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Law of Contracts in Times of Covid-19 Pandemic: Polish Report

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Law of Contracts in Times of Covid-19 Pandemic: Polish Report

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As the world struggles with the Covid-19 pandemic, the debtors try to perform their contractual obligations despite the hardship it brings about. In the meantime contract lawyers are focused on trying and finding remedies that would help face the new circumstances. The remedies that enable the parties either to modify the contract or to bring it to an end seem the most apt solution in the context of current pandemic. Having said that, two provisions of the Polish Civil Code are to be considered, namely article 475 (read in conjunction with the article 495) and 357[1].

The first one covers the issue of the so called impossibility of performance. According to the article 475, in the case of the subsequent (supervening) impossibility of performance – that is where the impossibility occurred after the contract was formed – the debtor is released from their duty to perform. Once the contract performance becomes impossible the contract is terminated automatically. This is true not only for contracts giving rise to unilateral obligations. Despite the fact that the article 475 confines the above-mentioned effect to such contracts (as due to systemic interpretation directives it is said to be applicable only to them), the article 495 of the Polish Civil Code leaves no doubts that the effect of automatic termination is also valid in the case of mutual contracts. This is clear in the light of § 1 of the article 495 as it provides that in the case of impossibility of performing the obligation by any of the parties to a contract, both parties are discharged and thus

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the contract is terminated in its entirety[1]. However, according to Article 495 §2 where the obligation is mutual and one party's performance has become partly impossible, this party is no longer entitled to receive the other party's performance in the appropriate part. The other party may rescind the contract if the partial performance would inflict the nature of the obligation or the purpose of performance known by both parties.

The termination upon impossibility of performance analysed in this report comes into play where the impossibility cannot be attributed to either party to a contract (that is the impossibility is not caused by any fault, be it intentional or negligent actions or omissions of the parties). There is no doubt that in the context of Covid-19 pandemic debtors will have no problems with demonstrating that this condition is fulfilled. The same holds true for another prerequisite of application of the article 475 or 495, namely the requirement that the impossibility of performance be objective. In contrast to the so called subjective impossibility of performance – which occurs where a contract is not possible to be performed by a given debtor – the impossibility in the meaning of articles 475 and 495 must be objective, which entails that the impossibility goes to the essence of the contract (its very nature) and is not due to the circumstances concerning the debtor[2].

In the Polish Legal writing two types of objective impossibility are distinguished: factual (or physical) and legal. The former occurs, for example, when the object of performance ceased to exist (i.e. got destroyed) or actions constituting performance became factually impossible for any other reason. Whereas the latter is linked to the legal context and may be the case where in order to perform the contract (to avoid the breach) actions would have to be taken by the debtor that are not in line with the law, which is in place at the moment when the performance is due[3]. The nature of obstacles such as supply chain shortage, absence of employees (e.g. due to special parental leaves) or legal limits imposed by special legislation (e.g. restricting free movement, banning from rendering services or travelling abroad) make both legal and factual impossibility of performance likely to be invoked by debtors seeking effective defence. Whether they can succeed in raising it, is, however, conditioned on whether impossibility can be considered permanent.

In the case law it is unanimously held that impossibility of performance in the sense of articles 475 or 495 of the Polish Civil Code is to be ascertained only if it is permanent, as opposed to temporary impossibility which does not trigger remedies spelled out in the provisions under scrutiny[4]. At the first glance it may seem that the condition of impossibil-

[1] Krzysztof Zagrobelny in Edward Gniewek, Piotr Machnikowski (ed), 'Kodeks cywilny. Komentarz' (C.H. Beck 2019) 1119; Fryderyk Zoll, 'Wykonywanie i skutki niewykonania lub nienależytego wykonania zobowiązań' in Adam Olejniczak (ed), System prawa prywatnego. Prawo zobowiązań – część ogólna (C.H. Beck 2014) 1160.

[2] See Piotr Machnikowski, Justyna Balcarczyk, Monika Drela, 'Contract law in Poland' (Wolters Kluwer 2011) 132.

[3] Bogusław Lackoroński in Konrad Osajda (ed.) 'Kodeks cywilny. Komentarz' (C.H. Beck 2020); see also Piotr Machnikowski, Swoboda umów według art. 353[1] KC. Konstrukcja prawna (C.H. Beck 2005) 194.

