Client Alert | Corporate & Commercial

Italy

The impact of Coronavirus *(i)* on commercial contracts and *(ii)* on certain company law aspects for companies organised in the form of joint-stock companies

March 2020

[**IMPORTANT NOTE**: This document is updated as at 23 March 2020 at 17:00: given that the state of emergency and the related regulatory framework are constantly evolving on a daily basis, the contents of this memorandum may be subject to further changes.]

1. Foreword and reference framework

Following the increase in cases of Coronavirus Covid-19 infection in various areas of the world as well as in Italy, the Italian Government has decided to introduce extraordinary and urgent measures to counter the spread of the virus and to strengthen the national health system.

In this regard, it should first be noted that, on 9 March 2020, a decree issued by the President of the Council of Ministers introducing new urgent measures to contain and manage the epidemiologic emergency caused by Coronavirus Covid-19 was published in the Official Gazette. In particular, said decree provides for especially stringent measures, such as the **restriction of movement of natural persons within, as well as to and from, the entire national territory** and further strengthens the prevention and containment measures previously imposed.

On 11 March 2020, a further decree was published in the Official Gazette, having the same subject-matter as the previous decrees, which mainly ordered, inter alia, the suspension of retail business activities, with the exception of the sale of food and basic necessities.

Subsequently, the text of Decree Law No. 18 of 17 March 2020, known as "Heal Italy" ("*Cura Italia*"), containing measures to strengthen the national health service and provide economic support for families, workers and businesses related to the epidemiological emergency caused by Coronavirus Covid-19, was published in Official Gazette No. 70 of 17 March 2020. So, the "Heal Italy" decree law supplements the emergency measures already adopted by the Government to prevent the transitory crisis in economic activities caused by the Covid-19 epidemic from producing permanent effects, such as the definitive disappearance of businesses in the most affected sectors.

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Finally, on 22 March 2020, a new decree law was issued which *(i)* further strengthened the prevention and containment measures already imposed on movement within the territory[1] and *(ii)* ordered the suspension of all industrial and commercial production activities, with the exception of those expressly indicated in the annex to the decree [2] : http://www.governo.it/sites/new.governo.it/files/dpcm_20200322_allegato_1.pdf.

Consequently, in the light of the above, it is appropriate to examine in greater depth the extent of the impact of said measures on undertakings and on legal relationships existing between the various economic operators, considering that the situation not only affects corporate functions, such as personnel and production activities, but also has a considerable impact on the supply chain and logistics.

In this regard, as a preliminary point, it should be noted that in any case, **for the time being, the movement of people and goods between different municipalities is still possible only in case of proven extremely urgent working needs to be documented by filling in the relevant self-certification form made available online (https://www.interno.gov.it/sites/default/files/allegati/modulo-autodichiarazione-17.3.2020.pdf)**.

For further information on the measures adopted by the Italian Government and for any further updates, please consult the relevant institutional websites of the Government (http://www.governo.it/it/approfondimento/coronavirus/13968) and the Ministry of Health (http://www.salute.gov.it/portale/nuovocoronavirus/archivioNormativaNuovoCoronavirus.jsp) , the web pages set up by the individual Regions, as well as updates for companies and explanatory notes provided by Confindustria, including those provided by Assolombarda at the following link https://www.assolombarda.it/servizi/assolombarda-e-confindustria/informazioni/coronavirus-covid19.

2. Commercial contracts

a. Commercial contracts subject to Italian law

The recent spread of Covid-19 is - also in Italy - affecting, sometimes considerably, the performance of commercial contracts. Indeed, more and more often, in the last few weeks, the fulfilment of the obligations underlying sale and purchase contracts, procurement contracts, supply contracts, etc. has been delayed or, in some cases, made impossible by the spread of Covid-19, also because of the numerous urgent regulatory measures being taken by the authorities of all countries concerned. However, even where the fulfilment of contractual

[1] Article 1, paragraph 1, letter b) prohibits "*all natural persons from moving or travelling, by public or private means of transport, to a municipality other than the one in which they are currently located, unless motivated by proven working needs, absolute emergency or for health reasons*" and also prohibits them from returning to their domicile, home or residence.

