LATHAM&WATKINS

CORONAVIRUS (COVID-19)

LEGAL IMPLICATIONS FOR CONTRACTS

**The analysis below sets out the relevant considerations from a German law perspective*

Does the contract contain a clause, for example, on *force majeure*, *material adverse change (MAC)* or *material adverse effect (MAE)*?

NO

Consider the following statutory remedies available under the German Civil Code (GCC):

A. Impossibility (Sec. 275 GCC)

Is it possible to argue (based on the terms of the contract and the applicable factual background) that performance of the contract has been rendered impossible or disproportionately onerous in the circumstances? If so, consider the following:

- Impossibility will not override contractual terms or apply if:
  - I. Parties contractually agreed the consequences of the supervening event (*e.g.*, by a *force majeure* clause)
  - II. The party invoking impossibility has caused the underlying event intentionally or negligently
  - III. The event was self-induced or foreseeable at the time of the contract (so consider the date the contract was entered and the state of COVID-19 at that point)
  - IV. An alternative method of performance is possible
  - V. Performance has become more expensive, or
  - VI. The cause of the frustration was the result of a failure by one of the parties' suppliers
- If performance of the contract is found to be impossible, it will automatically be discharged and sums paid may be recoverable, taking into account the benefit received. Consider whether this is a desirable outcome before relying on this doctrine.

B. Change in the contract's basis (Sec. 313 GCC)

Have circumstances that became the basis of a contract changed significantly since the contract's conclusion and would the parties not have entered into the contract or agreed on different terms if they had foreseen this change? If so, consider the following:

- A party may demand that the contract is adapted to the extent that, taking account of all the circumstances of the specific case, in particular the contractual or statutory distribution of risk, one of the parties cannot reasonably be expected to uphold the contract without adaptation.
- A material change in the contract's basis may also be deemed to exist if material conceptions that form the basis of the contract turn out to be incorrect.
- If an adaptation of the contract is not possible or unreasonable, the aggrieved party may revoke or terminate the contract.

C. Termination for compelling reasons (Sec. 314 GCC)

Is there a compelling reason to terminate a long-term contract because, taking into account all the circumstances of the specific case and weighing the interests of both parties, a party cannot reasonably be expected to continue the contractual relationship until the agreed end or until the expiry of a notice period? If so, consider the following:

- If the compelling reasons involve a breach of contract, a warning notice may be necessary before a contract can be terminated.
- Termination of the contract does not preclude a claim for damages.

YES

Does the clause expressly refer to: epidemic, pandemic or contagious diseases?

NO

Does the clause refer to a government intervention / changes in government policy?

Consider the facts being relied upon to engage such wording

NO **YES**

Is there any applicable or "catch-all" wording which might assist, *e.g.*, "acts of God" or "other similar cause beyond the parties' control"?

Consider the facts being relied upon to engage such wording

YES

Consider the following practicalities if relying on a contract clause:

- What notices have to be given to obtain the protection of the clause?
- What is the scope/effect of the protection given by the clause?
- Will relying on the clause in one contract create any tension with insisting on a counterparty's performance of another contract?
- What is the mechanism to resolve disputes around whether the clause has been validly invoked?
- The party seeking to rely on the clause must establish that the force majeure, MAC, or MAE event was sufficiently material. The party should therefore collect documentary evidence: (i) in support of the occurrence of the material event; (ii) as to how the event has caused interruption to the performance of the contract; and (iii) the ongoing impact of the event.
- Plan in advance steps to avoid or mitigate the consequences of COVID-19.
- Consider the consequences of invoking the contractual provision; could it lead to relief from performance, eventual termination of the contract, or potentially cause long-term disadvantages to your business, *e.g.*, cash flow problems?

- Closely monitor the development of COVID-19, government orders, and conduct of other businesses in the same space.
- Also review applicable insurance policies.

None of these remedies are straightforward to establish and so the risk of unsuccessfully asserting these remedies should be carefully considered, especially given that it might put a party in breach of contract thereby giving its counterparty a right to claim damages or terminate the contract.

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