Appeal Division of the Gauteng High Court finds that the COVID-19 Pandemic and accompanying Government-imposed lockdown regulations cannot always act as a supervening impossibility in a lease agreement, to allow rental remissions.

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The Appeal Division of the Gauteng High Court recently ("**the Court**") (in an appeal hearing from the Magistrate's Court) delivered the judgement of *Hennops Sports (Pty) Ltd v Luhan Auto (Pty) Ltd*[1] which deals with the non-payment of rental as per a lease agreement during the COVID-19 pandemic ("**COVID**"). The pith of the appeal and legal question was whether COVID-19 and the accompanying Government-imposed lockdown regulations can be considered a supervening impossibility of performance in terms of the lease agreement concluded between the parties.

This is the first judgment where a South African Court makes a direct finding on whether the COVID lockdown regulations constituted an event of supervening impossibility which would entitle a lessee to a remission of rental.

Background

Hennops Sports (Pty) Ltd ("**Hennops**") concluded a written lease agreement with Luhan Auto (Pty) Ltd ("**Luhan**") in terms of which Hennops leased immovable property to Luhan for the purpose of conducting business as a motor vehicle dealership ('**the lease agreement**"). The rental was due monthly in advance.

In March 2020, the lockdown regulations prescribed that during the lockdown period all businesses that were not considered essential businesses should cease operations. Luhan was not an essential business and was thus compelled to cease business operations from the premises. Consequently, Luhan failed to pay for rental for the period April to July 2020.

[1] (A52/2022) [2002] ZAGPPHC 953 (2 December 2022)

Hennops issued summons claiming the arrear rental amount plus penalties as per the lease agreement. Luhan defended the action[2] and pleaded *casus fortuitus / vis major*, alleging that COVID (and the lockdown regulations) prevented its commercial activity and accordingly performance of its obligations in terms of the lease agreement were made temporarily impossible due to no fault of Luhan.

This matter was first heard in the Magistrates Court where the Magistrate concluded that the lockdown regulations constituted a supervening impossibility of performance in terms of the lease agreement, as a result it upheld Luhan's defence. The Court *a quo* ordered Luhan to pay only 50% of the reduced rental for the period June-July 2020. Hennops brought this decision on appeal to the Court.

For purposes of this article, we only review one of the legal questions considered by the Court on appeal i.e. whether COVID and the resultant lockdown regulations caused a supervening impossibility of performance in terms of the lease agreement

Assessment and findings of the Court

The Court looked at the essential legal requirements of a lease agreement to navigate whether lessee's failure to generate income or make profit affects the continuation of a lease

The Court referred to the case of *Kessler v Krogmann*[3] which held that the essential terms of a lease agreement are as follows:

> "…*there must be an ascertained thing and a fixed rent at which the lessee is to have the use and enjoyment of that thing."*

In terms of the common law, the lessee must be given undisturbed possession of the thing and the lessor must be paid rental, in return. It was common cause that the immovable property that was leased to Luhan remained intact and was able to be used to house the motor

[2] Luhan also instituted a counterclaim in relation to a previous agreement reached to reduce the rental amount, however, this is not relevant for current purposes.
[3] 1908 TS 209 at 297 quoted with approval in *Ferndale Crossroads Share Block (Pty) Ltd and Others v Johannesburg Metropolitan Municipality and Others* 2011 (1) SA 24 (SCA)

vehicles intending to be sold (albeit that Luhan could not trade). The Court stated that the lockdown regulations did not prevent the conclusion of lease agreements, it did not render it illegal to give usage and enjoyment of immoveable or to pay rental for such enjoyment.

The Court held that the purpose of Luhan renting the immovable property from Hennops was to provide a space for a Luhan to keep its stock safe. This purpose was never rendered illegal by the lockdown regulations.

After considering various authorities regarding lease agreements (and the *essentialia* thereof), the Court held that what is important is the foundation of the contract as opposed to the one-sided object of contracting. If the one-sided object of contracting is frustrated, the contract is not hit with by supervening impossibility, nor can it be said that the contract performance is frustrated so to discharge parties of their respective obligations.

The Court stated that commercial impossibility does not give rise to the principle of supervening impossibility and accordingly a party cannot be discharged from performing a contract because it is non-profitable for that party. While the COVID regulations undoubtedly had an impact on the profitability of Luhan, profitability is not one of the *essentialia* of a lease agreement. The parties did not conclude the lease agreement with the sole purpose of trading as this purpose only serves the interests of the lessee (Luhan) and not that of the lessor (Hennops). The reciprocal obligations to be adhered to by the parties were simply the undisturbed possession of the leased property by Hennops in exchange for the payment of rental by Luhan. The Court stated that there is no connection between undisturbed possession of the leased property and profitable sales in the lease agreement. While the lease agreement specified that immovable property leased to Luhan would be used to conduct a motor vehicle sales business, the lease agreement was not founded on the successful sales of motor vehicles but rather the physical housing of the vehicles.