[2] Production activities that are suspended pursuant to the decree at issue may in any case be continued if they are organized at a distance or using smart working (see article 1, paragraph 1, letter c) of Decree Law of 22 March 2020).

obligations remains possible, it may be presntly much more burdensome than expected and/or reasonably foreseeable at the time when the contract was entered into.

As a result of the above, Covid-19 is increasingly assuming the characteristics of what could be classified as a force majeure event.

The Italian Civil Code does not provide a real definition of force majeure, although it does provide for some institutions whose application presupposes the occurrence of events attributable to the concept of force majeure.

For contracts subject to Italian law, without prejudice to the relevance of any contractual clauses (see the so-called force majeure and/or hardship clauses including the so-called material adverse changes - MAC clauses typical of international practice, sometimes transposed also in domestic practice), reference shall be made, in particular, to the institutions of the supervening impossibility of performance for reasons not attributable to the debtor (pursuant to Articles 1218, 1256 and 1463 et seq. of the Italian Civil Code) or hardship in performance (pursuant to Articles 1467 et seq. of the Italian Civil Code) as well as the rescission for harm pursuant to Article 1448 of the Italian Civil Code.

Supervening impossibility (pursuant to Articles 1218, 1256 and 1463 et seq. of the Italian Civil Code) means any situation preventing performance that cannot be foreseen and cannot be overcome through the effort that can legitimately be required of the debtor.

In general terms, a breach of contract corresponds to the non-performance or incorrect performance of the service under the contract, which may expose the defaulting party to contractual liability towards the other party. However, according to the general principle laid down in Article 1218 of the Italian Civil Code, should the non-performing party prove that the breach of contract was the consequence of the impossibility of performing the service for “reasons not attributable to that party”, the latter may be held not liable.

More specifically, while the original impossibility of performance prevents the obligation from arising, the impossibility occurring after the beginning of the relationship between the parties, on certain conditions, causes its extinction, with the consequent dissolution of the contractual obligation and release of the debtor from the obligation to fulfil its performance.

A mere greater difficulty in performance or an impossibility of performance relating exclusively to the subjective sphere of the debtor is not sufficient for the application of the institution in question.

On the contrary, it is necessary that the contractual performance in itself has objectively become impossible to perform and/or that the conduct necessary for performance cannot be required of the debtor because it has become objectively too burdensome. It is of course essential to verify that the situation preventing performance has not been caused by the intentional or negligent conduct of the debtor and is not, therefore, attributable to the debtor. In this respect, case-law considers it sufficient to ascertain, on the basis of a concrete assessment, that the

situation impeding performance had arisen for any cause which the debtor was neither obliged nor in a position to avoid.

Without prejudice to the above, the concept of impossibility of performance can be further divided into the following sub-categories: (i) permanent impossibility (determined by an irreversible impediment or by an impediment whose end cannot be foreseen), (ii) temporary impossibility (determined by an impossibility of a transitory nature), (iii) partial impossibility which implies the extinction of the contractual obligation exclusively for the part which has become impossible.

Once the abovementioned conditions have been verified, the contractual obligation that has become impossible is extinguished, with consequent (total or partial) legal termination of the contract if said impossibility is absolute and final.

In the event of temporary impossibility, pursuant to the combined provisions of Articles 1256 and 1463 of the Italian Civil Code, the contract will not be terminated and performance may be legitimately suspended; once the reason for the temporary suspension has been overcome, the contract will become fully effective again. The suspended obligations will instead be extinguished if the impossibility continues until, according to the purpose of the obligation or the nature of the subject-matter, the debtor can no longer be considered obliged to fulfil its performance or the creditor is no longer interested in obtaining said performance.

