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# Coronavirus – Implications on Agreements

## Force majeure, impossibility, loss of business basis, hardship, frustration?

The outbreak of the coronavirus challenges not only the human beings and health care systems but also the economy. Not only companies with Chinese business activities are affected. All other companies can be confronted with problems in the supply chain as well. In particular, the question is how the current situation can affect contracts already concluded, for example if goods can no longer be delivered or procured or can only be delivered or procured at much higher cost. Is this a case of force majeure, impossibility, hardship, loss of business basis or frustration and what does this lead to with regard to contractual obligations and rights in different legal systems?

We have prepared this matter for you:

### FORCE MAJEURE AND HARDSHIP IN GERMAN LAW

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Events such as the spread of the coronavirus and the resulting restrictions will put your supply contracts to the test, as you will often be confronted with the concept of force majeure, either because your supplier invokes force majeure against you or because you want to invoke it against your customers to oppose any claims for damages.

With regard to supply contracts, German law does not know these terms. Therefore, they only become relevant through a **specific clause in the contract**, which is particularly common in supply contracts. There are, however, significant differences in terms of the wording. Now is the time to take a close look at the contract in order to make the best of the current situation and, if necessary, make adjustments for the future. The main focus of the review should be on the following points:

- ▶ Which law is applicable?
- ▶ What is considered force majeure and what is not?
- ▶ What is the legal consequence?

If the clause defines the meaning of force majeure more precisely, it is of particular interest in the current situation whether epidemics and official orders are considered to be force majeure and whether the occurrence of such circumstances at the company's own suppliers or subcontractors makes it possible for the company to invoke force majeure itself. With regard to the legal consequence, in particular two scenarios are used: Either the contract is automatically dissolved in the case of force majeure or the contractual obligations are suspended and then reinstated after the end of the extraordinary event (possibly also only suspension for a certain period of time and agreement on a subsequent right of detachment if the event endures).

If the clause does not determine what is to be considered force majeure, German case law on travel law may be applied, if German law is applicable. There, force majeure is defined as "an external event that cannot be avoided even by exercising the utmost care that can reasonably be expected" (see BGH NJW 2017, 2677). In several decisions, epidemics have already been classified as such force majeure (see inter alia AG Augsburg, judgment of 9 November 2004 - 14 C 4608/03 or AG Homburg, judgment of 2 November 1992 - 2 C 1451/92-18). In addition, official orders such as embargoes or restrictions of production can also be classified as force majeure (e.g. OLG Frankfurt a.M., judgment of 16.09.2004 - 16 U 49/04).

Cases of economic impossibility are to be distinguished from the impossibility of contract performance due to force majeure. In these cases, an agreed hardship clause will generally take precedence. In addition, it will also be helpful to take a look at a possible reservation of self-supply, the (non)binding nature of delivery periods, a possible price adjustment right as well as the liability regulations.



## IMPOSSIBILITY AND LOSS OF BUSINESS BASIS IN GERMAN LAW

If no contractual provision has been made for the case of force majeure, the law is applicable, in particular the **impossibility according to Section 275 BGB**. Section 275 BGB applies if the service is impossible or requires an effort that is grossly disproportionate to the creditor's interest in performance, taking into account the content of the contractual obligation and the imperatives of good faith. According to case law and literature, Section 275 BGB also applies in the case of only temporary impossibility of performance for the respective duration of the impediment to performance (see inter alia BGH NJW 2013, 3437; Lorenz in BeckOK BGB, 53rd edition 01.02.2020, Section 275 marginal 39). In this respect, case law even goes a step further and considers the temporary impossibility to be equal to a permanent impossibility, if the achievement of the purpose of the contract is called into question by the impediment and the one or the other party can no longer be expected to demand or perform the service after a fair consideration of the mutual interests (inter alia BGH NJW 2007, 3777). If a supplier from Wuhan is no longer able to deliver due to quarantine and/or officially ordered closure of the company, it is therefore quite obvious that the supplier can invoke impossibility within the meaning of Section 275 BGB. This will be different in the relationship of a German company to its customers, if its own customers can no longer be served due to lack of self-supply (e.g. because its own supplier from Wuhan can no longer deliver). Because if the goods can be ordered elsewhere in the market, in case of higher prices, there will be only a performance difficulty and not an impossibility.

