

The covid-19 crisis and (international) contracts

The covid-19 pandemic is not only testing health systems worldwide, but rather is also creating enormous challenges for entrepreneurs. Massive economic disadvantages threaten when contractual and service relationships are disrupted, which make swift action necessary.

Performance impairments (default) in connection with (international) contracts

Disruptions to a contractual relationship or along the supply chain are emerging in various forms, for example

1. a supplier's factory is closed due to official order;
2. border closures prevent timely delivery/assembly of the product or preliminary materials;
3. a supplier's production business stops after covid-19 infections;
4. a supplier limits production due to recommendations by the World Health Organisation (WHO).

Suspension of the performance obligation?

In such cases, the question arises as to whether the supplier is still obliged to perform or whether the performance obligation is suspended (temporarily). Ultimately this is a question of the contractual risk allocation.

Statutory or contractual provisions

In Article 79 of the CISG, § 275 of the German Civil Code (BGB) or the often-agreed *force majeure* clauses, there are provisions which are coupled to an event defined as something beyond the parties' control, which for factual or legal reasons at least temporarily makes it impossible for the party obliged to perform to fulfil its performance obligation. The primary legal consequence is then the suspension of the performance obligation. The contractually-agreed performance obligation remains if the event was foreseeable or preventable, or if the party obliged to perform is liable pursuant to the contract for the consequences of the disruption.

§ 313 of the BGB is a special regulation in German law (frustration of contract). No event excluding the performance obligation is required here, but rather a change to the contractual equilibrium due to external influences. The party obliged to perform is theoretically able to fulfil that obligation, but a significantly higher, unreasonable amount of time and expense would be required to do so. In such case, the party obliged to perform is primarily entitled to demand that the contract be adjusted.

Central element: "*force majeure*"

The "*force majeure*" which is decisive pursuant to these provisions is subject to strict prerequisites: unforeseeability, unavailability and exceptionality.

Natural disasters and epidemics can be “*force majeure*” in principle, but it always needs to be ascertained on a case-by-case basis whether there is an impediment to performance which releases the supplier from its performance obligation without triggering compensation claims.

Appraisal of the exemplary cases

The elements to be taken into consideration in the individual case can be illustrated on the basis of the abovementioned examples, where in a first step, pursuant to German law, recalibration of the contractual equilibrium through adjustment of the contractual delivery periods comes into question in each instance:

1. A supplier whose production has been closed down by official order due to covid-19 has been rendered unable to perform, for legal reasons. However, it might be necessary to ascertain whether that supplier is obliged to change to another factory where production is still permitted.
2. In the event of border closures, in principle a supplier being (temporarily) released from its performance obligation due to the actual impossibility of performance comes into consideration. However, it needs to be checked to what extent the respective border closure was foreseeable and whether an alternative form of transport is reasonable. The following principle should be applied: the more concretely the transport problems were foreseeable and the more alternative transport options are available, the likelier it is to be presumed that performance has precisely not become impossible for that supplier.
3. If a supplier’s production stops because its workforce becomes ill, in principle a general business risk is realised. Due to the extraordinary nature of a pandemic, however, in the case of covid-19 infections a non-compensable release from the performance obligation might come into consideration due to actual impossibility. Here it would particularly need to be checked to what extent the covid-19 infections were foreseeable, to what extent the supplier has taken protective measures, and whether alternative production or procurement sources are available.
4. If a supplier wants to shut down its production due to a recommendation issued by the WHO, at first glance this does not constitute impossibility of performance. The WHO does not have the power to enact any legal instruments which make it legally impossible for suppliers to perform. While it is recognised, for example, in travel law that WHO warnings can give rise to an instance of force majeure, the considerations underlying that categorisation in the tourism industry should not simply be transferred to the production industry. It seems questionable whether an instance of force majeure can be deemed to exist solely due to recommendations made by a non-government organisation or even due to official recommendations (e.g. travel warnings issued by the German Federal Foreign Office).

Conclusion

This brief outline shows that, even in times of covid-19, generally invoking “*force majeure*” is associated with risks. The contractual and statutory provisions are always to be assessed in the individual, specific situation. The outcome of that assessment depends on a multitude of factors, which will be different from case to case, and precludes any generalised appraisal or allocation to case groups. In most instances it will be crucial to evaluate the contractual allocation of risks and

to work out in negotiations what contract adjustments can restore that risk allocation. In contrast to usual performance impediments, where covid-19 is involved the disruption event cannot be allocated to the risk sphere of one of the contract parties, which necessitates an equalisation of interests.

We here at PPR & PARTNER have prepared ourselves for the current situation and the resulting special requirements, and are of course at your side, fully ready to assist.

Your contact partners regarding questions about performance disruptions in connection with business contracts are Dr Stephan Wolff, and Fabian Batthaus, LL.M.