In the case of bilateral contracts, the extinction of one of the contractual obligations shall cause, pursuant to Article 1463 of the Italian Civil Code, the dissolution of the entire contractual obligation. Such dissolution shall occur by law, with no need for any initiative of the party or intervention of a court. However, in the event of disputes, the parties may request the court to issue a declaratory judgment stating, unequivocally, that the contract has been terminated due to impossibility of performance and allowing, if necessary, to request, pursuant to Article 1463 of the Italian Civil Code, the reimbursement (in accordance with the rules on reimbursement of undue payments under Article 2033 of the Italian Civil Code) of the counter-performance, if it has already been performed.

On the other hand, in plurilateral contracts, the impossibility of performance of one of the parties does not imply the dissolution of the contract with respect to the others, unless the failed performance is to be considered, in the case at issue, essential for all parties.

The institution of **supervening hardship** (regulated under Articles 1467 *et seq.* of the Italian Civil Code) on the other hand allows for the termination of contracts whose balance is altered by supervening events - extraordinary and not reasonably foreseeable at the time of entering into the contract - which do not fall within the normal area of risk of the contract and which make any of the performances underlying the contract excessively onerous or objectively debased in its value and/or usefulness.

As a rule, supervening hardship applies to contracts involving reciprocal obligations and to be performed on an ongoing or recurring basis or otherwise providing for a deferred term.

The assessment as to the satisfaction of said conditions must be carried out by means of a concrete investigation.

In this regard, first, in order for supervening hardship to arise, there must be a tangible imbalance in the value ratio between the respective contractual performances.

Second, it is necessary that such imbalance in the performance value has been caused by events that are, respectively, extraordinary (in terms of the frequency, size and intensity of the event) and unforeseeable (subjectively, in relation to the relevant obligation).

Third, it must be further ascertained whether the risk involved with the extraordinary and unforeseeable circumstances referred to above exceeds the normal area of risk of the contract, i.e. the risk margin intrinsically underlying any contractual agreement. For this reason, the Italian Civil Code (Article 1469 of the Italian Civil Code) provides that the institution of supervening hardship shall not apply to contracts that are inherently hazardous or agreed as such by the parties.

If, as a result of such analysis, the performance turns out to be excessively onerous and is (even partially) outstanding, one may ask the court to terminate the contract.

During the proceedings, the counterparty that is interested in maintaining the contractual commitment in place may decide to take the contract "back to equity" by bringing the imbalance in the value of the contractual performances back to the normal area of risk of the contract, thus avoiding the termination effect.

The Italian legal system (see Article 1448 of the Italian Civil Code) disciplines a further general action that might have a certain relevance in the health emergency we are experiencing: the action of **rescission for harm**. By such action, it is possible to obtain the rescission of all synallagmatic contracts - with the sole exception of "aleatory" agreements - characterised by an abnormal disproportion between the parties' performances.

More specifically, Article 1448 of the Civil Code, provides that an action for rescission may be exercised if three conditions are jointly satisfied: i) the state of need of the injured party, meaning a situation of economic difficulty, even temporary, which has affected the party's free will to enter into a contract and led such party to accept the disproportion between the performances; ii) the value of the performance fulfilled or promised by the injured party being more than double the value of the counter-performance; iii) the taking advantage of the state of need by the contracting party benefiting from the disproportion.

Concerning the latter requirement, in particular, the case law has made it clear that mere awareness of the injured party's state of need is sufficient. If such conditions exist, the injured party is entitled to bring an action for rescission within one year of entering into the agreement, provided that injury persists at the time when the application is made. Article 1450 of the Civil Code, in compliance with the principle of contract preservation, allows the party against whom rescission is requested to propose a modification of the contract capable of eliminating the

imbalance between the performances and causing the synallagmatic relationship to be brought back to equity.

With specific reference to **sales contracts**, where one or both of the contractual performances are not fully implemented, the provisions described above shall apply.

