

real estate e-bulletin

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FRENCH LAW ON CRAFT INDUSTRIES AND TRADES, COMMERCE AND VERY SMALL ENTERPRISES, KNOWN AS THE "PINEL" LAW

The French Parliament definitively adopted the Pinel Law (loi relative à l'artisanat, aux commerces et aux très petites entreprises) on 5 June 2014. The law will now be promulgated by the French President, unless a referral is made to the Constitutional Council within 15 days of government receiving the bill. The entire first section is dedicated to "adaptation of the commercial lease regime".

MAIN PROVISIONS

Restrictions on fixed-term commercial leases (Article 2 of the Pinel Law – future Article L. 145-4 of the French Commercial Code)

Apart from with respect to:

- leases with an initial term exceeding nine years;
- leases for premises built for a single specific use (known as "single-purpose" leases);
- leases for premises exclusively for office use; and
- leases for storage premises (as defined with respect to the annual tax on office buildings located in the Paris region - Article 231 *ter* of the French Tax Code).

Lessees will no longer be able to waive their right to terminate after each three-year period, such that all leases will be "3/6/9" leases.

Short-term leases (Article 3 of the Pinel Law – future Article L. 145-5 of the French Commercial Code)

- Maximum term permitted for exceptional short-term leases increased from two to three years.
- After the three-year term, the parties cannot enter into a further short-term lease for "the same business operated in the same premises".
- One-month period allowed beyond expiry of the three-year short-term lease during which the tenant may be asked to leave, prior to the automatic application of commercial lease status.

Tenancies at will (Article 4 of the Pinel Law – future Article L. 145-5-1 of the French Commercial Code)

- Court-developed definition enshrined in the law: commercial lease status "shall not apply to tenancies at will, which, regardless of the duration thereof, are defined by the fact that occupation of the premises is only authorised on the basis of specific circumstances that do not depend solely on the parties' wishes".

Schedule of condition (Articles 3 and 13 of the Pinel Law – future Articles L.145-5 and L. 145-40-1 of the French Commercial Code)

- Under commercial leases: a schedule of condition must be drawn up "in the presence and with the agreement" of the lessor and the tenant, or by a third party appointed by them, when the tenant takes possession of the premises as well as when it quits them, or in the event of assignment of entitlement to the lease, or assignment or free transfer of the going concern.

Lessors that have not taken all necessary measures to ensure the schedule of condition is drawn up may not assert that the tenant received the premises in good condition (Article 1731 of the French Civil Code).

- Under short-term leases: a schedule of condition must be drawn up "in the presence and with the agreement" of the lessor and the tenant, or by a third party appointed by them, when the tenant takes possession of the premises as well as when it quits them; such schedule of condition must be appended to the lease.
- In both the above cases: a court official (whose fees are borne 50/50 between the lessor and the tenant) may be appointed pursuant to an application from either party if they cannot agree upon the schedule of condition.

Inventory of service charges, taxes, duties and works (Article 13 of the Pinel Law – future Article L. 145-40-2 of the French Commercial Code)

- An implementing decree will stipulate the "service charges, taxes, duties and fees that, due to their nature, cannot be charged to tenants, and the terms according to which lessees should be informed".
- A "detailed and exhaustive inventory of all types of service charges, taxes, duties and fees pertaining to the lease, indicating their allocation between the lessor and tenant", must be appended to all lease agreements.
- Lessors must provide lessees with an annual summary statement of such service charges, taxes, duties and fees (the deadline for such will be set by decree).
- Lessors must inform lessees of any new service charges, taxes, duties or fees applicable over the term of the lease.
- Lessors must provide tenants, upon signature of the lease and every three years thereafter, with (i) a provisional statement of the works the lessor intends to carry out over the next three years (together with the provisional budget) and (ii) a summary of the works carried out by the lessor over the past three years (together with the cost thereof).

- In property complexes with multiple tenants:
 - the amount of taxes, duties and fees that can be allocated to each tenant must strictly correspond to the premises leased and to the share of the common areas necessary to their use;
 - the allocation of service charges or of the cost of works between the various lessees must be set out in the lease and must be "in line with the surface area used";
 - lessors must inform tenants of any development over the term of the lease that could affect the allocation of service charges between them.
- This is a mandatory public order provision and will apply regardless of the use of the leased premises (any provision to the contrary will be deemed unwritten).

Notice requirements (Article 18 of the Pinel Law – future Article L. 145-9 of the French Commercial Code)

- Notice may be validly given, at the discretion of the parties and regardless of the lease provisions, by registered letter with acknowledgement of receipt requested or by extra-judicial document.
 - ⇒ Service by court official still required for requests from lessees for renewal and responses to such requests.

