

Reform of the law regarding commercial real estate leases under the “LME” law No. 2008-776 of August 4, 2008

The law on economic modernization was published in the Official Journal on August 5, 2008.

The objectives set forth in the text of this law are to modernize the economy at its core in order to stimulate growth, employment, and consumer purchasing power. With the possible exception of decrees applicable to certain particular measures, the entire text of the law should become effective on January 1, 2009.

This article summarizes the principle modifications to the French Commercial Code in connection with the modernization of the “*Statut des baux commerciaux*”, or the law regarding commercial real estate leases (hereinafter referred to as the “Commercial RE Leases Law”), as set forth in Chapter III of the LME.

1. Modifications to the registration conditions of leasees and heirs with the register of companies

In accordance with Article L. 145-1 of the French Commercial Code, the applicability of certain regulations specific to commercial leases, collectively known as the Commercial RE Leases Law, requires that the lessee operate a business, as well as the registration of the lessee with the register of companies or trade register.

Before the LME, each leasee to a commercial lease had to be registered in the register of companies. If not, it would lose the benefits provided for it under the Commercial RE Leases Law. Following the LME, however, a leasee could retain the benefits provided under such laws even if it fails to register, as long as the business operator is properly registered.

Similarly, before the LME law of August 4, 2008, heirs and assigns to a deceased lessee had to personally register if they wanted to continue operating the business of the predecessor lessee. Now, on the other hand, such heirs and assigns can merely request that the registration of the predecessor be maintained to enable them to continue to operate the business.

2. A Voluntary adoption of the type of commercial lease by professionals

The law on economic modernization will allow professionals to choose the type of lease they want, allowing them to benefit, if they want, from the benefits available for commercial leases under the Commercial RE Leases Law.

Therefore, professionals will have a choice between professional leases governed by Article 57A of the law of December 23, 1986 on the one hand, or commercial leases governed by the Commercial RE Leases Law on the other hand.

3. Modifications to the rules regarding short-term commercial leases

A commercial lease subject to the Commercial RE Leases Law cannot technically have a term that is less than nine years. Parties can mutually waive this requirement, however, and enter into what is known as a “short-term” commercial lease with a term of two years or less.

Article 44 of the LME will modify Article L. 145-5 of the French Commercial Code by hereinafter allowing parties to enter into several short term commercial leases as long as their aggregate term does not exceed two years, which was not possible before the LME because short-term leases could not be renewed under any circumstances.

As was the case before the new law, if the lessee remains in possession after expiration of the two-year term limit, then the lease converts into a commercial lease subject to the Commercial RE Leases Law.

4. The end of the “local practices” factor to determine notice requirements in connection with terminations and renewals

Prior to the LME, local practices were used as a factor to determine certain applicable time limits/notice requirements regarding commercial real estate leases, in connection with termination and renewal requests. The time limits/notice requirements before the LME, which could vary factor among geographic regions, as a result of the use of the “local practices”, from six months to 18 months, are now cancelled altogether.

Consequently, the local practice factor no longer exists and is replaced by focusing on the first or last day of the calendar quarter, depending on whether the lease is being terminated or renewed (Articles L. 145-9 and L. 145-12 of the Commercial Code).

In addition, an evicted lessee will be now required to vacate the premises within three months following receipt of the eviction indemnification. (Article L. 145-29 of the Commercial Code.)

5. The ability of parties to choose the terms of the commercial real estate lease

The cost of construction index (CCI) serves as a reference point for quarterly rent adjustments made to commercial real estate leases, as well as to set price ceilings when leases are renewed.

To restrain recent significant increases in commercial real estate rents (which have come about, in part, as a result of considerable variations in the CCI over the last few years), some professional organizations that represent owners/lessors and operators/lessees have proposed substituting the CCI with a new sectoral index known as the “Index of Commercial Real Estate Leases” (ICL), which is a weighted average of (i) the index on consumer prices (50%); (ii) the CCI (25%); and (iii) an index based on the retail trade at issue’s gross sales (25%).

This new index should evolve at a rate of 2.5% to 3% per year (as opposed to the 17.87% increase of the CCI each of the last three years), bringing it more in line with the actual growth of the retail trades in question thanks to its formula.

The conditions applicable to this new index have yet to be fully established, however. Indeed, the ILC is not likely to apply unless the parties expressly agree to it by means of an addendum or amendment to their existing lease or at the time of renewal, and only if the commercial real estate lease relates to a business activity defined by decree (which had not been published as of the date of this newsletter).

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