The above-mentioned principles and rules described must also be deemed applicable to **supply contracts** (contracts whereby one party is obliged, in return for a price, to perform periodic or ongoing services involving goods or services for the other party). More specifically, aforementioned Article 1467 of the Italian Civil Code on hardship, referring verbatim to contracts "involving ongoing or periodic performance", extends the termination remedy provided for therein (the termination will have no effect with respect to performances already fulfilled - see the combined provisions of Articles 1467 and 1458 of the Italian Civil Code) also in favour of supplied parties and suppliers, without prejudice, of course, to the considerations made above with regard to the concepts of hardship and area of risk of the contract as well as impossibility to perform. However, it is likely that, in some cases, rather than terminating the contract *tout court*, it may be of greater interest to the parties to quantify the extent of the supply *ex novo*, in order to parameterise it to the real current needs of the supplied party. If the parties do not spontaneously find an agreement to adjust the contract to that effect, the defendant in the action for termination for hardship may, under Article 1467, paragraph 3, of the Civil Code, propose to the other party the fair modification of the contractual conditions: in such case, the concrete appropriateness of such offer will be submitted for review to the court in charge of the case.

The Italian Civil Code also contains provisions specifically dedicated to the subject under examination in **procurement contracts**, aimed at protecting the economic balance of the contract and at preserving, insofar as is possible, its effects. Pursuant to Article 1664 of the Italian Civil Code, the contractor and the principal may ask for an adjustment of the originally-agreed price if - due to unforeseeable events - increase or decrease in the cost of raw materials or personnel has occurred such as to cause a variation of at least 10% of the total agreed price. In such cases, price adjustment may only be allowed to the extent of the difference exceeding one tenth of the total price agreed. The provision also gives the contractor the right to obtain fair compensation in the event of any difficulties arising from geological, water and similar causes - not envisaged by the parties.

In any event, given the possibility of derogating from the above-mentioned provisions, there is still a need to examine, on a case-by-case basis, the specific contractual provisions, which may for example involve an increase in the threshold above which a request for price review is justified. When the requirements of Article 1664 of the Italian Civil Code are not met, prevailing case law considers the general discipline of supervening hardship described above to be applicable to procurement contracts. If a contract is terminated because the execution of the work has become impossible due to reasons not ascribable to the parties, the principal will in any case be required to pay the part of the work already completed to the extent it is useful to the principal (see Article 1672 of the Civil Code).

In the light of the foregoing, it is therefore theoretically possible that a health emergency of international relevance such as the one we are facing today and the related measures, as well as the conduct of market operators in such extraordinary situation, when totally or partially preventing performance or causing it to be excessively burdensome - or even allowing rescission for harm - may fall within the above mentioned cases, at least in case of contracts signed before 31 January 2020[3], subject to their subsequent assessment on a case-by-case basis, taking into account the specific contracts actually entered into.

More specifically, in this regard, it should be noted that the Decree Law of 17 March 2020, the so-called "Heal Italy" Decree, has expressly acknowledged, as a result of the suspension, throughout the national territory, of events, shows and performances of any kind, including cinema and theatre performances, held in any place, whether public or private, and the suspension of the opening of museums and other cultural institutions and places, the supervening impossibility of the performance due in relation to tickets for shows of any kind, including cinema and theatre performances, and entrance tickets to museums and other cultural attractions.[4] Buyers shall submit, within thirty days from the date of entry into force of the decree, a specific request for reimbursement to the seller, enclosing as an attachment the relevant purchase receipt. The seller shall, within thirty days from submission of the request, issue a voucher of the same amount as the purchase receipt, to be used within one year from the issue[5]. Furthermore, Article 91, paragraph 1, of the Decree clarifies that compliance with the containment measures set out in Decree Law No. 6 of 23 February 2020 may exclude, in individual cases, the debtor's liability pursuant to and for the effects of Article 1218 of the Italian Civil Code, as well as the application of any forfeiture or penalties connected with delayed or non-performance.

From a practical point of view, it is recommended to collect all the documentation that can prove, in a specific case, (i) that Covid-19 and/or Covid-19-related legislative measures amount to a cause of *force majeure*, (ii) any prejudice (e.g. an increase in the cost of the performance, a decrease in revenues or the impossibility to perform) arising, directly or indirectly, from the obligation to comply with the measures set out in the emergency orders issued and/or to be issued to combat Covid-19 and/or, in general, (iii) any anomalous imbalance in a contract relationship.