[4] See Supreme Court 5 December 2000, V CKN 150/00 and 15 November 2013, V CSK 500/12.

ity of performance being permanent is not fulfilled in the majority of situations analysed in this paper, for obstacles linked to the Covid-19 pandemic will hopefully end within the time of a few months. However, one should bear in mind that whether impossibility of performance is permanent is to be decided in respect to given contract by taking into account its purpose and the type of performance due[5]. "Permanence" is a term with no fix, objective meaning and thus the requirement denoted by it may be met even where in a given case impossibility is of rather short duration.

Historically the provisions on impossibility of performance were given extensive interpretation. Some authors claimed that they are applicable not only in the case of actual impossibility and spoke in favour of broadening their scope of application to situations were performance, although possible, would be impractical because of excessive cost or excessive burden of performance[6]. This approach can be viewed as a substitute for traditional contract law figures similar to *frustration of purpose* in common law, *Wegfall der Geschaeftsgrundlage* (*§ 313 of BGB*) or *eccesiva onerositá* (article 1467 of the Italian Civil Code) which the Polish Law has not had in place for a long period of time. This changed in 1990 with the passing of the amendment of the Polish Civil Code which introduced the so called *rebus sic stantibus clausula* (article 357^1 KC) into the Law of Contract. As a consequence, the above-mentioned lacuna seems filled in and extensive interpretation of the provisions of impossibility of performance is no longer legitimate[7].

The article 357^1 provides the parties to a contract with special remedies. Namely, it enables them to claim the modification or termination of the contract where due to extraordinary change in circumstances, the performance of the contract becomes excessively onerous or would threaten one of the parties with substantial loss that the parties did not foresee when concluding the contract. Thus the article 357^1 covers instances where the performance of contract would meet an essential hardship, but would still be possible (and consequently could not be terminated upon the articles 475 and 495).

The termination or modification of the contract on the basis of article 357^1 does not operate *ex lege*. It is consequent upon an order which the court is empowered to issue after one party to a contract files a respective motion[8]. In contrast to some legal systems (see e.g. the article 1467 of the Italian Civil Code), article 357^1 is not *expressly* confined to long-

[5] Machnikowski (n 3) 195.

[6] See Biruta Lewaszkiewicz – Petrykowska, 'Niemożliwość świadczenia następcza' (1970) 4, Studia prawno ekonomiczne 80; Kazimierz Kruczalak, Skutki niemożliwości świadczenia według prawa cywilnego (Wydawnictwo Prawnicze 1983) 50.

[7] Zdzisław Gawlik in Andrzej Kidyba (ed.) 'Kodeks Cywilny. Komentarz. Tom III. Zobowiązania. Część Ogólna' (Wolters Kluwer 2010) 628; Zagrobelny (n 1) 1079; see also Piotr Machnikowski in Edward Gniewek, Piotr Machnikowski (ed), 'Kodeks cywilny. Komentarz' (C.H. Beck 2019) 804.

[8] Under Article 357^1 of the Polish Civil Code, if, following an extraordinary change of circumstances, the performance would be faced with excessive difficulties or threaten, which the parties did not foresee when concluding the contract, the court may, after considering the interests of the parties, define the mode of performing the obligations and the degree of the performance, and even decide upon termination of the contract, in accordance with the principles of

term contracts or contracts giving rise to continuous or periodic obligations. However, as a matter of fact it is applicable mostly to such contracts, for in the case of spot contracts there is very low probability for them to be affected by any change in circumstances[9]. Neither the provision at stake excludes its application to gratuitous contracts (contracts giving rise to unilateral obligation)[10].

The formulation of article 357[1] leaves no doubt that it is only applied to contracts and no obligations arising under unilateral juridical acts are covered by this provision[11]. The court's power to modify or terminate the obligation under article 357[1] cannot be extended to extra-contractual obligations, e.g. obligations which arise by operation of law (i.e. the obligation to reverse an unjustified enrichment or to pay damages for loss caused to another)[12]. Moreover, the court will have no power to vary or terminate the contractual obligation under article 357[1] where the debtor assumed the risk of the change of circumstances either expressly (e.g. by inserting a hardship clause or similar terms into the contract) or impliedly (if the debtor is to be deemed to have assumed this risk because of the purpose or the nature of the contract, especially when it is of speculative character)[13]. For the remedies provided in the article in comment to arise, the performance of contract must be affected by a change of circumstances which can be considered exceptional (extraordinary). The risk of natural changes in circumstances that influence social and economic life (e.g. variation of market prices which are normal in market economy) is to be borne by parties to a contract and no remedy is available if such changes occur. Another requirement that needs to be met for the article 357[1] to apply is the requirement of unforeseeability. In the Polish Law of contract it is referred rather to the way the change of circumstances affects the contract than to the change itself. In practical terms it means that the remedies spelled out in the article 357[1] may be triggered only where the parties to a given contract did not foresee (and could not reasonably be expected to have foreseen[14]) that the change in circumstances which materialised would have made the performance of their contract excessively onerous or would put one of them under the risk of substantial loss. Approached in this manner, the requirement at hand may well be fulfilled even if the parties predicted (could have predicted) the change of circumstances itself[15]. As a conse-