The Court stated that it is of paramount importance to note that the lockdown regulations did not affect virtual manner of conducting business. The lockdown regulations did not imply that

vehicles and/or stock could not be housed in the immovable property or that those that attract financial obligations must not honour those obligations.

The Court referred the recent judgment of Acting Justice Pretorius in the *Nogoduka-Ngumbela Consortium (Pty) Ltd v Rage Distribution (Pty) Ltd t/a Rage*[4] matter where it was held that performance in terms of the lease was prohibited by the promulgations of the lockdown regulations and, as such, the inability to perform constitutes objective legal impossibility. The Court, with considerable regret, disagreed with the finding of Acting Justice Pretorius and stated that nowhere in the lockdown regulations lies a prohibition of performance recorded in the lease agreement i.e. make a lease property available for enjoyment and use and payment of rental in return.

The Court is of further of the view that the Supreme Court of Appeal ("**SCA**") in the matter of *Slabbert NO & 3 Others v Ma-Afrika Hotels t/a Rivierbos Guest House*[5] missed the golden opportunity to settle authoritatively so the conundrum in relation to supervening impossibility of COVID and the subsequent lockdown regulations. The SCA stated the following:

> "…*I am of the view that it is not necessary for this Court to decide whether the restrictive regulations applicable during the period 26 March 2020 to September 2020 constituted a supervening impossibility of performance that discharged the respondent from the liability to pay the full amount of rental. At best for the respondent, Hansen may mean that the period during which the Covid-19 regulations prohibited or restricted trade … is a direct and immediate cause of inability to perform*…"

Regrettably, so it was held, the SCA did not make a definitive finding as to whether the impairment of an ability to fully trade and exploit the commercial potential of the premises constituted *vis major* that will discharge liability to pay rental during hard lockdown.

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[4] (3587/2020) [2021] ZAGPJHC 568 (19 October 2021)
[5] (772/2021) [2022] ZASCA 152 (4 November 2022)

The Court also referred to the Canadian judgment of Mew J in *Braebury Development Corporation v Gap (Canada) Inc*[6] in which it was held:

> "…*the question is whether the COVID-19 restrictions radically altered the terms of the lease agreement. While this event did prohibit Gap from operating its retail stores temporarily between March 2020 and May 2020 and then at a reduced capacity until September 2020, it is not clear that this would be sufficient to engage the doctrine of frustration. Furthermore, to radically alter the terms of the lease, the supervening event must not merely increase the burden of satisfying the contractual obligations, but must affect the nature, meaning, purpose, effect and consequence of the contract so far as it concerns either or both parties*…"

The Court agreed with the sentiments expressed by Mew J.

The Court concluded that the ceasing of operations as required by the lockdown regulations did not imply an interruption of all lease agreements, it was thus still legal for premises to be hired and rental to be paid during the hard lockdown. It was not the terms of the lease agreement that Luhan was only allowed to conduct a specific operation (virtual trading would have been possible, even in the absence of physical movement of people). Accordingly, performance in terms of the lease agreement was not made impossible in this case. The Court held that there was no supervening impossibility as a result of the lockdown regulations.

<u>Outcome</u>

The Court upheld the appeal and found that the Court *a quo* erred in finding that the lockdown regulations amounted to a supervening impossibility of performance of the lease agreement. The Court stated that a cessation of operations did not fundamentally change the nature of the lease agreement as concluded by the parties. Consequently, the operation of the lease

[6] 2021 ONSC 6210 (CV-20-322 Kingston). The matter dealt with almost similar facts

agreement was not destroyed by the lockdown regulations and Luhan was held to be liable for the arrear rental as well as the penalties payable in terms of the lease agreement.

Concluding remarks

This judgment answers the question that the SCA declined to make a finding on in an earlier judgment relating to rental remissions. The essence of this judgment is that whilst the lockdown regulations had an effect on the profitability of various non-essential businesses, this amounts to a commercial impossibility, not supervening impossibility which would allow remission of rental.

Even though the Court concluded that COVID and the subsequent lockdown regulations did not constitute a supervening impossibility in this instance, each case must still be assessed on its own merits, having regard to the terms and purpose of the lease agreement. The judgment underpins the principle that one must determine whether, in each instance, the nature of the lease agreement was changed / destroyed by introduction of the lockdown regulations. If there was no such change or destruction, then there was no supervening impossibility which would relieve a tenant from its obligation to pay rental.

For more information regarding this judgment and its impact, as well as any of the previous judgments on this topic, please do not hesitate to contact us.