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[3] On 30 January 2020, following the reporting by China (31 December 2019) of a cluster of pneumonia cases of unknown aetiology (later identified as a new coronavirus Sars-CoV-2) in the city of Wuhan, the World Health Organization (WHO) declared the coronavirus epidemic in China a public health emergency of international concern. The following day, the Italian Government, after the first precautionary measures adopted from 22 January, taking into account the particularly widespread nature of the epidemic, declared a state of emergency and implemented the first measures to contain the contagion throughout the country.

[4] See Article 88 of Decree Law No. 18 of 17 March 2020. Such provisions are applicable until the date of effectiveness of the measures provided for in the Prime Ministerial Decree dated 8 March 2020 (i.e. 3 April 2020) and any further decrees issued pursuant to Decree Law No. 6 of 23 February 2020.

[5] Similar provisions are provided for by Article 28 of Decree Law No. 9 of 2 March 2020 in relation to travel documents and tourist packages. The above-mentioned Article 88 of the Decree Law of 17 March 2020 has extended this last provision also to employment agreement with workers with a residence permit ("*contratti di soggiorno*").

b. International commercial contracts

The impact of Covid-19 on international contracts, and in particular on the parties' failure to perform their obligations should be put in relation to the law negotiated by the parties and governing the specific relationship as well as to the interpretations based on the relevant regulatory system.

Frequently, the law governing the contract is identified in laws and regulations of common-law countries such as English or US law. Such legal systems, unlike those of civil-law countries (e.g., Italy, France and Germany) do not recognise the broad general principle of "*force majeure*", while providing, on the contrary, for concepts with a more limited scope, such as the English "frustration" and the US "impractibility". Therefore, in contractual relationships governed exclusively by English or US law, a party may invoke *force majeure* only if such remedy has been, as is often the case, contractually provided for. In such cases, it will be necessary to assess whether, according to the wording of the *force majeure* clause contained in the contract, Covid-19 and the related restrictions imposed by public authorities can be considered as qualifying events for invoking *force majeure* and avoiding claims and actions for breach of contract.

Likewise frequently, the contract is governed by specific treaties such as the 1980 United Nations Convention on Contracts for the International Sale of Goods, which provides that a party is not be liable for its non-performance, or for failure to perform any of its obligations under the contract, if it proves that the failure was due to an impediment beyond its control and not reasonably foreseeable.

At a supranational level, the Unidroit Principles of International Commercial Contracts ("**PICC**") (2016 version - https://www.unidroit.org/instruments/commercial-contracts/unidroit-principles-2016) regulate *force majeure* under Article 7.1.7, as follows: "1. *Non-performance by a party is excused if that party proves that the non-performance was due to an impediment beyond its control and that it 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. 2. When the impediment is only temporary, the excuse shall have effect for such period as is reasonable having regard to the effect of the impediment on the performance of the contract. 3. The party who fails to perform must give notice to the other party of the impediment and its effect on its ability to perform. If the notice is not received by the other party within a reasonable time after the party who fails to perform knew or ought to have known of the impediment, it is liable for damages resulting from such non-receipt. 4. Nothing in this Article prevents a party from exercising a right to terminate the contract or to withhold performance or request interest on money due.*".

This concept is closely linked to the concept of hardship, defined - under Article 6.2.2. of the PICC - as follows: "*There is hardship where the occurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party receives has diminished, and (a) the events occur*

or become known to the disadvantaged party after the conclusion of the contract; (b) the events could not reasonably have been taken into account by the disadvantaged party at the time of the conclusion of the contract; (c) the events are beyond the control of the disadvantaged party; and (d) the risk of the events was not assumed by the disadvantaged party.".

