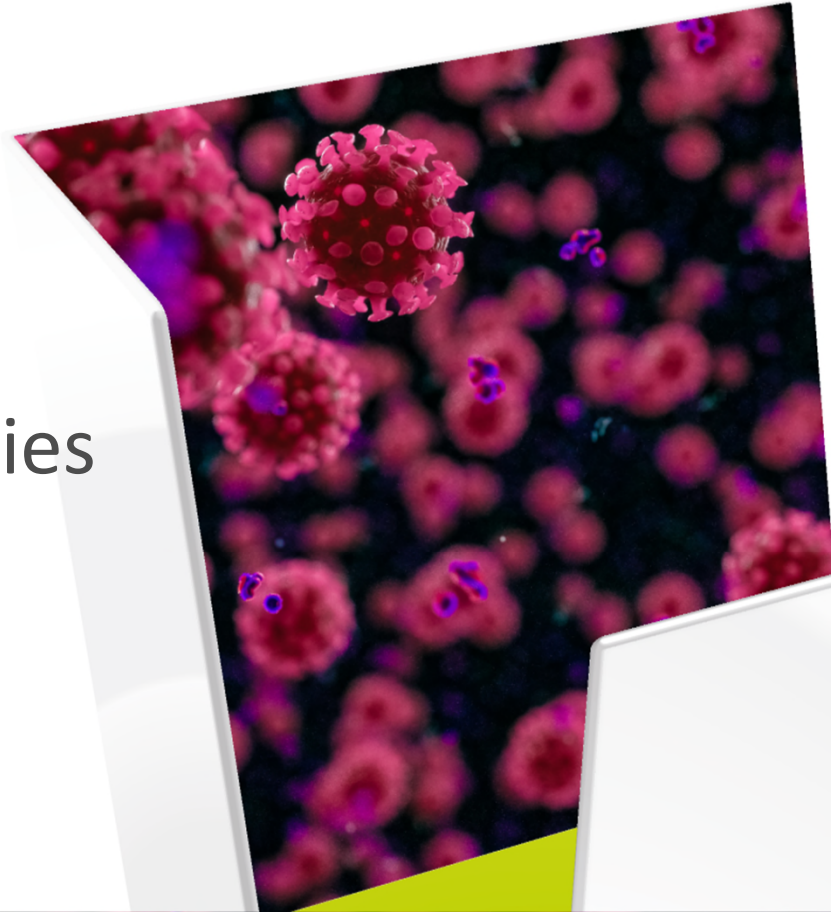


COVID-19 webinar series

26 March 2020

COVID-19 and the supply chain
– contracts and *force majeure*



Context: A multi-layered issue



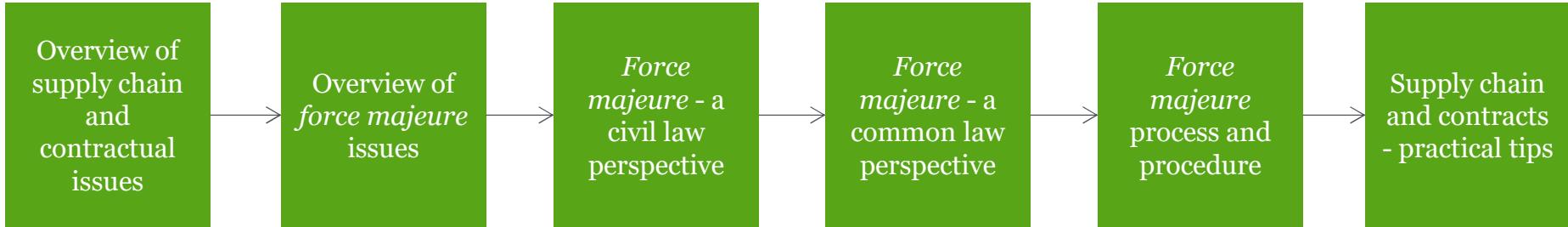
Peter Watts

Partner, Corporate and Commercial
London

+44 20 7296 2769

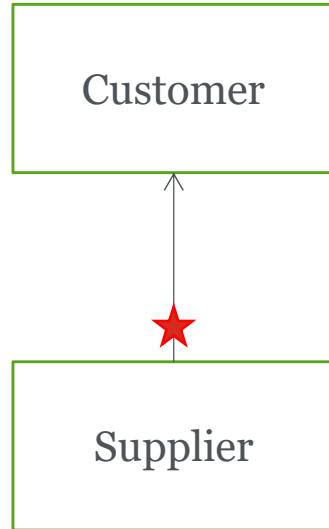
peter.watts@hoganlovells.com

Agenda

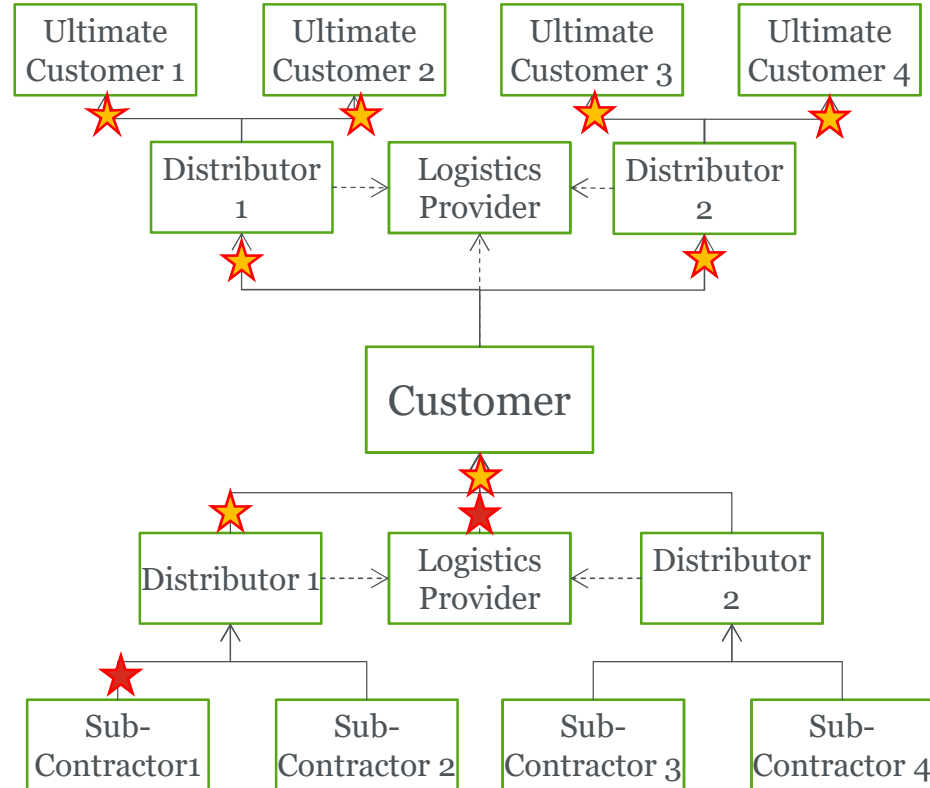


Context: A multi-layered issue

Micro



Macro



Practical issues we are seeing

- Challenges in all directions
- Problems with performance and payment
- Direct and indirect causes
 - Legal prohibitions
 - Policy statements
 - Direct practical issues (own sickness levels)
 - Indirect practical issues (shortage of stocks in the supply chain)
- Speed of change and government overrides
- Confusion and business people at the sharp end

Legal considerations

- Is there a contract?
- Nature of obligations and governing law
- Frameworks and commitments
- Breach
 - Financial claims
 - Termination rights
- *Force majeure*
- Other contractual triggers:
 - Change control
 - Automatic price or performance adjustments
 - Termination rights
- Exclusion of liability – particularly with consumers and SMEs

Practical considerations

- What is your goal?
- Do you understand your supply chain?
- Do you know what the contract terms are?
- Managing communication
 - “first responders”
 - Impact of practical steps and communication on legal position
- Record-keeping
- Availability of legal and practical recourse (e.g. recovery of goods)
- Ability to take over sub-contracts
- Insurance

Force majeure & contract issues explored



Tanja Eisenblätter

Partner, Commercial Litigation

Hamburg

+49 40 41993 528

tanja.eisenblatter@hoganlovells.com

What is *force majeure*?