Removal of rent cap (Article 11 of the Pinel Law – future Articles L. 145-34, L. 145-38 and L. 145-39 of the French Commercial Code)

- The circumstances under which the rent cap ceases to apply remain unchanged:
 - lease renewal (Article L.145-34 of the French Commercial Code): significant change in the premises' characteristics, the use of the premises, the parties' respective obligations or local marketability factors, leases granted for terms of more than 9 years, leases for single-purpose premises or premises exclusively for office use, 9-year leases extended by tacit agreement to a term of more than 12 years, etc.;
 - triennial rent review (Article L.145-38 of the French Commercial Code): significant change in local marketability factors resulting in a variation of more than 10% in the market rental value;
 - court-ordered rent review (Article L.145-39 of the French Commercial Code): variation of more than 25% in the rent pursuant to an indexation clause.
- However, if the rent cap ceases to apply for one of the above reasons, the resulting variation in the rent will nonetheless be limited to 10% of the "rent paid over the previous year", except for, in the event of a renewal:
 - premises exclusively for office use;
 - leases for "single-purpose" premises;
 - 9-year leases extended by tacit agreement to a term of more than 12 years.

Triennial rent review (Article 12 of the Pinel Law – future Article L. 145-38 of the French Commercial Code)

- Revised rent effective as from the date of the request for triennial rent review (mandatory public order provision).

- Any alternative provisions (stipulating, for example, that the revised rent shall be due retroactively as from the beginning of the new three-year period) will thus be ineffective.

Indexation (Article 9 of the Pinel Law – future Article L. 145-34 of the French Commercial Code)

- Removal of references to the construction cost index (ICC) for calculation of the rent cap upon renewal or triennial rent review, should such index be stipulated in the lease.
- The rent cap must therefore be calculated on the basis of either the tertiary activities rent index (ILAT) or the commercial rent index (ILC), according to the lessee's activity.
- However, the ICC can still be used for indexation clauses.

Lessee's right of first refusal (Article 14 of the Pinel Law – future Article L. 145-46-1 of the French Commercial Code)

- Creation of a right of first refusal in the event of sale for lessees of retail or craft-industry premises (unclear whether or not this right of first refusal will apply to warehouses and offices).
- Procedure: the lessor must notify the tenant of the planned sale, indicating the price and terms thereof – failure to do so renders the notification void; such notification constitutes an offer to sell; the tenant has one month during which to either accept or reject the offer; should it accept, the tenant then has two months as from the date on which it so responds during which to complete the sale (increased to four months if acceptance of the offer is conditional upon obtaining a loan); the offer to sell lapses if the sale is not completed within such time.
- If the lessor decides to sell for a price or on terms that is/are more advantageous to the buyer, the notary is required (if the lessor has not already done so) to inform the tenant of such price and terms – failure to do so renders the sale void; such notification constitutes an offer to sell to the tenant.
- Right of first refusal not applicable in the event of (i) a "single sale of several units within a retail complex", (ii) a "single sale of separate retail units", (iii) a "sale of a retail unit to the co-owner of a retail complex", (iv) a "sale of a building comprising retail units in its entirety" or (v) a "sale of premises to the lessor's spouse, or to any ascendant or issue of the lessor or lessor's spouse".

MISCELLANEOUS PROVISIONS

Sanctions for non-compliant clauses (Article 6 of the Pinel Law – future Article L. 145-16 of the French Commercial Code)

- Any clauses that do not respect the mandatory public order provisions on commercial leases shall be deemed unwritten (as opposed to annulled, as previously).
 - ⇒ There will thus be no limitation on challenges to such clauses (whereas applications for nullity are time-barred after a certain period).

Application of commercial lease status to foreigners (Article 5 of the Pinel Law)

- The articles of the French Commercial Code excluding certain foreign traders or lessors from the benefit of commercial lease status have been removed.

Lease assignment (Articles 7 and 8 of the Pinel Law – future Articles L. 145-16-1 and L. 145-16-2 of the French Commercial Code)

- In the event of a lease assignment under which the assignor agrees to act as guarantor:
 - the lessor must inform the assignor of any payment default on the part of the assignee within one month from such default;
 - guarantee limited to three years as from the date of assignment of the lease.

Commercial leases included in disposal plans for lessees in financial difficulties (Article 15 of the Pinel Law – future Article L.642-7 of the French Commercial Code)

- When a lease is included in a disposal plan for a lessee in financial difficulties, the competent commercial court can authorise the buyer to extend the activities permitted under the lease to include complementary or related activities.

Effects of a demerger or transfer of all assets and liabilities of the tenant (Article 6 of the Pinel Law – future Article L.145-16 of the French Commercial Code)

- All rights and obligations arising under a lease for the company to which the lease was granted may be transferred to a new company created as a result of a demerger or transfer of all assets and liabilities, notwithstanding any stipulations to the contrary.
- Previously, only mergers and partial contributions of assets were provided for.

TIMEFRAME FOR APPLICATION OF THE PINEL LAW

The Pinel Law will apply to leases entered into or renewed as from the 1st day of the 3rd month following the law's promulgation, except for as regards:

- the obligation to draw up a schedule of condition upon vacation of premises (for both commercial and short-term leases – see section 4 on the main provisions above), which will apply to all vacations of premises for which a schedule of condition was drawn up upon entry into possession;
- the lessee's right of first refusal (see section 10 on the main provisions), which will apply to all sales of premises occurring as from the 6th month following the law's promulgation.

Any clauses in existing commercial leases that do not respect the mandatory provisions of the new law will remain legal until the renewal of such leases. The law will therefore not apply to existing leases until such time as they are renewed.

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