POPOV LAW SERVICES

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Dear Friends,

It hardly makes sense to produce an English version of our "force-majeure legal alert" with references to particular articles of the Russian Civil Code. However, predictably, we received a lot of questions from our clients last two weeks, who ask of Russian law approaches to what is going on. Thus, we suggest you the imitation of typical dialog with a client. Please keep in mind that now we speak of only Russian law.

Is the virus — force-majeure?

In most cases yes, however not the virus, but restrictive measures taken as a governmental reaction to the epidemy. And to the extent, as it directly prevents from contractual performance.

Let's guess, for example, of Russian company RusCo which has taken an obligation to supply anti-virus masks to foreign company ChinCo. Later, Russian Government adopted a Decree which prohibited the export of those masks; in that case RusCo's failure to perform shall be treated as caused by force-majeure, and the company shall not be held liable. Unless…

Saying "force-majeure" in this simple case we should take at least two things into account:

(1) Whether it was possible to predict the restriction at the moment of signing contract. If the companies signed their contract when some countries already adopted similar measures, and reasonable person could expect the same in Russia, than it may not be a force-majeure, but a commercial risk instead.

(2) If for RusCo it was possible to find similar masks in the country of ChinCo, or somewhere, so making the obligation executable, than the criteria "unavoidable" would not work, so that may not be a force-majeure.

Great, but what if RusCo did not supply goods to a Russian customer RusGovCo because RusCo's foreign sub-supplier ChinCo failed to supply, as borders closed?

That changes the previous advice. Russian law specifically provides that sub-contractor's failure to supply shall not excuse from breach of obligations. There is case law confirming that statement.

If the United Nations Convention on Contracts for the International Sale of Goods (1980, Vienna) governed the relations between RusCo and RusGovCo, it could potentially save the situation. However, this is not our case.

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That brings us to one unpredictable thing: either Russian courts (1) will apply the law in the same manner as in previous years, and then RusCo will be held liable; or (2) they will change the approach and say: "RusCo did not supply not because it cannot choose good subcontractors, but because the subcontractor was unable to perform, being excused based on force-majeure". No one can predict how this case law will develop. Further, if the Supreme Court will not issue recommendations promptly, than we will have a chance to see contradicting court practice within a few years.

So… what to do?

Read to the end.

If we lease premises…

… than no virus prevents you from paying the lease fee, unless you do it manually with coins. There may be various situations, but in each case when you want to avoid liability, you have to prove that you were not able to perform specific obligation. By specific obligation we mean: pay, deliver, perform service, etc. (not the whole contract in its entire complexity).

Often question is: what if I cannot pay because my foreign partners did not pay me for force-majeure reason? The answer is more or less predictable. Economic crisis was never a ground for recognizing force-majeure. In this case, breach of contract is caused by economical reasons, but not by governmental prohibition. Look at the same situation from another angle — if one company RusCo1 fails to pay because ChinCo does not pay to it, but at the same time another company RusCo2 (whom ChinCo also owes a lot) has a lot of cash and is able to pay, should we take a different approach to these two Russian companies? The answer is definitely "no".

But still paying for lease is useless, as we do not use most premises, and who knows how we will do in future…

Why you do not use? Because your company decided to send all employees to home office? Or because of governmental prohibition? We mean that effective period of the company's decision may last much longer.

Theoretically, Russian law allows reducing the lease fee if the conditions of using premises become significantly worse. However, nobody knows whether the courts will apply that provision of law to the epidemy situation. Many lawyers expect that not.

But does not a force-majeure event terminate a contract?

Force-majeure only can release from liability but does not terminate a contract. However, a party can terminate the contract unilaterally, if because of the force-majeure that party loses it's interest in a contract.

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For example, from your supplier ChinCo you ordered something for the company's birthday, which you wanted to celebrate on April 01, 2020. ChinCo was unable to deliver because of we all know what. In this case ChinCo shall be released from liability, and you will have a choice:

(1) terminate the contract unliterally, as you will not need that "something" later; or
(2) if you do not so terminate, ChinCo shall have to supply when the borders will open.

An obligation terminates automatically if it becomes impossible to perform. Ever.

More interesting: what if prevention to perform follows from governmental acts (e.g., order of mayor of a town). Yes, this is force-majeure and impossibility to perform. However, if later a court holds that order invalid, the contractual obligation shall survive.

Will force-majeure release us from liability, if we performed mayor's order which was unlawful?

Most likely, yes. Force-majeure is not an order or decree or regulation whatsoever. Force-majeure is a fact of impossibility. In court you will have to prove that you were not able to perform because you had (were forced) to follow that regulation, whether it was lawful or not.

We know that some governmental regulations call the circumstances as force-majeure. However, ultimate legal assessment may make only court.

Does Russian law know Hardship concept?

Yes, it does, with some specific regulation. Briefly: if you can perform a contract, but because of changed circumstances it is extremely difficult to perform, than court may terminate or amend the contract.

A difference from force-majeure event is that in case of hardship it still possible to perform an obligation, although very difficult. The Civil Code suggests four criteria for indicating hardship:

- at the moment of signing no party expected that the circumstances would so change
- an interested party could not manage or overcome the circumstances
- performance of contract on initial conditions significantly will change the balance of contract, and interested party will have a material damage
- interested party shall not bear a risk of changing circumstances, based on contract or respective business practice

In court an interested party shall have to prove that if it knew about changes in circumstances, it would not enter into the contract or would enter on significantly different conditions.

We believe that we will see cases where courts will apply this concept, although we are skeptical about references on "changed market" or "significant decrease of consumption because of epidemy". Our skepticism is based on the fact that Russian courts never recognized economic

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crisis as a hardship. That approach may theoretically change if whole industries will significantly suffer in typical contractual relations, especially if that will have a social effect. In other words, we have one more area of uncertainty.

Further, for certain types of contracts Russian law suggests special regulation. E.g., if in work performance contract price of materials or subcontractors' fees significantly increase, than contractor may claim to increase the work fee; as we indicated above, in lease contract a lessee may require decreasing of the lease fee if conditions of using the premises became significantly worse; etc.

And yet — what to do?

Act. Reaction of normal business to the uncertainties shall be — decrease amount of those and save money as maximum as you can. That requires two simple things: (a) audit of what you have in contractual relations and identify risk zones; and (b) decide for each case whether to negotiate with contractual counterparty, or wait for counterparty's first move. Keep in mind that for application of hardship negotiations are mandatory.

In any case, remember that you should behave in a fair manner. Fairness in business relations Is a very popular concept now with Russian courts, so in almost each case courts test the parties' behavior for fairness. Specifically, your actions, based on the audit, may include (but not limited to):

(1) inform your counterparty of force-majeure event within contractual (or reasonable, if the contract is silent) term; do all legal notices in time (e.g., notice of termination)
(2) assess whether you want to receive your counterparty's performance; whether your counterparty may lose an interest in your performance — then discuss with lawyers if it makes sense to initiate negotiations
(3) if you want to terminate a contract for force-majeure, do not confirm your interest in that contract by performing it (e.g., by accepting goods) or otherwise

Definitely, advice here is a "general theory of the universe" because all practical cases are different, a one minor detail in a case can dramatically change the approach.

We believe that our summary was useful for initial understanding of how to react on the situation. Needless to say, should you have any questions, please do contact us at any time at law@popov-law.com

At your service,
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