An event which:

- (a) is outside the control of a party and/or an exhaustive or non-exhaustive specified list of events
- (b) prevents performance
- (c) often requires reasonable endeavours to overcome
- (d) suspends obligations
- (e) potentially results in termination

Force majeure clause and governing law

- Check for governing law:
 - Common law: An express *force majeure* provision in the contract is needed in order to claim *force majeure*
 - Civil law: *Force majeure*-type provision in governing law
- Check if there are overriding notification requirements and rules on the effects of notifying a force majeure event.

Is COVID-19 covered?

- Determination will be easier where governments/legal authorities (for example, China) have officially certified coronavirus as a force majeure event.
- Exhaustive list/non-exhaustive list
 - If the list includes epidemics or pandemics:
 - To trigger the clause, it probably won't say:
 - who has to declare an epidemic/pandemic or whether the epidemic/pandemic has to be:
 - in a certain country/region only or global
 - in only certain places where the contract is to be performed, such as place of manufacture/product delivery/service delivery
- Extent of interference
 - “impeded”, “hindered”, “prevented” or “interfered with”
- Causal link

No *force majeure* clause included

- No *force majeure*-type clause? Event not covered by the contract words?
Other provisions you might rely on:
 - Material adverse change
 - Price adjustment
 - Liability limitations and exclusions
 - Extensions of time
 - Variations
 - Changes in law (for example, laws prohibiting employees or transport from working, which slow down the supply chain)
 - Frustration (unlikely to succeed in many jurisdictions)

Force majeure in a common law jurisdiction (English law)



Angus Rankin

Partner, Construction and Engineering
Disputes

London

+44 20 7296 5030

angus.rankin@hoganlovells.com

Force majeure in a common law jurisdiction (English law)

- The term *force majeure* itself is not an English law concept
- Therefore, in an English law contract, crucial to define the scope of *force majeure* and rights/obligations arising from it in the contract terms
- English law principles might still be relevant in determining important questions under the clause e.g.
 - How to interpret the list of *force majeure* events;
 - The extent of an affected party's duty to mitigate impact; and
 - Causation - the affected party will still need to establish the causal link between the events and the slowdown/stoppage in performance

Other common law concepts in play during the pandemic

- Frustration: high bar to meet and (if met) its effect is to automatically discharge the contract and excuse the parties from future obligations
- English law (in summary):
 - Frustrating event occurs after contract formation;
 - Renders party's performance impossible, illegal or radically different;
 - Not available where parties' contract made express provision covering the situation (consider interplay with *force majeure* clause);
 - Contract not frustrated if alternative method of performance is possible; and
 - Contract not frustrated merely because it is more expensive to perform.
- Other common law concepts: good faith?

Force majeure in a civil law jurisdiction (German law)



Detlef Hass

Partner, Commercial Litigation
Munich

+49 89 290 12 215

detlef.hass@hoganlovells.com

Force majeure in a civil law jurisdiction (German law)



Case study:

Supply contract

NO *force majeure* clause

German law applicable

- Basic rule: Each performance obligation must be considered separately
- Relevant statutory law provisions:
 - Impracticability of performance (section 275 German Civil Code, “GCC”)
 - Legal consequence: No obligation to provide the respective performance BUT claim for damages possible, if Impracticability is due to fault
 - Frustration of contract (section 313 GCC)
 - Legal consequence: Adaption of contract through negotiations, ultima ratio: termination of contract

Force majeure in a civil law jurisdiction (German law)

Case Study: Administrative order to close respective supply business due to pandemic

Impracticability, sec. 275 GCC?

