

# The impact of COVID-19 on lease agreements in Germany – practical considerations

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Authors: [Sandra D'Ascenzo](#), [Rostyslav Telyatnykov](#), [Andreas van den Eikel](#), [Holger Wolf](#)

COVID-19 is currently affecting all areas of (economic) life. Many businesses are being forced to reduce costs due to a decrease or a loss of turnover and may not be able to pay their rents any longer. For both landlords and tenants, the question arises about the impact of the COVID-19 pandemic on their lease relationships. Does the contract need to be adapted to the current situation? Is there a claim to reduce or defer the rental payment obligation? Can the contract be terminated due to a delayed payment under these circumstances? What else is there to consider?

## Forecast – practical recommendations

- Tenants are not entitled to suspend or reduce the payment of the rent due to collapsing turnovers or official operating prohibitions. The landlord can be entitled to a right of termination if the tenant is in default with the payment of rent. In the event of such early termination, the tenant is obliged to pay damages to the landlord, the amount of which depends on a subsequent letting.
- However, also landlords should often have an interest in their tenants surviving the crisis. It may therefore be recommendable to enter into negotiations on possible (temporary) adjustments to the lease at an early stage. On the other hand, it should not be ignored that also landlords have to fulfil their obligations towards banks and their contractual partners and are dependent on the rental income for this purpose.
- The legislator is planning extensive regulations for the protection of tenants as part of a "Coronavirus emergency package". Under these regulations, landlords will not be allowed to terminate the contracts with tenants who are unable to pay the whole or part of their rent in the period from 1 April 2020 to 30 June 2020 due to the impact of COVID-19. Comparable provisions shall also apply to consumer loan agreements concluded before 15 March 2020. For loan agreements which are not consumer agreements, no regulations are planned.
- Arrangements between the parties which go beyond the package of measures will therefore be necessary in order to adapt the lease relationship to the current circumstances, e.g. if applicable, the suspension of contractual operating obligations, if there is no official operating prohibition, or a (temporary) reduction of the rent, since a deferral of payment leads to the building up of liabilities by tenants which they may not be able to cover.
- If adjustments to the lease agreement are agreed, these must be documented by means of amendments to the lease agreements complying with the written form requirements. Especially now, tenants might tend

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to try to dissolve the lease due to a breach of the written form requirements, which leads to an early terminability of the lease.

- The wording of the amendment is of greater importance. Firstly, a reference should be made to the current situation with regard to the adjustment, in order to exclude further claims by the tenant based on the disruption or the loss of the basis of the transaction. Secondly, the regulation to be made must also take into account the insolvency law situation and the risk of challenges under insolvency law.

## Legal considerations

- For lease agreements also in times of a crisis, "pacta sunt servanda" generally applies. This means that the landlord must continue to make the leased property available for use and the tenant must in general pay the rent without any reductions.
- The tenant is only entitled to reduce the rent if the rental use is significantly disturbed due to a defect of the leased property. This requires, however, that the circumstance constituting the defect relates to the leased property, i.e. its condition or location (e.g. in case of a lock-out by the landlord) and not, as in most current cases, to the fact that the tenant cannot continue its business as usual.
- A claim of the tenant for adjustment of the lease agreement, in particular for reduction of the rent, is therefore only possible by applying the principle of disruption or the loss of the basis of the transaction. The German Civil Code (BGB) contains a regulation (§ 313 BGB), which limits in extreme exceptional cases the general principle that contracts must be complied with.
- According to the consistent case law, the principle of disruption or loss of the basis of the transaction is not applicable if the realised risk was contractually assigned to one of the parties, as it is generally the case in many commercial leases: the landlord bears the risk of making the leased property available for undisturbed use and the tenant bears the risk of being able to run its business undisturbed in all other respects.
- It is questionable whether the current situation deviates from the contractually agreed risk allocation in such a way that the parties would have concluded deviating provisions if they had foreseen the COVID-19 pandemic. This depends on the individual case. However, in most cases, this will probably not be the case.
- The allocation of risk is no longer relevant in the event of force majeure (war, natural disasters, epidemics). The current situation, which involves business closures and curfews, is likely to be a critical case. However, it cannot be excluded that force majeure can be assumed at least if the situation continues to deteriorate.
- Furthermore, if it is assumed that force majeure is given or that the parties would have included deviating provisions into the agreement, it has to be assessed whether it is still reasonable for the tenant to adhere to the unchanged contract or whether, according to the case law of the Federal Court of Justice (*Bundesgerichtshof*) "adherence to the contract leads to intolerable results that are not in line with the law and justice". It remains to be seen whether and to what extent the planned legal measures of the government to protect the tenants will play a role in the assessment of the question of the basis of the transaction.
- If the requirements of the statutory regulation on the disruption or the loss of the basis of the transaction are fulfilled, the primary legal consequence is the adaptation of the contract to the changed circumstances. However, the adjustment does not occur automatically. Rather, the disadvantaged party has a right to the participation of the other party in the modification of the contract. The adjustment of the contract depends on the individual case and ranges from a deferral or reduction of the rent to a temporary suspension of the rental obligations with an extension of the lease term up to a waiver of rent. Only in such cases, in which it is also not reasonable for the tenant to adhere to the adapted contract, a termination of the lease agreement could be considered.

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White & Case LLP  
John F. Kennedy-Haus  
Rahel Hirsch-Straße 10  
10557 Berlin  
Germany  
**T** +49 30 880911 0

White & Case LLP  
Graf-Adolf-Platz 15  
40213 Düsseldorf  
Germany  
**T** +49 211 49195 0

White & Case LLP  
Bockenheimer Landstrasse 20  
60323 Frankfurt/Main  
Germany  
**T** +49 69 29994 0

White & Case LLP  
Valentinskamp 70/EMPORIO  
20355 Hamburg  
Germany  
**T+49 40 35005 0**

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