MEMORANDUM

Subject*: 10 Q&A: The Effects of COVID-19 on Contracts*

1. WHAT IS FORCE MAJEUR AND FRUSTRATION?

In the simplest term, force majeur means “compulsory case”. The concept of force majeur is not defined under Turkish Code of Obligations (“**TCO**”). The conditions of force majeur are determined by Supreme Court precendents. Accordingly, the case which would be determined as force majeur must be (i) inevitable, (ii) irresistible, (iii) unpredictable and (iv) non-responsibility of any parties (no party has fault on occurrence of case/damage.)

Frustration is the case that inevitably causes the debtor to violate his obligation separately from his will and his behavior in the contractual relationship. For this reason, every force majeur case includes frustration however not every frustration case can be qualified as force majeur.

In respect to results of both concepts, it is necessary to assess as to whether the performance of the obligation will be performed sooner or later in the contractual relationship. In case the obligation can be performed **sooner or later,** in other words, non-performance situation is **temporary**, it will become necessary to refer frustration considering the concrete case.

Either a fact causes a **permanent** non-performance of an obligation or a fact causes a temporary impossibility of performance/ to make it excessively difficult to perform, respectively this will referred to force majeur and frustration.

2. IS COVID-19 FORCE MAJEUR OR FRUSTRATION?

Consequently, in case COVID-19 permanently makes the obligation impossible to perform, it may be referred to force majeur or in case it does not make the obligation impossible to perform/ temporary makes the obligation to perform may be referred to frustration. The results of force majeur and frustration are different from each other and will be explained below.

3. DOES THE PRESENCE OF FORCE MAJEUR MAKE THE CONTRACT PER SE INVALID?

There is a misperception in our society which remains as follows; in case a fact - that may be worded as force majeur - occurs, parties would discharge from their obligations/ contract would be terminated/ be pending directly.

However, the results of force majeur may differ depending on the nature of the fact. It is very important to note that the matter that one fact only has the conditions in the 1st Q&A may not directly name it force majeur. It is widely recognized that whether a force majeur is present or

not which shall discharge from obligation can only be decided by taking into consideration of all nascency conditions of the fact.

For instance, as per Supreme Court decisions, even though a flood is accepted as a force majeur, a packing house which is constructed on stream bed and its causes cannot be formed as force majeur. Similarly, in case a supplier commits to keep average number of orders - which were ordered in the past - during the commercial relationship from the beginning of the year, any fact as earthquake, war, military coup etc. which shall be formed as force majeur for the third parties, may not be considered as force majeur.

Even though the facts in both examples are conceptually considered as force majeur, suitable causal link between force majeur and its effect on performance and the fault of debtor shall be examined separately case by case.

It is crucial to note that, especially for the merchants, the conditions of force majeur are considered in a very limited scope by Courts.

4. WHAT ARE THE RESULTS OF NOT HAVING "FORCE MAJEUR" CLAUSE IN A CONTRACT?

In a contract; examples, conditions and consequences of force majeur may not be regulated. Even in this case, as far as it provides the requirements, a fact may be considered as force majeur and the parties may benefit from the rights which are granted them on the grounds of force majeur.

5. IN A CONTRACT, DOES IT CAUSE A LOSS OF RIGHT BY NOT COUNTING THE OUTBREAK OR SIMILAR EXPRESSION AMONG FORCE MAJEUR FACTS?

The parties may decide on contract to consider which facts shall be named as force majeur. In this case, facts other than these ones included in the contract shall not be considered as force majeur. (Supreme Court Assembly of Civil Chambers, Decision Date: 6.12.2017, Docket No: 2017/15-2821, Decision No: 2017/1552) In case, all force majeur facts are counted one by one not but the outbreak or contagious disease as force majeur, there is a possibility that COVID-19 may not be counted as force majeur.

Howsoever it is understood from the literal meaning that the counted facts under force majeur clause are regulated as sampler and the outbreak or contagious disease are not indicated, COVID-19 may be accepted as a fact of force majeur.

For instance, in case of a clause similar to the one below, COVID-19 may be considered as force majeur.

"…*In terms of this contract, the force majeur clause includes the facts which influence the performance of the Contract, acts of out of reasonable control by the party who will perform, facts and specifically included the ones below but not limited to.*"

Consequently, in case facts of force majeur are counted in the contract and outbreak is not mentioned in the contract then COVID-19 may not be considered as force majeur.

6. IN CASE THE CONTRACT CONTAINS OUTBREAK OR CONTAGIOUS DISEASE CLAUSES, WOULD FORCE MAJEUR PER SE BEARS ITS LEGAL CONSEQUENCES?

Essentially, the answer to this question is given in the 3rd Q&A of this information note. The party claiming force majeure shall be free from the burden of proof as long as outbreak or contagious disease are counted in the contract under force majeure clause.

In other words, it would not be necessary to prove whether the outbreak or contagious disease is a force majeur. Thus, as it is mentioned above, the force majeur may differ by considering every conditions of each case (e.g. flood case). However, outbreak and contagious disease are counted as force majeur in the contract, shall be accepted directly as force majeur without any further assessment.

Nevertheless, the claimant affected by the force majeur has to prove the causal link between non-performance and force majeure and, in any case he/she has to fulfill his/her obligations of notification.

