

COVID-19: The Legal Consequences of Significant Disruption on Your Contracts

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COVID-19 and other disruptions can create multiple business challenges, including service interruptions, financial hardship and workforce concerns. Vendor contracts are no exception. Vendors provide integral services and can be excellent partners in building the customer's brand and making the customer more profitable. However, in time of disruptions, businesses must evaluate their options under existing contracts and strengthen provisions in future contracts to minimize risk.

When negotiating contracts, it is easy to dismiss certain provisions as "boilerplate," thinking that these terms are standard within the industry, are non-negotiable, and can safely be ignored. However, such assumptions often are not true, and unwary businesses can find themselves in deep distress once the agreement has been signed and problems arise. One such term, especially relevant now, is *force majeure*.

Force Majeure, or Acts of God

As contracts have been disrupted by COVID-19 and its related consequences, *force majeure* ("superior force") clauses have taken on greater importance. These clauses protect non-performing parties if a contract cannot be performed due to unanticipated causes beyond that party's reasonable control. Contracts may define *force majeure* specifically by listing events, such as earthquakes, floods, terrorism, governmental actions, war and hurricanes, as well as pandemics. Others may define the term generally as anything out of a party's reasonable control or may include both specific events as well as a general catch-all.

Action item: Businesses should examine their current contracts carefully today to identify any *force majeure* clauses and take note of their terms, especially any notice or mitigation requirements. In negotiating any new contracts, businesses should consider how the current disease and future epidemics could affect the agreement and prepare for a similar situation in the future.

One coronavirus-related question often arising today is whether a *force majeure* clause justifies the suspension of performance under a contract. The answer depends on the specific contract language, local law, and the causal connection between the pandemic and the parties' ability to perform their contractual obligations. As it pertains to COVID-19, if travel bans or other governmental restrictions prevent a party from meeting its contractual obligations, any broadly worded *force majeure* clause may well apply. The party seeking to invoke *force majeure* must show a causal connection between the event and its inability to perform. As in any contract matter, a party cannot invoke a *force majeure* clause unless it complies strictly with the technical requirements of the contract. Typically, this includes prompt notice of a claim of *force majeure* and regular updates of efforts to mitigate.

Other contractual remedies may also be available in the event of hardship.

Frustration of a Contract's Purpose

If a contract lacks a *force majeure* clause, in many jurisdictions the doctrine of "contractual frustration" may provide relief for a party that finds itself unable to perform its obligations. Typically, the party will have to show that a truly unexpected event has made it physically or commercially impossible to fulfill the agreement. This defense may be difficult to prove, as its application often depends on the specific circumstances of the contract at issue.

Insurance Coverage

Either party (most commonly the vendor) may be required to obtain and maintain specified levels of insurance during the term of the agreement. These provisions typically require the other party to be provided with a certificate of insurance and to be named as an additional insured. Losses arising out of a party's inability to fulfill its contractual obligations may give rise to an insurance claim. Coverage will depend on the policy's specific terms and conditions. Businesses should look at the policy provisions and provide notice of loss to the insurance companies promptly.

Termination

Termination provisions may provide (1) a right of one or both parties to terminate for convenience, (2) an ability to terminate for cause, and (3) the option for nonrenewal. In the event a business opts to terminate early, it should review the contract carefully to understand what notice is required and the potential cure periods.

Now more than ever, contracts should be drafted carefully to protect the interests of the parties. Oft-overlooked sections, such as *force majeure*, insurance and termination, can dramatically impact potential liability in the event of non-performance. While not all problems can be avoided or anticipated, taking the time to review and negotiate the provisions in a contract on the front end can save considerable time, expense and headache later. At some point business will return to normal, and we all want to ensure that decisions we make today will not impact us negatively in the future. ■



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