

## Covid-19: Impact of the Coronavirus Outbreak on Lease Agreements

### Introduction

Covid-19 Coronavirus (**Covid-19**) outbreak, which showed up in the city of Wuhan in China at the end of 2019 and led to deaths of a high number of people, has been characterized as pandemic and a threat to all the countries by the World Health Organization on 11 March 2020.

In addition to severe consequences of the Covid-19 on human health, it can be said that the Covid-19 has also material impacts on commercial and economic aspects so far and will give rise to additional consequences in the near future. Accordingly, legislative changes bearing the nature of precaution against the Covid-19 have recently been made in relation to lease agreements, following the other precautions taken by the Turkish law-maker and regulatory authorities. This information note will discuss legal issues related to the impacts of the Covid-19 on workplace lease agreements, those executed within the scope of commercial activities in particular.

### Shall Covid-19 constitute a force majeure event or any other event of impossibility of performance in relation to lease agreements?

First of all, it should be noted that force majeure is not explicitly regulated under the Turkish legislation but can be defined under the precedents of the Turkish Court of Cassation (*Yargıtay*) as extraordinary events which (i) are not arising from a debtor's fault, (ii) occur beyond the activities and the businesses of such debtor, (iii) cannot be foreseen/prevented and (iv) may restrain the debtor from fulfilling its contractual liabilities.<sup>1</sup>

Article 136 of the Turkish Code of Obligation (Law No. 6098) (**Turkish Code of Obligations**) regulates the impossibility of performance and sets out that any debt which becomes impossible to perform due to reasons not attributable to the debtor itself shall cease to exist. Thus, extraordinary outbreaks which are not of debtor's fault, occurring beyond the activities and the businesses of debtor, unforeseeable and not preventable and which may restrain the debtor from performing his obligations may constitute force majeure events as per the provisions of the Turkish Code of Obligations and the precedents of the Turkish Court of Cassation.

As a general rule under the Turkish Code of Obligations, lease agreements can be validly executed without being subject to any form requirements and parties may freely agree upon the content of such agreements in accordance with the freedom of contract principle to the extent permitted by the applicable laws. In this regard, the provisions of any lease agreement should be reviewed with a particular focus on force majeure clause (if any) thereunder in order to determine whether the Covid-19 constitutes a force majeure event under the respective agreement or not. As regards to lease agreements where pandemic/contagious outbreaks are explicitly listed as force majeure events, the Covid-19 would constitute a force majeure event under such agreements for the purpose of the performance of obligations arising therefrom and the legal consequences associated with such event will be applied. That being said, when it comes to lease agreements where a force majeure clause has been inserted but pandemic/contagious outbreaks are not explicitly designated as such, the respective force majeure clause should be interpreted. In particular, lease agreements where no broad provision extending the scope of force majeure events is set forth, the circumstances of the concrete case as well as the impacts of the Covid-19 on obligations arising from the underlying lease agreements should be taken into consideration for the purpose of such interpretation.

It should, however, be noted as a general rule that monetary obligations may not become impossible to be performed as obligations of a category (of goods) cannot become impossible in principle. Additionally, with a view to examining if any event other than the force majeure ones may give rise to impossibility of performance or not, the relevant parties should firstly determine whether the event of impossibility in question is temporary or permanent.

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<sup>1</sup> The judgement of the Assembly of Civil Chambers of the Court of Cassation dated 27 June 2018 and numbered E. 2017/90 K. 2018/1259.

The closing of certain enterprises based on administrative decisions of the Administration or recommendation decisions of the professional associations as part of precautions taken against the Covid-19 should in turn mean that the performance of obligations arising from lease agreements will be temporarily impossible due to reasons not attributable to the parties and that the performance of the obligations may become possible upon the expiry of such extraordinary event. As such, particularly in case of the below-mentioned events, parties may be able to allege temporary impossibility of performance existing under the Turkish law doctrine and the precedents of the Turkish Court of Cassation and obligations arising from the relevant lease agreements will not cease to exist but may be suspended until the event of impossibility expires. It should be kept in mind that the parties must have mutual agreement on suspension of obligations and the performance time of the obligations must be appropriate for such suspension. It is worth pointing out, in any event that, separate analysis should be conducted over the specific circumstances of the concrete case on a case-by-case basis.