But in addition to the impossibility according to Section 275 BGB, German law also knows **the loss of business basis according to Section 313 BGB**. In the case of an unreasonable difficulty in performance (so-called economic impossibility), Section 275 BGB does not provide a release from performance, but there could be a claim for adjustment (in particular with regard to the price) under Section 313 BGB, because an unreasonable difficulty in performance represents a legitimate case of the loss of business basis. However, whether an increase in difficulty leads to the loss of business basis is always a question of the individual case. It is required that the performance would only be possible with "overobligatory" efforts. In principle, the seller bears the procurement risk, the possibility to refer to Section 313 BGB is an absolute exception.

## FORCE MAJEURE ACCORDING TO THE UN SALES LAW

The UN Convention on Contracts for the International Sale of Goods (CISG) shall apply to international sales of goods (CISG) which are subject to the law of a contracting state or if the parties have agreed on its applicability. Unlike the German Civil Code (BGB), the CISG grants a claim for damages against the seller not dependent on fault. However, Art. 79 CISG puts this into perspective by providing the possibility of exemption from the obligation to pay damages: a party is not liable for the non-performance of one of its obligations if it proves that the non-performance is based on an impediment beyond its control and that this impediment was unforeseeable at the time of conclusion of the contract. A release is often assumed in the typical cases of force majeure if this results in an impediment to performance for the debtor. The literature assumes that epidemics can also constitute such an impediment to performance within the meaning of the provision (see inter alia *Schwenzer in Schlechtriem/Schwenzer/Schroeter, Kommentar zum UN-Kaufrecht*, 7th edition 2019, CISG Art. 79 marginal 16; *Mankowski in MüKo HGB*, 4th edition 2018, CISG Art. 79 marginal 34). State interventions, such as closures of companies, blockades or the closure of transport routes, which make fulfilment impossible, are also recognised impediment to performance (*Mankowski in MüKo HGB*, 4th edition 2018, CISG Art. 79 marginal 35).

## OTHER JURISDICTIONS

Many other jurisdictions have rules on force majeure as well.

**In EU law, it should be noted that** (Art. 12(1)(c) of the Rome I Regulation) "*the consequences of total or partial breach of obligations*" are assessed according to the substantive law applicable to the contract. This includes release from performance due to impossibility, withdrawal and exercise of the withdrawal, adjustment of the contract in the event of loss of business basis or the intervention of so-called hardship clauses in long-term contracts and the consequences of force majeure (cf. *Hohloch in Erman, BGB*, 15th ed. 2017, Art 12 of the Rome I Regulation, marginal 10). Useful guidance regarding this topic is also provided in "[International Sales, Supply and Distribution Law](#)".

In **France**, the loss of business basis is regulated by law in CC Art. 1195. In **Italy**, Art. 1467 of the Civil Code applies to these cases. In **Portugal**, Art. 437°/1 of the Civil Code allows the parties to request termination of the contract in such cases. In **Greece** this is found in Article 388 of the Greek Civil Code.

In **China**, Art. 107 GPCL states that "*Civil liability shall not be borne for failure to perform a contract or damage to a third party if it is caused by force majeure, except as otherwise provided by law*". Likewise, **Turkish law**, which is mainly based on the **Swiss Code of Obligations** (where Art. 119 CO regulates impossibility), is aware of impossibility and only grants claims for damages depending on fault. Art. 1827 of the **Mexican Civil Code** excludes impossible or illegal obligations. Price changes and many other cases of force majeure regularly do not meet these strict requirements.



In **common law** there is **frustration** and in rare cases also **impossibility** is conceivable. In US law, the *doctrine of excuse* covers cases of *impossibility*, *frustration of purpose* and *commercial impracticability*, the latter being codified in Section 2 - 615 UCC and having clear references to force majeure but being interpreted very narrowly (*Grün/Steffens* in *Internationale Wirtschaftsverträge*, 2nd edition 2017, Section 10 marginal 30 f.). However, a no-fault compensation claim is granted as well.

## WHAT HAS TO BE DONE?

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Not only in order to be able to react appropriately to the current situation and proactively work out solutions with suppliers and customers, but also to be prepared for similar incidents in the future, it is advisable to critically review supplier and customer contracts and make adjustments if necessary. When drafting contracts, there are various options for reducing the economic risks in the event of force majeure.

If you want to invoke force majeure against your customers, we recommend that you also apply for a so-called CCPIT certificate. This certificate is issued by the China Council for the Promotion of International Trade and eases the necessary proof of force majeure to your customers. Of course we can help you with this as well as with the contract review and, if necessary, the necessary redrafting. Just contact us!



## PLEASE DO NOT HESITATE TO CONTACT US!

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