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New coronavirus – commercial law relationships

With regard to the spread of the new type of coronavirus SARS-CoV-2 disease (hereinafter only the “Coronavirus“) we provide some useful information related to contractual relationships with your business partners. Following China, a number of measures against the spread of the epidemic (quarantines, ban on mass events, etc.) has been introduced in Europe including the Czech Republic. Different situations may occur with regard to the contractual relationships with business partners which can cause that the fulfilment of contractual obligations becomes more difficult or impossible.

Legal consequences

In the contractual relationships governed by Czech law, in particular act No. 89/2012 Coll., the Civil Code will apply. The contractual parties are obliged to fulfil their contractual obligations in due and timely manner regardless of the external circumstances; however, there are certain exceptions to this rule specified below.

A. Breach of contractual relationships

If a party breaches a contractual obligation, it is obliged to provide compensation for the resulting damage to the other party. If, however, the breach was caused by an unpredictable objective event (so called force majeure – e.g., wars, natural disasters or epidemics and pandemics), a release from the obligation to provide compensation for the damage (so called **liberation**) is possible.

For the liberation, following conditions have to be fulfilled at the same time:

1. Occurrence of an extraordinary, unforeseeable and insurmountable obstacle,
2. the obstacle temporarily or permanently prevents the fulfilment of the contractual obligations, and
3. the obstacle is independent of the tortfeasor’s will.

Coronavirus is an extraordinary temporary obstacle independent of the tortfeasor’s will. In case of more intensive protective measures it can also become insurmountable (e.g., closure of borders, shutdown of operations and production).

With regard to the foreseeability, two situations can fundamentally occur. First Coronavirus cases appeared in China in December 2019. If a contract or a partial order was concluded in November 2019 and earlier, the Coronavirus would be unforeseeable. If a contract or a partial order is concluded at present, the Coronavirus is already foreseeable, the parties have to take it into account and there would be no release from the obligation to provide compensation for the damage. With regard to the contracts concluded from December 2019 to January 2020, the

issue of the liberation would be questionable. Generally speaking, the sooner the contract was concluded, the higher is the chance of the release from the liability.

Exceptions from the liberation. The liberation is impossible provided that the obstacle arises from the tortfeasor's personal circumstances (e.g., the illnesses and quarantines of tortfeasor's employees probably makes the liberation impossible) or arises when the tortfeasor is already in default of performance (e.g., if a party is already in delay with delivery, the Coronavirus does not release it from liability). The release from liability is also impossible provided that a party is obliged to overcome the obstacle (see force majeure clause below).

The possibility of release from the liability for damage **does not affect the obligation of the contractual parties to pay contractual fine**, unless agreed in the contract otherwise.

The content of the contract is of importance as well. A frequented provision in the contracts is so called **force majeure clause**. It is usually a provision on exclusion of the liability for damage or on its limitation in the stated cases which covers also such external unpredictable events. If the contracts with business partners are already in place, it is appropriate to thoroughly check for whose benefit or to whose detriment such clause is. If a contract is only to be concluded, it is appropriate, taking into consideration the present state of affairs, to insert such force majeure clause in the contract.

B. Substantial change in circumstances

It is another way how to adjust a contractual relationship affected by external circumstances. This option is often limited or contracted out. This option consists in the right to ask the court to change the contractual obligation by restoring the balance of rights and duties of the parties or to cancel the obligation. However, taking into consideration the length of the court proceedings the use of this option is not very sensible.

C. Subsequent impossibility of performance

In case of Coronavirus, the applicability of the provisions on the subsequent impossibility of performance is rather unlikely. It will be possible to perform the obligation after a determined period.

3. Impact on cross-border transactions

The above information is relevant in case of application of Czech law. However, the above described mechanisms are in some way contained in majority of European jurisdictions. If no law governing the contract has been chosen by the parties, the essential rule is the applicability of the law of the state where the registered office of the seller or supplier is situated.

Summary

Mere concerns about the Coronavirus or internal preventive measures of a party (even if justified) are not sufficient for the application of the above described mechanisms. If there are already material measures (quarantine, limitation of mass events) with real impact on you or your business partner, the application of the liberation or claims resulting from the change in circumstances cannot be excluded.

However, the subject obstacle has to constitute the main and immediate cause of the undue or late performance. Unless agreed otherwise, the liberation does not apply on contractual fines. Other consequences of breach of the contract cease to exist neither (e.g., despite of liberation, a party is still obliged to withdraw from the contract provided that the statutory or contractual conditions are fulfilled).