Under the combined provisions of the definitions of *force majeure* and hardship laid down in Articles 6.2.2. and 7.1.7., events may occur which may be covered by either definition according to the PICC. In such case, it is up to the debtor to decide which remedy to apply: if the debtor invokes *force majeure*, his/her purpose is to be exonerated from the consequences of the non-performance; if, on the other hand, the debtor decides to invoke hardship, it is with the aim of renegotiating the contract so that it remains in force, albeit with amended terms and conditions.

It must be pointed out that the PICC are soft-law non-mandatory instruments intended to address the problem of sectoral harmonisation of international trade law.

It is customary in international commercial contracts to regulate in a more precise and detailed way which circumstances may amount to *force majeure* and hardship and their consequences on the validity of the contract.

Therefore, in the event that there is a possibility - either because of a specific contractual clause, or because of a reference to a foreign law or an international treaty - to invoke *force majeure*, at least three remedies available to the party concerned may be envisaged, namely, suspension of performance, renegotiation of contract or termination of contract. As far as suspension of contract is concerned, it should be noted that international contracts often regulate such remedy having regard to the maximum term of the contract and, in case of extension beyond such term, termination of contract or the obligation of the parties to renegotiate the terms and conditions of the contract in good faith. The renegotiation-of-contract remedy, which may be adopted, for example, by entering into a written agreement amending the original contract, will result in setting out of new terms and conditions on performance or, in cases of greater difficulty, establishing a new balance in the parties' performance in view of the changed circumstances. As regards the termination-of-contract remedy, the *force majeure* clause contained in the contract may rarely operate as a cause of automatic termination, although such remedy will be inevitable in all cases where performance has become impossible or no longer practicable for an indefinite time or for a period of time that frustrates the obligations set out in the contract.

From a practical point of view, as already mentioned in relation to commercial contracts governed by Italian law, it is recommended to collect all the documentation that can prove, in a specific case, (i) that Covid-19 and/or Covid-19-related legislative measures amount to a cause of *force majeure*, (ii) any prejudice (e.g. an increase in the cost of the performance, a decrease in revenues or the impossibility to perform) arising, directly or indirectly, from the obligation to comply with the measures set out in the emergency orders issued and/or to be issued to combat Covid-19 and/or, in general, (iii) any anomalous imbalance in a contract relationship.

3. Company law aspects for companies organised in the form of joint-stock companies

The decree law of 17 March 2020 for the management of the emergency also provides for significant measures to facilitate the holding of shareholders' meetings.

Indeed, with reference to timing, Article 106 of the decree provides for a general and automatic extension of the deadline for calling shareholders' meetings to approve the financial statements within 180 days of the end of the financial year, in derogation from the provisions of Articles 2364, second paragraph, and 2478-bis, of the Italian Civil Code or from the other provisions of the By-laws. Moreover, since the deadlines of the Board of Directors are calculated backwards, the extension also affects de facto the deadlines of the Board of Directors in relation to the approval of the draft financial statements.

With regard to the procedures for holding ordinary and extraordinary shareholders' meetings of S.p.A.s, S.a.p.A.s, S.r.l.s and cooperative companies, it shall be possible to provide, also in derogation from the different provisions of the By-laws, that voting be expressed electronically or by correspondence and that shareholders' meetings be attended by telecommunication means without in any case the need for the chairman, secretary or notary, as applicable, to be in the same place. With regard to this latter aspect, reference is also made to notarial decision No. 187 of 11 March 2020 of the Notarial Board of Milan, according to which it is no longer necessary for the chairman and the secretary to be present in the same place.

With specific reference to S.r.l.s, Article 106, paragraph 3, of the Decree Law of 17 March 2020 also provides that voting may take place by written consultation or by express written consent, also in derogation from the provisions of Article 2479, paragraph 4, of the Italian Civil Code and from the other provisions of the By-laws.

All the aforementioned provisions of the Decree Law of 17 March 2020 are applicable to Shareholders' Meetings convened by 31 July 2020 or, if later, by the date until which the state of emergency on the national territory in relation to the health risk associated with the outbreak of the COVID-19 epidemic will be in force.

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