EVERSHEDS SUTHERLAND

Legal Compass
Contract Law

March 2020

Contractual risks in connection with possible performance difficulties as a result of the coronavirus epidemic – Switzerland

Authors

Peter Haas
Partner

Martin Rauber
Legal Director

The coronavirus continues to spread worldwide and especially in Switzerland. Reports of new measures ordered by governments are currently coming thick and fast, and society has to adjust to even more extensive restrictions.

1. Introduction

Governments in many countries are ordering new measures against the coronavirus epidemic almost on a daily basis, with ever more restrictions on the economy and society. Interventions in the personal freedoms of companies and individuals are also a daily occurrence. This can go so far that contractual obligations can no longer be met.

It is conceivable, for example, that some units of a company may be quarantined or closed by an official order because too many employees are absent due to illness or individual quarantine. As a result, production and the delivery or the provision of services is no longer possible.

Moreover, it is conceivable that only the administration of a company can no longer be active due to official orders and customer orders can no longer be processed.

All these scenarios have one thing in common: the company can no longer meet its contractual obligations or is at least severely impaired in its capacity to do so.

This inevitably raises a number of non-standard legal questions, the answers to which may be difficult to find in individual cases if and to the extent the applicable contract does not cover them. This concerns in particular issues such as default, liability, termination rights, force majeure, etc.

In the following sections, an overview of the legal issues arising in connection with the coronavirus epidemic from the Swiss perspective is outlined.

2. Duty to perform as general principle

In general, the Swiss Code of Obligations provides that a contracting party that has contractually agreed to provide a service must make every effort to fulfil this obligation. Any impediment to the performance of the service, independently of how extensive it may be, thus generally falls within the risk area of the respective contracting party that has undertaken to perform.

Consequently, if a contractual party is unable to provide the contractually owed service on its own, it must examine whether it can procure this service in another way and thus provide it to its contractual partner. For example, it must check whether it can procure the products it is obliged to supply and which it cannot (any longer) manufacture itself due to the coronavirus epidemic by other means. For example, it may be possible to purchase the products in question from a third party. This also applies by analogy to services.

With regard to the above scenario, where the administration of a company is quarantined, the company must examine whether this function can be ensured by other means, for example by working from home. If such alternatives are possible, performance is still possible and the other party can claim statutory and/or contractual default rights in the event of non-delivery or late delivery.

3. Duty to notify and to mitigate damage

It should be further borne in mind that in the event of difficulties to perform the contractual duties or in case that providing services has become more difficult, the company has a duty to notify its contractual partners.

In addition, the generally applicable principle of the so-called duty to mitigate damages must be observed. In the event of an impediment to performance, a company must take all reasonable measures to mitigate any damage to its contractual partners as much as possible.

4. Impossibility to perform its contractual duties

Swiss law distinguishes between the aggravation of performance and an actual impossibility of performance. This distinction can be blurry in practice and in individual cases. If the contractual partner can in good faith no longer be reasonably expected to perform its contractual duties because the obstacle to performance proves to be virtually insurmountable, this is, from a legal point of view, generally considered to be an impossibility.

In such a case, a further distinction must be made as to whether the impossibility is permanent or merely temporary. A temporary impossibility of performance is generally a case of default triggering any applicable statutory or contractual rules (e.g. contractual penalties).

Conversely, a permanent impossibility rather than a temporary impossibility exists if, for example, the end of the impossibility is not foreseeable or if it is certain that the performance of the service will not be possible again before the due date. In the event of a permanent impossibility of performance, the contractual obligation shall be deemed to have expired. Any consideration already received, such as payments on account of the delivery of products, shall be refunded. According to Swiss case law and doctrine, it is not clear whether full restitution is to due or whether restitution must be made only to the extent that the concerned person is still enriched. There is much to suggest that the latter is the case. This also means that in such a case the default rules do not apply. A contractually agreed penalty can therefore not be claimed.

However, the legal situation as summarized above must be assessed differently if the company is responsible for the reason behind the impossibility. This question arises in particular if the company has not done everything in its power to fulfil its generally applicable obligation to perform (see section 2 above). If the company can be held responsible for the impossibility to perform, this constitutes a breach of contract with corresponding liability consequences for the company.

5. Cases of "force majeure"

Contracts often contain clauses that limit liability or provide the parties with the possibility to extraordinarily terminate the contract in the event of "force majeure". The Swiss Code of Obligations also contains a provision which can lead to the termination of the respective contract in the event of force majeure.

Generally speaking, force majeure is defined as unforeseeable and unavoidable events that are not attributable to human conduct, i.e. that are outside the sphere of influence of the parties to the contract, and which are caused by unavoidable force from outside.

The current coronavirus epidemic with its resulting increasingly far-reaching restrictions may fall under this definition under certain circumstances, depending on each individual case. In particular, this implies that the restrictions are still considered unforeseeable. However, this criterion in particular must be critically assessed at the present time and is not necessarily fulfilled when new contracts are concluded, i.e. in the further course of the epidemic (see below, paragraph 6).

