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krfacts

COVID-19: contract law and Federal Emergency ordinances

Special Edition on co ntract law and bridging loans:
The coronavirus (COVID-19) and the associated conditions give rise to new legal questions, the answers to which pose a difficult challenge for experts. In view of the highly complex situation, our goal is to provide information on the legal issues as simply as possible. In this special edition of krfacts, contract law (I.) and the bridging loans granted by Federal Council Ordinance (II.) are presented.

On 20 April 2020, the COVID-19 Ordinance, which was passed by the Federal Council, also came into force. This contained a provision supplementing the Credit Ordinance discussed in the present case with regard to the joint and several personal liability of the borrower's executive bodies and persons involved in the management or liquidation of the company. The present krfacts is therefore dealt with in Chapter II. No. 6.

Translated with www.DeepL.com/Translator (free version)

I. Contract law

Pursuant to Article 185 of the Swiss Federal Constitution, the Federal Council is able to take action to safeguard internal security and for this purpose to issue ordinances and orders. It has done so by issuing the COVID-19 Ordinances, which have implications on contractual performance.
The primary question of interest is what the consequences are of the failure to provide the contractually owed service if the failure is due to COVID-19.

If an event is cancelled or a contractual partner is unable to provide the agreed service, a question arises as to what should happen. Who must be required to bear the resulting losses?

Swiss law incorporates the principle of "*pacta sunt servanda*", i.e. contracts must be honoured. The risk of a change in circumstances must in principle be borne by the party that is affected by the adverse consequences. However, this principle is not absolute. It may be set aside by *force majeure* or an unforeseeable change in circumstances. The following aspects must be examined:

1. Examination of the contract or the general terms and conditions

The first step is to check whether a contract or (validly accepted) general terms and conditions contain a *force majeure* clause or provisions governing any other change in circumstances. If so, the contractual terms apply. It has not yet been conclusively clarified whether the Coronavirus constitutes a *force majeure* occurrence, although this is generally considered to be the case. The answer will be more clear-cut if the contract expressly refers for example to an "epidemic", "pandemic" or "governmental decrees". If there is a *force majeure* clause and that clause is applicable, consideration must be given in particular to any contractual notification duties.

2. Non-contractual force majeure

Even if not expressly provided for under contract, the doctrine of *force majeure*, which is not expressly regulated under Swiss law, may be applicable with reference to the notion of "good cause" or "impossibility". If the contract itself does not contain any such stipulation, the specific provisions of the Swiss Code of Obligations (CO) apply on a subsidiary basis; these include for instance the provisions governing "good cause", where an option for termination is often envisaged. In the event that performance has become definitively impossible, Article 119 CO will ultimately apply, according to which an obligor is not required to perform where performance has become impossible through no fault of the obligor. Under bilateral contracts the requirement of reciprocal performance also lapses, without any obligation to pay damages owing to the absence of fault.

3. "Clausula rebus sic stantibus"

If performance has not become definitively impossible, where not expressly provided for under the contract, here too the specific provisions of the Swiss Code of Obligations apply on a subsidiary basis. In such cases the rules applicable in relation to default will be engaged in the first instance, i.e. the obligee is required to set a reasonable grace period to the obligor in order to perform (Article 107 CO); it is unclear how long this grace period has to be in circumstances falling under the COVID-19 Ordinances. Here too, other specific provisions of the Swiss Code of Obligations, such as those concerning "good cause", apply alongside or instead of the consequences of default. Finally, the doctrine of "*clausula rebus sic stantibus*" may also apply. This legal institute allows a contract to be adjusted in the event of a change in circumstances that was not foreseeable and that causes a serious disruption of the contractual equilibrium, i.e. a major imbalance between performance and consideration.

4. Caution when concluding new contracts

If contracts are concluded at this point in time, that means after the beginning of the COVID-19 crisis, the parties will have to assess their ability to perform precisely. If they cannot fulfil their obligation to perform due to the measures taken by the Federal Council, they may be liable for damages. This is because, given the current awareness of the crisis, an impossibility of performance attributable to COVID-19 could possibly be regarded as self-inflicted.

It is a complex matter to identify the specific legal position in any given situation, and the outcome will depend upon the specific individual circumstances. It is therefore recommended that the individual circumstances of the case be analysed in detail.

For legal questions regarding rental contract law, please refer to the Special Edition krfacts "Real Estate", for legal questions regarding employment contract law, please refer to the Special Edition krfacts "Employment issues", both dated 09 April 2020, which can also be viewed and downloaded at www.krlaw.ch.

