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Impact of COVID-19 legislative changes: Contracts and coronavirus – Initial considerations under Mexican law

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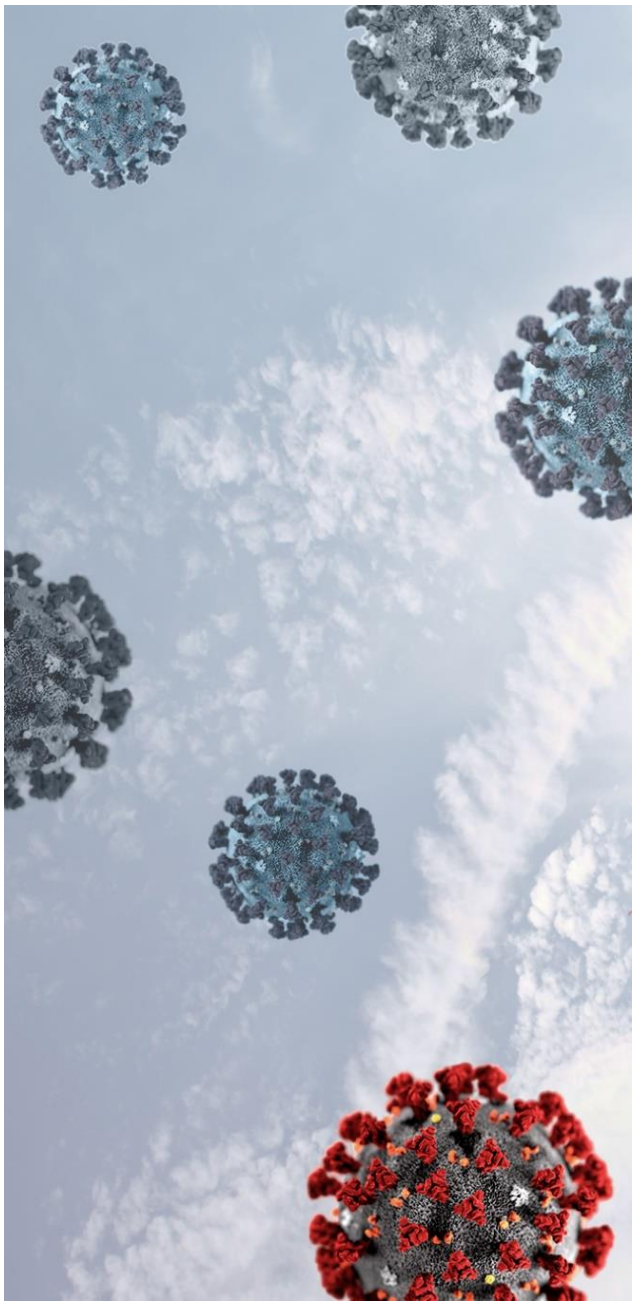

With the spread of coronavirus (COVID-19) across borders, concern over the effects of the outbreak on commercial contracts has led to a growing sense of urgency and a spate of requests for legal advice.

When it comes to commercial and business relationships, the impact of COVID-19 is unquestioned, and as such, it must be assessed on a case by case basis. However, certain key concepts should be considered when assessing such impact, at least, when Mexican law comes into play: force majeure and rebus sic stantibus clauses.

Besides the effect of coronavirus outbreak on commercial law relationships, possible repercussions on labor relationships and public law also need to be considered in light of the legislation and specific case law.

Concern over the impact of the coronavirus outbreak in China on commercial contracts has been steadily rising since news of the disease broke late December last year. With the cross border spread of the virus, the number of cases has greatly increased in countries doing business with Mexico, such as Spain, Canada or the United States, the cancellation or postponement of events, and the impossibility to fulfill certain contractual obligations, results in a growing sense of urgency and a spate of requests for legal advice.

The effect of the coronavirus on commercial relationships is unquestioned. What is not so clear, perhaps, is the appropriate legal response to instances of frustration of commercial relationships stemming from the outbreak. Though each case needs to be considered individually, Mexican contract law does contain certain key concepts to bear in mind.

Force majeure: contractual provisions

Normally, force majeure is considered, contractually, as a limitation of liability. However, regard should be taken to the relevant contractual provisions that could define whether the specific circumstance amounts to a contractual force majeure, independently from the legal definition of force majeure, entitling a party to refrain from fulfilling its obligations. This is noteworthy because certain force majeure cases could be considered as excluded from those limiting liability depending on the wording of the relevant clause.

In some cases, the possibility of arguing a force majeure case is subject to the respect of certain formalities such as time frames and notification processes established in the contract. Failure to duly notify on time a force majeure event could bar the affected party to rely upon said force majeure.