Furthermore, one of the initial topics relating to the above would be the consequences of lease agreements executed in relation to (i) enterprises operating as public recreation and entertainment places (e.g. cinemas, gyms, amusement parks, association clubs, bars and night clubs), activities of which have been temporarily suspended as of 24:00 on the date of 16 March 2020 based on a decree of the Ministry of Interior Affairs dated 16 March 2020 and numbered 5361, and (ii) workplaces located at shopping malls which have been almost entirely closed upon a recommendation decision adopted by the Association of Shopping Mall and Investors.

Under a lease agreement being in force, the lessor is obliged to make the lessee use the leased property as well as to make the leased property available to the lessee whereas the lessee is under obligation to make payment of lease amounts to the lessor at maturity. Meaning that, each of the parties to a lease agreement is obliged to fulfil its own debts in consideration for the other party's obligations under the relevant lease agreement having a synallagmatic nature. However, due to the above precautions in place, if a lessor fails to have the relevant lease property available for the use of the lessee for a temporary period, one might say that obligation of the lessor has become temporarily impossible. As there is a temporary impossibility of performance, the obligation of the lessor to make the lessee use the leased property cannot be deemed automatically to be ceased to exist in every case. That being said, the lessor who cannot perform its obligations due to such temporary impossibility will not be in a position to oblige the lessee to pay the lease amounts. In such a case, it can be said that the reciprocal obligations of the parties are suspended, postponed for a temporary period of time and accordingly, the lessor cannot oblige the lessee to pay the lease amounts. In case of such a request from the lessor, the lessee can allege the non-performance of the lessor's obligations which allows the lessee to abstain from fulfilling its own obligations until the other party duly performs its debts, as a defence of non-performance regulated under Article 97 of the Turkish Code of Obligations. Even in such an event, the precedents of the Turkish Court of Cassation indicate that the parties will continue to be bound by the provisions of the agreement during the tolerance term of the agreement and that the binding force of that agreement will be terminated upon the expiry of the respective tolerance term.

On the other hand, the term of lease agreements in relation to enterprises, activities of which have been suspended as part of the precautions taken by the Turkish government against the Covid-19 may overlap the period of time when the temporary suspension decisions are implemented. That is to say, the term of the lease agreement may fall into the same time of period as the governmental suspension decision. If so, it should be kept in mind that temporary impossibility will no longer be the case and the obligations of both parties may cease to exist as these have become permanently impossible. In this respect, we would like to highlight that the provisions of workplace lease agreements should be analysed on a case-by-case basis in light of the relevant circumstances. Having said that, in any event where the impossibility of performance arises, the debtor must notify the other party that its obligations have become impossible and must take the necessary precautions in efforts to prevent further damages. Any debtor failing to

fulfil these requirements will have to compensate any damage incurred by the other party due to the debtor's failure.

## **May the impacts of Covid-19 lead to hardship in relation to lease agreements?**

Considering that lease agreements impose monetary obligations on lessees, another topic to be addressed in relation to the impacts of the Covid-19 on such agreements is whether the provisions of hardship under Article 138 of the Turkish Code of Obligations would be applicable or not.

According to the aforesaid article, the hardship remedy allows either party to request from the competent judge to revise the terms and conditions of the respective agreement in line with new extraordinary events which were unforeseen, unforeseeable at the time of execution (*l'imprévision*) and not attributable to the debtor and which have made performance of the debts significantly difficult. However, if such adaptive revisions cannot be made, this remedy allows the debtor to terminate the relevant agreement imposing continuous obligations (if any). To this end, extraordinary events must have changed the pre-existing circumstances to the detriment of the debtor to the extent that (i) it cannot be reasonably expected from the debtor to perform its obligations in accordance with the principle of *bona fide*, which in turn means that these have deteriorated the balance of either party's obligations in a manner not tolerable by the debtor, and that (ii) the debtor must have not fulfilled its obligations or must have fulfilled its obligations with a reservation of its rights arising under the hardship provisions.

