



Under the microscope

Managing short and longer term dispute risk arising out of COVID-19

Companies across the globe are being impacted by the COVID-19 outbreak – whether this be through its impact on their workforce, interruption of their supply chain or otherwise.

Since the outbreak, we have been advising companies across the globe on the contractual consequences and, in particular, on the question of whether force majeure or equivalent concepts apply or not. This is an issue which will have an impact on companies in all sectors. However, to date, we have seen a greater prevalence in the construction, oil and gas, aviation, retail and leisure sectors.

Whilst many of the principles behind force majeure are common across the globe, its application varies from jurisdiction to

jurisdiction, with differences particularly stark between common law and civil law jurisdictions, and across differing legal traditions. We have teams of dispute resolution lawyers in all key global jurisdictions who understand these issues and who are now regularly helping companies manage the business challenges they face as a result of the COVID-19 outbreak.

In this document we set out the **key issues** companies should now be taking steps to address.

If you need support in respect of any of your trading or operating contracts during the COVID-19 outbreak, please contact one of our experienced lawyers:

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Our extended COVID-19 working group includes lead advisors in major economic centres around the world. Our team will connect you with right expertise whether local or global.

1. Risk of business disruptions causing companies to be unable to meet their commitments

Whether a business relies on a supply chain, the ability to export or import goods or send out employees to perform services, COVID-19 is now likely to impact on most businesses whether global or domestic. The impact may arise (by way of example) as a result of government restrictions introduced in certain countries, duties that companies may have to their employees, or reduced employee availability resulting from self-isolation or illness. Depending on the extent of the disruption, this could give rise to breach of contract claims, delay damages and/or termination of contracts.

2. Risk of any part of the supply chain being interrupted

Those businesses with long supply chains are plainly facing an increased risk of interruption to the supply of key products and materials. As COVID-19 spreads and its impact becomes greater, the threat to the supply chain increases. We have already seen the impact from China having imposed a significant lockdown on its workforce and the reduction in the supply of key materials manufactured in China. As travel becomes more challenging and as other countries take similar action, the position is only likely to get worse. It is therefore important that companies are looking at their contractual position throughout their supply chain (both up and down that chain) in order to see what potential relief they can rely upon.

3. Risk of large-scale staff absence preventing operation

A wide-spread effect of the COVID-19 outbreak is large-scale disruptions to staffing, affecting operations. Absence of key or a majority of staff can lead to closure of facilities, preventing business operations. The extent of staff absence may become a critical point for the ability of an entity to declare force majeure under some of its contracts, as many force majeure clauses provide that force majeure may only be declared when the event is beyond the control of either party. A company declaring force majeure because of staff absences may need to consider whether it has any other options, or alternatively it may need to be able to demonstrate that it had no other option, that it could not have operated with a remote work-force or alternatively that it could not have engaged any suitable replacement staffing. Further, the company may in future be required to evidence this state of affairs in order to justify its force majeure notice, in the event of a dispute.

4. Risk of your counterparties being unable to trade with you

Even if the COVID-19 situation does not affect your own operations directly, there is a risk that your counterparties may be affected. In addition to assessing the effect of disruptions on your ability to continue operating, it is also prudent to assess the risk to your business of disruptions to your main counterparties, suppliers or clients, and the extent of your contractual protections/risks. For example, a company that primarily does business online with remote staff resources and without a significant physical presence may not have to deal with substantial physical/travel disruptions at present, but this may not necessarily apply to its clients or customers which could be suffering serious practical constraints. What practical protections to you have in place for a situation where your main clients stop purchasing from you? Can you extract yourself from exclusivity constraints which would ordinarily prevent you from contracting with other companies in the market? Do you have contractual measures in place to assist you to prepare for the loss of a primary supplier or a primary client (e.g. a contractual right to call for increased supplies at short notice from your secondary supplier)?

5. For those contracts where these risks exist, the legal protections that may be available to you – whether force majeure, material hardship or otherwise

Where you have contracts under which you may not be able to perform your obligations, it is imperative to undertake a review of those contracts at an early stage. The most likely protection is to be found via force majeure which, in essence, relieves or temporarily suspends a party's contractual obligations whilst they are unable to perform those obligations due to events beyond their reasonable control. It is important to note that in common law jurisdictions, parties only benefit from force majeure if they have expressly included it within their contracts; however, in certain civil law jurisdictions, the concept of force majeure can exist as a matter of statute or code. It is therefore important to check what law governs your contracts and to take appropriate local advice.

Outside of force majeure, we anticipate that companies will seek to rely on material hardship clauses where they exist. Such clauses often temporarily alter a party's contractual obligations in circumstances where they are suffering from material hardship. The extent to which such clauses are used within contracts varies from sector to sector, with the chemicals sector in particular being one where we have seen extensive use of such clauses.

Finally, parties may also need to consider the question of frustration. Whilst, again, the precise nature of this test will change in each jurisdiction, frustration generally relieves a party from its contractual obligations where they have become impossible to perform. This is typically seen as a very high hurdle to overcome and it is therefore difficult for parties to rely on frustration. However, as the impact of coronavirus across the globe becomes more significant, the prospects of relying on frustration are likely to increase.

6. Notification requirements in order to rely on such protections – when and how should notice be given

Typically, where there is a right to some form of relief there will be notification requirements which must be followed. This is particularly the case in common law jurisdictions and contracts which include force majeure provisions. Parties seeking to rely on such clauses will need to read these clauses carefully and consider any specific notification requirements. This may include: (i) that notice must be given within a specific period of time; (ii) that updates are required within another specific period of time; (iii) that evidence be supplied showing how the force majeure is causing non-performance; (iv) evidence of mitigation and so on. In addition, the notice provisions in the contract, which are typically under a separate clause in a contract, must also be followed (i.e. the form of notice, correct address and addressee). Equally, those parties receiving force majeure notices will need to consider whether or not they are valid and comply with such requirements.

7. Your obligations in the circumstances (e.g. mitigating your losses)

In addition to obligations to notify, a party seeking to rely on relief such as force majeure may have an obligation to mitigate. There may be an express contractual duty to mitigate but under English law there is also a general common law duty to mitigate loss that is "reasonably avoidable". Contractual terms can impose a more onerous duty (for instance, the requirement to use best endeavours). It may be the case that in some circumstances, the most reasonable course of action is to do nothing; for instance where a supplier will deliver goods/services with a minor delay, but this minor delay would still have an effect on obligations owed to the ultimate customer (for instance by triggering entitlement to liquidated damages), it may be the best course of action to incur those penalties (i.e. do nothing), provided the loss caused by this course of action is lower than the cost which would be expended on procuring an alternative supplier at short notice. However, the question of what steps should be taken in order to satisfactorily mitigate will need to be considered carefully on a case by case basis.

8. Managing insurance cover

As well as checking for contractual protections, you also now need to be giving consideration to your insurance policies and testing what protection they afford to you. Key questions here include whether policies are triggered by the outbreak of COVID-19 and, if so, how much cover is afforded? Here the issue will be how many separate claims can be made, and how do those claims aggregate to use up the available cover.

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