Another relevant aspect to bear in mind is the consequence of arguing a force majeure case as it could allow the affected party to limit its liability, or even terminate the contract. However, if the sought remedy is not appropriate, the affected party could be held liable for damages.

Force majeure under Mexican Law

Mexican law recognizes two categories of cases limiting liability: fortuitous and force majeure events. Fortuitous cases are originated by men, while force majeure events are originated by nature. In both cases, the relevant circumstances must constitute an unforeseeable, general (except when it relates to the execution of a personal fact), absolute and, sometimes, definitive

obstacle. Regardless of the meaning in which the expressions “fortuitous event” or “force majeure event” are taken, their legal effects remain the same.

Section 2111 of the Federal Civil Code regulates fortuitous events: *"No one is bound to the fortuitous event except when he has given cause that contributed to it, when he has expressly accepted that responsibility, or when the law imposes it."*

Similarly, fortuitous events, as a grounds for exoneration of liability in international sales of goods, is regulated under article 79.1 of the Vienna Convention of 1980 (ratified by Mexico): *"A party is not liable for the failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control and that he could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract or to have avoided or overcome it, or its consequences."*

Although the parties are bound to fulfill their obligations stemming from the contract[1], no one can undertake what is impossible to perform, e.g., in the circumstances of force majeure. Mexican law considers fortuitous event as any event that, though foreseeable, is unavoidable or irresistible for the parties and results in frustration (even if only temporary) of the obligational relationship. Depending on the case, force majeure or fortuitous event will excuse the obligor from liability for breach, will discharge it from performing its obligations, or will suspend performance of the obligation if the effects of the force majeure event are temporary.

Whether the recent coronavirus outbreak constitutes a fortuitous event discharging contractual liability, releasing parties from having to perform a contractual obligation, or allowing performance to be postponed is a question that will have to be decided upon assessment of the specific nature of the obligational relationship, the wording of the contract, the circumstances existing at the time of frustration (including the state of knowledge concerning the outbreak, the measures taken or official recommendations followed, and the location), and in particular the degree to which the event was foreseeable or unavoidable by the parties in each individual case.

Rebus sic stantibus clause

Where the individual circumstances of the case do not allow the event to be classed as a fortuitous event, the parties could still consider whether other provisions laid down by some local

[1] Article 1796 of the Federal Civil Code.

civil codes, such as the one governing in Mexico City, might be relied upon, in particular the *rebus sic stantibus* clause.

Generally speaking, this rule holds that contracts may be revised or terminated where nationwide supervening changes in the circumstances extant at the time they were originally agreed upon, upset the balance between the contracting parties, making performance by one to the other unduly burdensome.

As to date, Mexican case law has interpreted that *rebus sic stantibus* clauses are not applicable for commercial acts and contracts whose governing law does not expressly include such provision (e.g. agreements under the Federal Civil Code). Nevertheless, a case by case assessment may be required in order to determine the governing law to each contract. Even in cases where said remedy is set forth in the law, such as Mexico City`s Civil Code, the nature of the contract and a shortened statute of limitations must be taken into account in order to obtain a favorable judicial ruling revising or terminating the contract.

Lastly, in addition to the effect of the coronavirus outbreak on private law relationships, possible repercussions on labor relationships and public law will also need to be considered in light of the legislation and the case law specific to those domains.

Conclusions and recommendations

The feasibility of relying on either of the remedies discussed above in cases of breach or expected breach of contract will depend on the nature of the contract and its contractual provisions, the governing law, the impact of the outbreak on performance, and the specific measures taken, all in the context of location and the economic sector concerned.

In view of the wide range of scenarios that could arise, we would recommend taking the following steps without further delay:

- Conducting an internal review of any potential or prospective disruption that might affect performance of contractual obligations, separately by contract and by each individual obligation. In this respect, a fundamental aspect will be to consider whether the parties have stipulated any specific terms applicable to events of this nature and, if so, what obligations were established and what were the (contractual) expectations of each party.

- Considering the advisability of notifying the contracting parties of any outbreak-related contingency that could potentially prevent performance of the contractual obligations. The

wording of notices of this kind will play an essential role in minimizing losses and potential consequences, and we would therefore recommend obtaining specialized advice when notices are being drafted.

- Gathering as much supporting evidence as possible attesting to the existence of the circumstances preventing performance of the contractual obligations and to the measures that have been taken to mitigate potential harm, even if such circumstance has seized.

- Evaluating the impact of any potential or prospective disruption in the performance of the contractual obligations on labor and public law relationships, which need to be considered separately since they are governed by their own bodies of law and case law.

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