



Legal Implications of a Global Pandemic

Adaptation of the Contract to the Changed Circumstances

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KPMG Georgia Legal Services



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Introduction

The negative impact of the global pandemic on the global and local economies has been increasing for past few months. The measures taken by various states in response to the virus have led to substantial changes in business relations, which has caused need to modify contractual terms.

Considering the application of various contractual mechanisms to respond to the new reality created by the pandemic, it has become particularly important to properly assess legal risks in the process of making business decisions in such cases when the contract does not precisely define the rights and obligations of the parties for similar events.

As part of the information campaign launched to reduce the negative impact of the pandemic, KPMG Georgia presents a snapshot of Georgian legislation and court practice under Article 398 of the Civil Code - Adaptation of the Contract to the Changed Circumstances.

Legislative Base

According to Article 398 of the Civil Code of Georgia:

1. If the circumstances that were the grounds for the conclusion of a contract have evidently changed after conclusion of the contract and the parties would not have concluded contract or would have concluded contract with different content, if they had considered these changes, then it may be requested to adapt the contract to the changed circumstances. Otherwise, taking into account the individual circumstances, a party to the contract may not be required to strictly observe the unchanged contractual terms;
2. It shall also be regarded as a change in circumstances if the perceptions, which represented the basis for the conclusion of a contract, prove to be wrong;
3. The parties shall first try to adapt the contract to the changed circumstances. If such adaptation is impossible, or if the other party does not agree, then the party whose interest has been harmed may repudiate the contract.

The right to request the adaptation of the contract to the changed circumstances and its legal implications differ from the cases of force majeure. The application of Article 398 is usually aimed at changing the terms of the contract, while the force majeure provisions are related to the exemption from liability for non-performance of the affected obligation.

Are you entitled to invoke Article 398 of the Civil Code in your legal relationships? - check if your particular case meets the following cumulative preconditions set out in the provision:

- Circumstances clearly changed or the perceptions turned out to be wrong after conclusion of the contract;
- These changed circumstances/perceptions were the basis for the conclusion of the contract;
- Have the parties considered such a change of circumstances, the contract would not have been concluded or would have been concluded on different terms.

What is necessary for the application of the norm?

- Negotiate with the other party in order to make the changes.

What rights do you have in case of impossibility of changes or refusal of the other party?

- The right to demand release from the obligation to comply with the terms of the contract;
- Withdrawal from the contract in the absence of circumstances precluding such withdrawal.

Relevant Practice of the Supreme Court

Criteria established by the court practice in order to assess the appropriateness of application of Article 398.

- Reasonable consideration of the change in circumstances was impossible for the parties at the stage of concluding the contract;
- The change has severe consequences for the debtor;
- Given the unexpected and particular nature of the change, ignoring it contradicts the principle of good faith.

In application of Article 398, the positions of the parties shall be assessed in consideration of the general principles of good faith in civil relations and the prohibition of the abuse of rights.

The Supreme Court of Georgia has made several explanations regarding the application of Article 398 of the Civil Code, which is an important guide for analyzing the legal risks of related business decisions:

- The application of Article 398 is allowed only in exceptional cases, where the parties could not have reasonably foreseen the change and such change is so special and unexpected by its nature that failure to consider such change will be contrary to the principle of good faith. Mere increase in real estate property prices may not be invoked as the ground for requesting adaptation of contract if such increase could have been foreseen by the parties due to the pre-existing trend on the market [sl-466-707-08, 398 November 25, 2018];
- Change in the currency exchange rate may become the basis for application of Article 398, if the parties would not have concluded the contract had they considered the change, or would have concluded it on different terms; the change was not foreseeable; the change is obvious and has grave consequences for the debtor [sl-1298-2018, March 22, 2019];
- If the refusal to change the contract is unjustified, i.e. the party fails to demonstrate that the refusal is justified with the intention to protect his/her legitimate contractual interests, the other party to the contract may be released from the obligation to comply with certain terms of the contract under Article 398 [sl-793-742-2017, January 17, 2018].

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