto). Further, Section 3 (2) of the Commercial Leases Covid Act explicitly states that the landlord is entitled to terminate the lease due to other reasons (i.e. other than default with payment of the rent or services) and it may also execute other rights in connection the tenant's payment default. By strict interpretation of this provision, it could be concluded that landlords are still entitled to execute their contractual or statutory rights, including right to demand payment of contractual penalties and/or default interest if the payments are not made when due. Should the tenant's payment obligation be secured by a deposit or bank guarantee, the landlord would also be entitled to retain the deposit, draw on the bank guarantee or even claim payment of the rent from a parent company of the tenant under a corporate guarantee (if available).

Therefore, landlords might be still entitled to terminate the lease due to the failure to pay relevant contractual penalties or replenish the deposit/issue new bank guarantee (if the respective lease agreement provides for such termination). It shall be though noted that exercising of the right to terminate the lease may be (i) moderated by the court if misused by the landlords or (ii) deemed to contradict the purpose of the Commercial Leases Covid Act (i.e. protection of tenants affected by the SARS CoV-2 coronavirus related restrictions). The courts might also take into account that the explanatory report to the Commercial Leases Covid Act prepared by the Czech Government notes that the protection should apply also to the secondary obligations of the tenants, i.e. prohibiting the landlords from termination of the lease due to delay in performance of obligations which arose as a result of the rent payment delay.

- Furthermore, Section 3 (4) of the Commercial Leases Covid Act stipulates that "all debts which became due during the relevant period (not paid by the tenant) must be paid until the end of the protection period." This sentence has been incorporated into the Commercial Leases Covid Act based on Ms. Kovářová's amendment proposal no. 4727. The explanatory report to this amendment proposal implies that the term "debts" means rent debt and not all debts of the tenant. Although we are of the view that this provision does not postpone maturity of the rent until the end of the protection period, this provision can be interpreted in a way that it effectively prevents landlords from enforcing payment of the rent (due in the period between 12 March 2020 and 30 June 2020) prior to the end of the protection period (i.e. before 31 December 2020). This section also entitles landlords to terminate the lease with 5 days' notice period, provided the tenant fails to pay the rent arrears incurred during the relevant period at the latest on 31 December 2020.
- Section 4 of the Commercial Leases Covid Act also provides a new termination reason in favour of landlords. The landlord would be entitled to demand termination of the lease, provided that it could not be reasonably required to bear effects of the measures under the Commercial Leases Covid Act. However, such wording is very general and it might be subject to disputes. Also, it is unclear what the words "demand termination" means as it is different from simple entitlement to terminate.
- Lastly, we are of the view that the Commercial Leases Covid Act should affect mostly retail leases as most of the office or industrial/logistics operators are not directly affected by the governmental restrictions. However, the conditions of application of the Commercial Leases Covid Act are open for interpretation and the courts might apply the Commercial Leases Covid Act extensively (i.e. also to office or industrial/logistics operators whose business is even indirectly affected by the governmental restrictions). Such extensive interpretation could prevail, for example, in the cases of retail store businesses the operation of which was prohibited by the restrictions and who are now unable to pay the rent in the logistics or office premises as a result of the restrictions.

## **Residential Leases**

The Residential Leases Covid Act aims to support tenants of the residential premises affected by the current restrictions imposed by the public authorities. Both Acts have a similar structure and wording as they were prepared simultaneously. The main difference is that relevant period under the Residential Leases Covid Act is longer (from 12 March 2020 till 31 July 2020). The Residential Leases Covid Act also explicitly provides that the tenant must without undue delay provide the landlord with the confirmation issued by the Czech Employment Office when evidencing a causal link between the payment default and the SARS CoV-2 coronavirus related restrictions. Lastly, the Residential Leases Covid Act entitles landlords to terminate the lease without notice period, provided the tenant fails to pay the rent arrears incurred during the relevant period at the latest on 31 December 2020.

## **DEFINITIONS**

### **"Commercial Leases Covid Act"**

Act no. 210/2020 Coll., Act on measures mitigating the effects of the SARS CoV-2 coronavirus epidemic on tenants of the commercial premises;

### **"Crisis Act"**

Czech Act no. 240/2000 Coll., the Crisis Act, as amended; and

### **"Residential Leases Covid Act"**

Act no. 209/2020 Coll., Act on measures mitigating the effects of the SARS CoV-2 coronavirus epidemic on tenants of the residential premises.

## **IMPORTANT TO NOTE**

In preparation of this Memorandum we have relied solely on the wording of the Commercial Leases Covid Act and of the Residential Leases Covid Act and related explanatory reports (in Czech: důvodové zprávy) prepared for the Acts and the proposed amendments. Due to the lack of applicable court precedents and other interpretation tools that would give guidelines for interpretation, this Memorandum represents solely a professional opinion of Clifford Chance Prague LLP, which can be used in particular for information purposes. It is possible that the relevant courts may have different opinions on the legal interpretation of the above issues.

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