THE INCIDENCE OF GOVERNMENT MEASURES TAKEN IN RELATION WITH THE CORONAVIRUS AND THE EXECUTION OF CONTRACTS UNDER SPANISH LAW.

Following the restrictive measures adopted by the Government of Spain and many autonomous regions of the state, as well as in other countries, questions arise regarding the possible impact of current or future measures in the execution of contracts, as the need to slow the progress of the COVID-19 virus may impose new restrictions. Our analysis will focus on contracts subject to Spanish law.

1. Force majeure: unforeseen and unavoidable event. Effects of its appreciation.

Pursuant to article 1105 of the Spanish Civil Code, "Outside of the cases expressly stated by law and in those in which the obligation so declares, no one will be liable for those events that could not have been foreseen or that, being foreseen, were unavoidable".

In presence of an event of the scale such as the subject of this analysis, the first question to be posed is whether it may be considered as an event constituting force majeure.

As for the interpretation and application of this provision, the case-law in Spain states:

1. Two cumulative requirements must be met so as an event deserves the consideration of force majeure: unpredictability and inevitability, the proof of which falls on the party invoking the force majeure in its favour.
2. The event constituting force majeure must be subsequent to the execution of the contract, and entirely unrelated to the claiming party.
3. There must be a total absence of liability from the party invoking force majeure.
4. In order to assess the concurrence or not of an event which would prompt force majeure, it will apply the normal and reasonable foresight which the circumstances will require in each specific case.
5. Finally, the party intending to apply the force majeure clause to release itself from the fulfilment of its obligations under the contract, shall act in good faith and undertake all necessary measures to mitigate the damaging effects deriving from said event.

As a consequence of the assessment of force majeure, the party invoking it shall not be liable for any breaches in which it may have incurred for the duration of the event constituting force majeure. This liability exemption and the scope of the remaining contractual obligations must be made on a case-by-case basis, as the same may be complete or only partial, and they may be definitive or only temporary.

The stipulations of the contract for instances of force majeure will always be of preferred application (the ‘pacta sunt servanda’ rule is established in article 1091, article 1255 and article 1258, among others, of Civil Code): it may have been agreed that the contract is subscribed "in any event", or a regime may have been agreed in case of a situation of force majeure taking place: for example, the extension of the contractual relationship beyond the term provided for the time necessary to allow complete fulfilment of the respective obligations.

In case of absence of specific contractual provisions, Article 1124 CC should apply, according to which the complying party shall be entitled to demand either fulfilment, either the termination of the contract, with the mere difference that the counterparty, benefited from the force majeure, shall be exempt from compensation for damages..

2. Application of the doctrine ‘rebus sic stantibus’.

Secondarily, in particular if the contract does not allow invocation of the measures taken to stop the spread of COVID-19 as constituting force majeure, the parties may rely on the ‘rebus sic stantibus’ doctrine.

Indeed, many contracts provide for a legal or regulatory risk clause, which covers the cases where, through legislative or government measures, changes occur in the balance between the rights and the obligations of the parties pursuant to the contract.

Case-law by the Supreme Court is prudent with regard to the application of said ‘rebus sic stantibus’ clause, from STS 15 October 2014 (appeal Nº 2992/2012), which, while certainly mitigating the excessive rigour with which the invocation of this file was being admitted in practice, the same was attenuated according to the circumstances of each case.

In any case, our High Court (SSTS 64/2015, 24 February, 237/2015, 30 April and 19/2019 of 15 January) requires that two budgets be provided for their application: unpredictability of risk and excessive hardship in the fulfilment of contractual obligations, which is often characterized as a breach of the relationship of equivalence in the considerations of the parties (principle of commutability of contract).

If the circumstances for the application of the ‘rebus’ doctrine or clause are given, the consequences would have to be determined: whether it would result in a mere modification of the contract or in its termination. The solution in favour of the contract modification, more in line with the principle of preservation of contractual acts and businesses (‘contractus’) is the preferential solution applied by the case-law, especially in the case of continuing performance or long-term contracts.

APPLICABLE REGIME TO FOREIGN DIRECT INVESTMENTS IN SPAIN AFTER THE DECLARATION OF STATE OF EMERGENCY FOR THE MANAGEMENT OF THE SITUATION PROVOKED BY THE OUTBREAK OF COVID-19.

1. The concept of “Foreign Direct Investment” under Regulation (UE) 2019/452.

Royal decree-law 8/2020, of 17 March, of urgent and extraordinary measures to face the economic and social impact of COVID-19 (“RDlaw 8/2020”) introduces in its Disposition final fourth a new article 7 bis of Law 19/2003, of 4 July, upon legal regime of the movements of capitals and foreign economic transactions (“Law 19/2003”), which submits to prior administrative authorization, suspending the previous liberalization regime, some foreign direct investments in Spain.