Within the scope of the above precautions in place, the temporary suspension of the activities of certain workplaces or the closing of the shopping malls in which they were operating may constitute an extraordinary event leading to hardship in terms of lessees who are under obligation to pay lease amounts at maturity. In addition, setbacks in the supply chain or significant decrease in the number of clients and the continuation of these circumstances may, depending on the conditions of the concrete case, fall into extraordinary event within the sense of Article 138 of the Turkish Code of Obligations and deteriorate the balance between the obligations of both parties to the extent not tolerable by the lessee. Therefore, the hardship provisions may be applied in particular cases where the performance of an obligation has not become impossible but has become significantly difficult upon the occurrence of an extraordinary event.

In the events where contractual provisions of hardship are present, such provisions shall be applied in the first place depending on the conditions of a particular case; however, if necessary revisions cannot be made to the relevant agreement in accordance with the equity principle, parties can apply to the competent Turkish court by reason of statutory remedy set out under Article 138 of the Turkish Code of Obligations. Also, we would like to point out that it would be the best option in most cases for both parties to conduct negotiations on revisions to be made in accordance with the new extraordinary events (if the required conditions are present) and accordingly revise the underlying agreement without seeking any judicial remedies, regardless of whether there is a contractual event of hardship between the parties.

Consequently, any lessee who has experienced an event of hardship within the sense of Article 138 of the Turkish Code of Obligations may request from the competent judge to revise the respective lease agreement in line with the new extraordinary events provided that such lessee has yet to pay the lease amounts or has paid the lease amounts with a reservation. If the agreement cannot be revised due to such event of hardship, the lessee can seek a judicial remedy for the termination of the agreement as long as it complies with the periods of time set out under the applicable laws.

## **What does the Omnibus Law bring about in relation to workplace lease agreements?**

According to Provisional Article 2 of the Law on Amendment of Certain Law (Law No. 7226) (the "**Omnibus Law**") which has been published in the Official Gazette on 26 March 2020 with immediate effect, failure to pay the lease amounts accrued from 1 March 2020 to 30 June 2020 in

relation to workplaces shall not constitute a valid ground for the termination of lease agreement or the evacuation of lessee from the leased property.

Moreover, it is worth noting that the above rule shall apply only to workplace lease agreements with a view to protecting the employment. That being said, lease amounts shall continue to accrue and lessees will not be discharged from their obligations to make payment of lease amounts relating to the relevant period of time. In parallel, default interests and penalty clauses will also remain applicable during such period specified under the Omnibus Law.

In consequence, the Omnibus Law restricts certain remedies that the lessors can seek in case of non-payment of the lease amounts between 1 March 2020 and 30 June 2020; and accordingly, the lessors will not be able to initiate execution proceedings for the purpose of evacuation upon the failure of the lessee to pay lease amounts for such 4-month period or to file a lawsuit in efforts to request for evacuation of lessee from the leased property following two notices sent to it.

## **Conclusion**

In light of our explanations above, it should be noted in a nutshell that the Covid-19 would have various impacts on the lessor and the lessee from a legal perspective, depending on the specifics of the concrete case as well as the provisions of the underlying agreement. As such, the provisions of the lease agreement executed between the parties must be thoroughly reviewed in order to ascertain any such impacts and possible consequences thereof, and the parties should make efforts to resolve disputes in an amicable way to the extent possible before seeking their judicial remedies, particularly during this challenging period of time.

Nevertheless, those who may be affected from the Covid-19 should keep a close watch on the relevant legislative developments, administrative decisions and precautions to be taken by the competent authorities in the upcoming days as legal relationship between the lessor and the lessee should be accordingly re-analysed in light of the same.

**Kind regards,**

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