community life. When terminating the contract the court may, as far as necessary, decide upon a settlement of accounts being guided by the principles specified in the preceding sentence.

[9] Adam Brzozowski, Wpływ zmiany okoliczności na zobowiązania. Klauzula rebus sic stantibus (C.H. Beck 2014) 127; Machnikowski (n 7) 710.

[10] Mirosław Bączyk, Leopold Stecki, 'Darowizna' in Jerzy Rajski (ed), System prawa prywatnego. Prawo zobowiązań – część szczegółowa (C.H. Beck 2018) 404; Brzozowski (n 9) 126.

[11] Brzozowski (n 9) 126.

[12] Brzozowski (n 9) 141.

[13] Machnikowski (n 7) 710; Brzozowski (n 9) 128.

[14] See Supreme Court 21 November 2011 r., I CSK 727/10.

[15] Brzozowski (n 9) 164; Machnikowski (n 7) 714.

quence disputes that are going to be resolved by applying the article 357[1] will be decided on the grounds on the actual impact that the pandemic had on the debtor's ability to perform or their monetary position. The burden of proof of the bearing that the pandemic allegedly had on the debtor's ability to perform or on their monetary position lies on the debtor seeking the application of the remedies offered in the article 357[1].

Despite the significant body of literature devoted to the subject of this report, there are still some doubts concerning the prerequisites of applicability of the article 357[1]. For instance, there are significant discrepancies between authors as to how the term "substantial loss" should be understood. It seems apt to assume that "substantial loss" is to be ascertained by comparing the position the party would have had, had the change in circumstances not materialised with the position they would have been in if the contract was performed after the change[16]. Thus the "substantial loss" may be reflected in the increased cost in performance of the party who demands termination or modification of the contract under article 357[1] or the decreased value of counter-performance. As said above, excessive onerosity is an alternative trigger of *rebus sic stantibus clausula*. In contrast to "substantial loss", it is not linked to economic value of performance but to personal hardship, such as putting one's health at risk in order to perform the contract. It seems that in the context of Covid-19 situation the latter may constitute a valid argument for *rebus sic stantibus* defence more often than usually.

In the context of current applications of article 357[1], its relation to special Covid-19 regulations becomes an important issue. As far as the Polish example is concerned, numerous provisions of these regulations (see articles 15k, 15ze, 15 zp, 31s, 31t, 31u, 31zu of the Act of 2 March 2020 on special solutions related to preventing, counteracting and combating COVID-19, other infectious diseases and emergencies caused by them[17]) directly affect the contracts concluded before the outbreak of the pandemic. As is the case of applying the article 357[1], the application of above-mentioned provisions results in amending or terminating the contracts covered by them. For instance, the article 31t bans the landlord from increasing the rent and terminating the lease, thus allocating the risk of specific change in circumstances (the outbreak of the pandemic) solely on the landlord. Whereas the article 15ze provides the decrease of rent of commercial spaces in shopping malls, which entails that the burden is entirely on the landlord. To the extent that special provisions of this kind allocate the risk of Covid-19 pandemic they are said to exclude the applicability of remedies spelled out in the article 357[1] of the Polish Civil Code[18].

[16] Radosław Strugała 'Ingerencja sądu w stosunek zobowiązaniowy na podstawie art. 357[1] KC' (2010) 8 Państwo i Prawo 51; Brzozowski (n 9) 172.

[17] Journal of Laws, item 374, as amended.

[18] See more in details Radosław Strugała 'Wpływ pandemii COVID-19 na wykonywanie umów w świetle art. 357[1] KC' (2020) 11 Monitor Prawniczy.