As to the duration of this new regulation, the Royal decree-law 11/2020, of 31 March, has rectified the previous one, repealing section 6 of article 7 bis of Law 19/2003 (as amended by RDlaw 8/2020), in which it was stated that the suspension of the liberalization regime would be in force until this suspension is lifted by Agreement of the Council of Ministers. It is controversial the will of legislator while repealing this section, but the most likely interpretation is that the new wording of article 7 bis of Law 19/2003 will have, from now, an indefinite duration.

The breach of the new regulation is considered a ‘very serious infringement’ which may result in fines ranging between €30,000 and the transaction value and public or private warnings.

It must be borne in mind that, as for the interpretation of the concept of Foreign Direct Investment (FDI) used by the RDLaw 8/2020, amending the Law 19/2003, must be read in the light of the provisions of Regulation (EU) 2019/452 of the European Parliament and of the Council, of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union ("Regulation 2019/452"), which, for the purposes of that Regulation, defines in its article 2.1) 'foreign direct investment' as an investment of any kind by a foreign investor aiming to establish or to maintain lasting and direct links between the foreign investor and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity in a Member State, including investments which enable effective participation in the management or control of a company carrying out an economic activity".

Despite Regulation 2019/452 shall not be applicable until 11 october 2020, it entered into force from 11 april 2019, and so, according to principle of "conforming interpretation", all national provisions related to FID must be interpreted in a harmonic or uniform sense.

On 25 March 2020, once the state of emergency has been declared in Spain by the Royal Decree 463/2020, of 14 March, the European Commission has issued a document with the title of "*Guidelines to the Member States concerning foreign direct investment and free movement of capital from third countries, and the protection of Europe's strategic assets, ahead of the application of Regulation (EU) 2019/452 (FDI Screening Regulation)*"[1]. In this document, the EC gives a response to the concern, raised by several Prime Ministers of EU Member States (among others, Spain), to avoid that companies considered as strategic assets may succombe prey to hostile takeovers[2]. At a European Union level, some specific actions are being taken, so that protecting European companies of foreign investors, providing EU Member States with criterion for the screening to be applied to the foreign direct investment, making it subject of prior administrative authorization in case of risk of public order, public security and public health.

2. Suspension of the liberalization regime of foreign direct investment set forth in article 7 bis of Law 19/2003.

The Government prohibits the acquisition by Foreign Investors of 10% holdings in companies active in sectors related to public order, public security or public health without a prior authorisation of the Spanish Government. Acquisitions of less than 10% of the share capital are also subject to authorization if resulting in an effective participation in the control or management of the target company.

The affected sectors are:

(i) critical infrastructures, both physical and virtual (energy, transport, water, healthcare, communications, media, data storage and processing, aerospace, defence, finance or sensitive installations);

(ii) critical technology and dual-use products;

(iii) essential supplies (energy, hydrocarbons, electricity, raw materials and food);

(iv) sectors with sensitive information such as personal data or with capacity to control such information; and

[1] https://trade.ec.europa.eu/doclib/docs/2020/march/tradoc_158676.pdf

[2] El 25 de marzo de 2020, los Presidentes de los Gobiernos de Bélgica, Francia, Grecia, Irlanda, Italia, Luxemburgo, Portugal, Eslovenia y España, han dirigido una carta conjunta en tal sentido a Charles Michel, Presidente del Consejo Europeo. La carta se puede ver en el siguiente enlace: https://www.mlex.com/Attachments/2020-03-25_YO7U122158640C40/Letter%20to%20Michel.pdf

(v) media.

Foreign investment in any industry –when the investment is equal to or higher than 10% of the share capital, or results in a participation in the effective control and management of the relevant company– shall be subject to a regime of prior authorization if the relevant investor is in one of the following cases:

(i) it is controlled directly or indirectly by the government of a third country, including public bodies or armed forces;

(ii) administrative or judicial proceedings have been initiated against it for exercising illegal or criminal activities.

(iii) Foreign investment in any industry –when the investment is equal to or higher than 10% of the share capital, or results in a participation in the effective control and management of the relevant company– shall also be subject to a regime of prior authorization if the relevant investor has invested or participated in sectors affecting the security, public order or public health in another EU member State, in particular in those sectors referred above.

RDL 8/2020 did not refer to any minimum threshold of the participation held by the Foreign Investor in another EU member State, but this gap has been filled by final Disposition third of RDlaw 11/2020, in which it is amended the wording of the previous article 7 bis.

From the latter disposition, it is established that, for the purposes of this article, foreign direct investments are those in which, as a consequence, the investor gets a participation equal or superior 10 per 100 of social capital of the Spanish company, or when, as a result of the corporate operation, act or agreement, an effective participation in the management or control of said society is hold. In this regard, it will be considered that a real ownership exists when these investors ow or control at the last instance, direct or indirectly, a percentage superior to 25% of social capital or voting rights of the investor, or when, by other means, they exerce the direct or indirect control of the investor.

A further regulatory development will establish the amount under which operations of direct investment shall be exempt of prior authorization regime

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