II. Bridging loans based on the Federal Emergency ordinance

The aim of bridging loans (COVID-19 loans) is to enable affected companies to ensure that they have sufficient liquidity with as little red tape as possible. Applications may be filed until July 31, 2020. The competent Federal Departments have created a homepage here[1] through which loan applications can be submitted.

Loans cannot be granted under certain circumstances. If a loan is granted, certain duties must be complied with, whilst a number of specified acts ("prohibited acts") must be ceased and desisted from (see section 6. below). If a loan is obtained on the basis of false information or any prohibited acts are carried out, a fine of up to CHF 100,000.00 may be imposed.

1. Two types of loan

Under the joint and several loan guarantee scheme, a distinction is drawn between interest-free loans of up to CHF 500,000.00 ("joint and several loan guarantees with simplified requirements") and loans of more than CHF 500,000.00 at an interest rate of 0.5% per annum ("other joint and several loan guarantees"). Both types of loans are granted for a term of 60 months, i.e. five years, with an option to extend for a further two years in situations involving particular hardship case.

It should be noted that the rate of interest is not fixed over the entire term and the Federal Department of Finance is able to adjust the interest rate on March 31 of each year, for the first time on March 31, 2021.

Up to the CHF 500,000.00 threshold, loans are granted exclusively on the basis of a declaration by the applicant, whilst for other joint and several loan guarantees a standard sectoral credit check is carried out by the bank prior to disbursement.

2. 10% of revenues or the "start-up" rule

A joint and several loan guarantee is available for up to 10% of 2019 revenues, based on the definitive or provisional 2019 financial statements; where these are not available, the calculation is based on the 2018 financial statements instead. This means that, for revenues of CHF 2.0 million, a loan of CHF 200,000.00 would be available.

For start-ups (start of business operations between January 01, and February 29, 2020, or incorporation during 2019 with an extended financial year), revenues will be assumed to be triple the net payroll bill for a financial year, subject to a minimum of CHF 100,000.00 and a maximum of CHF 500,000.00. The available loan will thus be between CHF 10,000.00 and CHF 50,000.00 (10% of these notional revenues).

[1] https://covid19.easygov.swiss/

3. Loans of up to CHF 500,000.00

The following prerequisites must be met for loans of up to CHF 500,000.00:

- sole tradership, partnership or legal entity based in Switzerland;
- statement by the applicant that:
  - he/she/it started trading before March 01, 2020;
  - no bankruptcy or debt restructuring procedures are pending at the time of the application;
  - revenues have been significantly affected by the COVID-19 pandemic;
  - no liquidity supports have been received under the emergency regulations in the area of sport and culture.

4. Loans above CHF 500,000.00

The following prerequisites must also be met for loans above CHF 500,000.00 and up to CHF 20.0 million:

- the applicant has an enterprise identification number;
- the bank has carried out a standard sectoral credit check with a positive result and has confirmed this decision to the loan guarantee organisation.

5. No loans available

No loans will be granted to companies that earned revenues in 2019 of more than CHF 500 million. In addition, no loans will be granted for the purpose of investment in fixed assets, although this rule does not apply to replacement investments, which are permitted.

6. Duties and sanctions in the event of non-compliance

If a loan is granted, the borrower is obliged under the terms of the loan agreement with the bank to cease and desist from certain activities. Any breach of these duties is punishable (fine of up to CHF 100,000.00), if not a prevailing criminal act of the Swiss Criminal Code is applicable (e.g. forgery of a document, fraud etc.).

The following acts, which are presented in abbreviated form, are prohibited until the loan has been repaid in full:

- the distribution of dividends or bonuses to the Board Members and capital investments;
- the granting or refinancing of private or shareholder loans;
- the repayment of group loans; and
- the direct or indirect transfer of such loans to related group companies outside Switzerland.

The COVID-19 Regulation on Insolvency Law introduces in its Art. 21 for the joint guarantee credit the personal and joint liability of the organs and the persons involved in the management or liquidation. This applies to the damage caused by the unauthorised use of the credit by one of the above-mentioned prohibited acts (Art. 6 of the COVID-19 Solidarity Guarantee Ordinance). The obligation to pay damages exists vis-à-vis the creditors of the company, the lending bank, the guarantee organisation as well as vis-à-vis the Federal Government itself. Therefore Art. 18a «Liability» was inserted in the COVID-19 Solidarity Guarantee Ordinance.

7. Capital loss and over-indebtedness

Until March 31, 2022, the loans up to CHF 500,000.00 granted under the joint and several loan guarantee scheme will be disregarded for the purpose of calculating any capital loss or over-indebtedness (cf. Article 725 of the Swiss Code of Obligations [CO]).

III. Further questions

Due to the developing situation and the different circumstances of each individual case, we recommend that you contact us with any legal questions.

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