6. Increased caution when concluding new contracts

The question of whether an impossibility already exists initially, i.e. at the time of the conclusion of the contract, or whether it occurs subsequently, i.e. during the term of the contract, is of crucial importance. While the Swiss Federal Supreme Court follows the rules set out in section 4 above in the case of subsequent impossibility, a so-called subjective impossibility (existing from the outset) entails major risks for the company. Such a subjective impossibility covers those situations in which the contractual debtor was already unable to perform his contractual duties at the time of conclusion of the contract, while performance was, in principle, i.e. objectively, possible. In such a case, the company can only avoid liability if it can prove that this impossibility is not attributable to it.

In terms of time, it is therefore of great and decisive importance what knowledge a company has of the effects of the coronavirus on its ability to fulfil the contract at the time the contract is concluded. If the company accepts an order and confirms it, knowing that production may have to be stopped or restricted to an extent that production and delivery cannot be carried out in time, the company is generally liable for the consequences of the failure to perform in accordance with the contract. The same applies if the company should have known under the given circumstances that the delivery would not be made on time.

7. Recommendation

It follows from the above that each situation must be considered on a case-by-case basis and in view of the specific circumstances of each case. Nevertheless, some general recommendations can be formulated which every company must implement in the near future.

First of all, depending on the respective business situation, it may be prudent to discuss the situation with the contractual partner and examine how the current situation should be dealt with and, in particular, which measures can be taken jointly to reduce (mutual) losses. If such discussions are not possible or do not lead to an agreement, the company must take measures to enforce its own rights or to defend itself against any claims made against it.

It is therefore strongly recommended that all actions be documented and the appropriate evidence secured in order for the company to be, in the event of a dispute, in the position to prove that it has done everything in its power to avert the negative effects of possible production stoppages or delivery difficulties in connection with the coronavirus epidemic. This evidence can help to prove in a dispute that it was impossible to provide the service (on time) and that the company is not at fault for such impossibility.

In addition, increased caution is required when concluding new contracts during the current coronavirus epidemic. It is therefore strongly recommended that the situations of default, i.e. delay, termination options, cases of force majeure, be clearly and explicitly dealt with in the contract.

8. Frequently Asked Questions

The above makes it clear that the coronavirus epidemic is not a free pass for contractual infringements. But what exactly can a company do if it is suddenly affected? The following FAQs should help you to get concrete answers to some specific questions.

Due to the effects of the coronavirus epidemic, you realize that you will no longer be able to fulfill your contractual obligations. How should you react?

First, the company is obliged to look for alternatives to enable the fulfilment of its contractual duties. Second, you must inform your contractual partner regarding the emerging difficulties in the fulfilment of the contract. All these actions must be documented and the relevant evidence must be secured.

Your customer claims that due to the coronavirus epidemic, he no longer needs a placed order and therefore withdraws from the contract. What can you do?

First of all, it needs to be assessed whether the relevant contract provides for such a termination right and, if so, under what conditions. If such contractually agreed termination rights are missing or if the corresponding conditions for exercising them are not met, the contractual partner cannot, in principle, withdraw from the contract simply because he no longer has a need for the contractual services. In principle, contracts must be fulfilled and the risk of no longer using a contractual service once ordered is legally borne by the purchaser/customer.

You have planned an event which can no longer be held due to official orders. Who bears this risk?

Even if it is officially prohibited to carry out the planned event, the provision of services does not qualify as impossible in every case. For example, the proprietor of the premises can, in principle, still fulfil his obligation to make the premises available to the company as organizer. However, the company may no longer be able to use the service as intended due to the governmental measures. This case differs from the above-mentioned case in that the customer not only does not need the service, but can no longer use it. In such a case it can be argued, namely on the basis of the Swiss Federal Supreme Court's case law, that the performance has become impossible and the concluded contract can therefore be terminated. Any services already rendered to each other must be reimbursed. In legal doctrine, however, there is controversy on this issue (see above, paragraph 4).

You order goods for the purpose of reselling them to end consumers. Now, the authority orders the closure of all shops except grocery stores and pharmacies. Can you cancel the order to save storage costs?

It must be assessed whether the order of the authority is an unforeseeable event. In particular in view of ongoing reporting in the media, the question arises whether the company should have expected such measures. Since, in contrast to the previous question, the company can in principle still use the goods, store them and resell them after the official order has been lifted, it is difficult to argue that it is impossible to fulfil the contract. The situation may be different in the case of perishable goods or goods which cannot be stored (for a longer period of time).

In order to cover such cases, it is advisable to agree and stipulate corresponding rights of withdrawal in the contract.

Your contacts for Contract law

Peter Haas
Partner

T: +41 31 328 75 75
peter.haas@eversheds-sutherland.ch

Daniel Bachmann
Partner

T: +41 31 328 75 75
daniel.bachmann@eversheds-sutherland.ch

Oliver Beldi
Partner

T: +41 31 328 75 75
oliver.beldi@eversheds-sutherland.ch

Sandra Boegli
Legal Director

T: +41 31 328 75 75
sandra.boegli@eversheds-sutherland.ch

Patrick Eberhardt
Partner

T: +41 22 818 45 00
patrick.eberhardt@eversheds-sutherland.ch

Dr. Martin Rauber
Legal Director

T: +41 44 204 90 90
martin.rauber@eversheds-sutherland.ch

eversheds-sutherland.ch