Short notes on:

EARLY TERMINATION OF COMMERCIAL LEASE AND THE CONSUMER PROTECTION ACT

Introduction

Terminating a commercial lease agreement prematurely does not have to be as complicated as one would expect. Due to various unexpected circumstances or events, it sometimes happens that a company or individual is unable to continue performance under the requirements of the agreement.

A commercial lease will naturally have stricter termination regulations in terms of the agreement and legislation than a residential lease agreement. With that being said, some of the key principals will be the same or similar.

Before the enactment of the Consumer Protection Act No. 68 of 2008, as amended (the “CPA”), the termination of particularly commercial lease agreements were regulated by South African contract law, common law and the Rental Housing Act No. 50 of 1999, as amended. The CPA has made it necessary for both tenants and landlords, commercial and residential alike, to comply with the statutory provisions governing such early termination. If procedures are followed correctly, the early termination by either party would not constitute a breach of agreement. This involves a formal legal process, and since the inception of the CPA, these agreements which traditionally favoured the landlord, no longer weighted unfairly in favour of him/her.

Termination of a lease agreement and the CPA

In practice, it happens more often that the tenant wishes to cancel the lease prior to the expiration of the fixed term lease agreement. Should a tenant wish to terminate the lease, the first point of call will be for the tenant to carefully study the signed lease agreement between the tenant and the landlord. Sometimes the lease agreement does not contain a clause regulating the requirements for early cancellation of the lease. In these situations the tenant should immediately refer to the CPA. However, it is crucial to ensure that your agreement falls within the scope of the CPA, as certain landlords or tenants have been excluded by virtue of their legal persona (ie a legal person – juristic person) or its size (business size).
The expiry and renewal, and by derivation the termination of lease agreements (fixed term contracts), is regulated in terms of section 14 of the CPA. This section stipulates that any fixed term contract may currently not exceed a period of 24 months. It further states that despite any provision to the contrary, and including the lease agreement, the tenant (consumer) may terminate the lease agreement in any of the following ways:

- Upon expiry of its fixed term, without penalty or charge¹. It is to be noted that the CPA stipulates that the landlord must notify the tenant of the expiry date between 40 and 80 business days’ prior to such expiry.
- Or at any other time, by giving the landlord 20 business days’ notice in writing or other recorded manner and form².

Effects of early cancellation

In both of the above situations, the termination is subject to the provisions set out in subsection 3 (a) and/or (b). This section merely states that the tenant will be liable to the landlord for any amounts owed to the landlord in terms of the agreement up to the date of the cancellation³. This means that the tenant must continue to pay rental amount for the notice period, and do so on a pro rata basis if applicable. It further goes on to mention that the landlord may impose a reasonable cancellation penalty in respect to the lease with the tenant in contemplation of the agreement enduring for its intended fixed term, if any, and must credit the tenant with any amount that remains the property of the tenant as of the date of cancellation⁴. The latter is only applicable where the tenant opts to terminate the lease agreement any time prior to the expiry thereof by giving the landlord 20 business days’ notice. This is included in the CPA to protect the landlord’s rights, while still finding a balance to be fair toward the tenant.

Even though the CPA grants the tenant the right to cancel the lease agreement before the fixed term expires, the Act also instill some fear among tenants, especially in commercial lease agreements. This is mostly due to the provisions in the Act that grants the landlord the rights to claim “reasonable cancellation penalties”, and nowhere is this defined clearly. This leaves the provision open to abuse by unscrupulous landlords. So industry has seemed to adopt the below mentioned approach.

¹ Consumer Protection Act No 68 of 2008 – Section 14(2)(i)(aa)
² Section 14(2)(i)(bb)
³ Section 14(3)(a)
⁴ Section 14(3)(b)(i) and (ii)
It is important to note that a landlord has the obligation to immediately advertise for a new tenant. This is solely the responsibility of the landlord, and not that of the tenant. The landlord will be entitled to include the advertising costs as part of the reasonable penalty it may hold the tenant liable for. This is important as prior to the CPA the landlord’s claim was based on his ability or inability to find a replacement tenant – which there was no obligation to find unless specifically agreed. Notably, these have in our experience proven to be key areas of abuse. Some landlords have attempted to convince the tenant that he/she must find a suitable replacement tenant, pay an exorbitant cancellation fee or simply refused to accept the cancellation. This is in contravention with the CPA. Importantly, the onus will rest on the landlord to show that it has made reasonable efforts to replace the tenant. The damages will only be calculable once the landlord finds a new tenant.

The reasonable penalty fee is therefore not intended to penalise the tenant, but rather to allow the landlord to recover costs that it would not have needed to incur, should the tenant have not cancelled the lease agreement prematurely. This costs may also include the rental lost due to the property remaining vacant after the tenant has cancelled and vacated the property. This however, does not give the landlord the right to charge the tenant for an exorbitant number of months that the property has been vacant. It needs to be actual reasonable financial losses shown by the landlord. The landlord cannot use this cancellation and the penalty costs thereof to make a financial gain or benefit, but merely to be reimbursed of any direct financial loss, expenses, or damages suffered.

The landlord will not be able to leverage the fact that it has been inconvenienced or suffered damages by the time consuming exercise of replacing the tenant as a method to accumulate penalty costs, but simply the actual financial damages, expenses incurred or losses due to the early cancellation and in line with such penalty clause.

**Conclusion**

Even though the CPA is vague with the definition of “reasonable cancellation penalties”, the landlord will only ever be entitled to recover those costs that have actually been incurred, and can be proved. Practically speaking, it should not take a landlord more than a month to find a replacement tenant, depending on the property’s location and condition. Should you feel that a landlord is acting unfairly, or should you require assistance with the formal cancellation proceedings, contact a professional at SchoemanLaw Inc.