7. HOW TO TAKE A STEP IN CASE THERE IS A PROVISION ON GOVERNING LAW WHICH ALLOWS YOU TO APPLY FOREIGN LAW?

The parties to a contract may have decided to apply a foreign law instead of Turkish law in case of a conflict.

Turkey is one of the members of CISG (Convention on International Sales and Goods). Therefore, in case a company resides in Turkey draws up a contract between a company which reside in another CISG member country – specifically not mentioned that CISG provisions shall not be applied – the Court has to apply CISG provisions. At that, the definition and conditions of force majeure should be assessed within the scope of Art.79 of CISG.

8. IS IT MANDATORY TO NOTIFY IN CASE OF FORCE MAJEUR?

In general, in case of force majeur, contracts lay a burden of liability of notification to the affected party who fails to perform his/her obligation and this notification has to be done immediately to the other party. The purpose of the notification is to allow the other party to take the necessary measures.

The fact that the force majeur is a pandemic/epidemic like in our case and the fact that it is known in all over the world does not put the liability of notification away. As it is mentioned, the purpose of this notification is for submitting to take necessary measures by creditor, the party who fails to perform his/her obligation is charged with this liability of notification.

In accordance with Art. 136/III of TCO, *"However, unless the obligor dully and timely notifies the creditor on the impossibility of the performance of the obligations and takes necessary precautions to prevent the increase of loss, the obligor shall be liable for the compensation of the resulting losses."* is regulated.

9. WHAT ARE THE LEGAL CONSEQUENCES OF FORCE MAJEUR?

A case that may be regarded as a force majeur may result in (i) impossibility of performance (ii) partial impossibility of performance

(i) Impossibility of performance: as a result of force majeur, perform of debt can be **permanently** impossible. Permanent impossibility is being unable to perform the debt since it is not possible to overcome obstacles in front of performance. For instance, in case it is decided to ban the production of a raw material because of COVID-19, this may result in an impossibility of performance for the importer. On the other hand, in case the prohibition is temporary, hardship may come to the agenda instead of impossibility of performance.

In case of impossibility, the debtor / contractor discharges of his/her debt.

(ii) Partial impossibility of performance: As a result of the force majeur, performance of the essential obligations under a contract may become partially impossible as well as totally impossible. In this case, partial impossibility may arise. Often partial impossibility occurs in quantity. In the example of Chinese government banned the production of raw materials, above mentioned, in case the manufacturer has delivered 750 tons of the goods out of the 1.000 tons before the ban to the importer in Turkey, it is considered as partial impossibility of performance for the remaining 250 tons.

In case of partial impossibility of performance, the debtor is discharged from the obligations which became partially impossible. In this regard, the importer pays price of only 750 tons, does not pay the price of 250 tons. However, in case it is understood from the intention of the parties that such contract would not be drawn up so that all the obligations would be ceased. For instance, as mentioned above, in case 1.000 tons of raw materials would not be supplied and the supplies could not be launched to the market, as a result of this, the obligation shall be ceased. In other words, the importer who ordered 750 tons does not pay the cost and in case of prepayment, he/she shall ask for the return of this payment.

10. WHAT ARE THE CONSEQUENCES OF FRUSTRATION? IS IT POSSIBLE REFORM OR CANCEL THE PENAL CLAUSE?

In case of describing a fact as frustration, it is necessary that the subject matter of the obligation is not permanently impossible or temporarily impossible or new conditions as to be put on subject matter of the obligation has to be against good faith.

The frustration may be referred to the case when an extraordinary fact occurs that parties would not have predicted or that is not possible to expect them to have predicted while conducting the contract and this fact is not occurred because of debtor's faut.

When the debtor/affected party fails to fulfill the commitment under the contract because of frustration is called as "**hardship**". The main difference between the "hardship" and "impossibility of performance" is that; the fulfillment is not impossible; it becomes difficult in case of hardship. For instance, a technology company cannot supply spare parts - which are ordered by its customers – from abroad because of COVID-19. In fact, it is possible to supply spare parts since it is not banned. However, this unexpected situation did not permanently make the supply impossible.

It should be emphasized that; in some cases, it may be unclear when the temporary impossibility will come to an end, or in case the debt is not performed on maturity date the fulfillment loses its economic value. In these cases, even though performance becomes too difficult, it will result in the hardship.

In some cases of hardship, asking the debtor to fulfill the performance may be a violation of rule of good faith. It is contrary to rule of good faith to ask from the technology company –as in the above example - to supply the spare parts for 3 times more expensive than the price of the produced in China from another country and moreover without increasing the contract price.

As a result, in case the COVID-19 does not make it impossible for the parties to contract, but makes it difficult to perform, the affected party may apply to the court and request that the contract be adapted to the new conditions. Therefore, it will be possible to contract price, delivery time, similar product to be supplied reduce or cancel the penal clause. For instance, the technology company may request to increase the contract price up to 3 times or delay the delivery date for 3 months and in case of a delay starting after 3 months, the penalty clause will be reduced from 5,000 Euros per day to 100 Euros. Of course, the customer may not accept such costs or new terms. The Court may adapt the contract to the new conditions according to the requests of the parties. In case there is no possibility to adapt, the parties have right to terminate the contract.

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