- Release from **SUPPLY OBLIGATION**
 - (+) if suppliers production, due to closure, is no longer operational
- Release from **ACCEPTANCE OBLIGATION**
 - (+/-) if customers processing production, due to closure, is no longer possible
 - (-) if customers sales is affected

Frustration of contract, sec 313 GCC?

- Effects on **SUPPLY /ACCEPTANCE OBLIGATION**
 - What to consider for negotiations?
Notification; long-term view; transparency
 - With that knowledge of facts ask...
 - Did the basis of the contract change?
 - Was the allocation of risks amongst parties materially affected?
 - Did the legislative environment cater for the problem?
 - Consequence: renegotiate contract adaption accordingly
 - Ultima ratio: terminate contract or stick to it and request damages for failure to renegotiate thereafter

Can the courts help?

- Mindset of judges regarding COVID-19?
- Availability of courts?
 - For main proceedings: questionable
 - For injunctive relief: priority of courts in many jurisdictions
- What can be done, if you have a situation which cannot be resolved otherwise?
 - Request relief for specific performance?
 - Available in more sophisticated court systems globally in exceptional cases
 - e.g. Supplier withholds/ stops performance unlawfully (e.g. *force majeure* as an excuse): requires a clear case
 - To enforce adaption of contract (sec 313 BGB): only in extreme circumstances
 - Wait and liquidate approach: Claim for damages to be filed after we will have come out of the tunnel

Force majeure process and procedure



Steven Barley

Partner, Commercial Litigation
Baltimore

+1 410 659 2724

steve.barley@hoganlovells.com

Contractual notice

- Providing notice:
 - Notice needed/recommended?
 - Amount of detail
 - Form, timing and updates
 - Implications for other contractual and business relationships
- Receiving notice:
 - Response needed/recommended?
 - Response detail
 - Implications for the existing contract
 - Implications for other contractual and business relationships

Act in good faith and remember documentation

- Good faith actions may be required and are useful in the event of a dispute
- Properly record and store communications with the other contracting party and your own compliance with the contract
- Document and retain evidence of all communications with other parties about the disruption and its effects, including order or service cancellations
- Retain documents relating to unforeseeability and/or impossibility
- Document potential damages
- If applicable, assess documentation required for insurance purposes
- Carefully document all reasonable steps taken to comply or mitigate

Prepare for the event's end

- Agree a date when obligations will resume after the event and its effects have ended, especially if the contract is unclear
- The supply chain will need time and resources to resume operations/clear backlogs
- The party claiming *force majeure* won't want to be in breach once the event is over
- If you can, explore a further extension of time for performance (you may have a right to request one under the contract)
- Better still, highlight to your counterparty that the event is over but the preventing effects are still being felt
- Effects of coronavirus are continuing and felt at different times by different parts of the supply chain - *force majeure* notices could continue to be issued after it is downgraded from a pandemic. At this stage, return to the contract wording to check if coronavirus is covered and whether the location of the *force majeure* event is mentioned. For example, would your clause be triggered if there were still an epidemic at the place of delivery but not the place of manufacture?

Review existing contracts and relationships

- Which counterparties are likely to be impacted by future *force majeure* events - engage and plan ahead
- Assess supply chain for future impacts
- Contractual assessments. Do *force majeure* clauses in your existing and future contracts allocate force majeure risk? Consider amendments.
- Consider including price adjustments, liquidated damages and other provisions not typically seen in *force majeure* clauses
- Refer to helpful industry or business practices
- Consider enhancing business continuity plans

Practical considerations



Elizabeth Donley

Partner, Corporate

Washington, D.C.

+1 202 637 5688

elizabeth.donley@hoganlovells.com

Practical considerations - today's reality

- The impact of COVID-19 on businesses continues to evolve
 - Ongoing dialogue and cooperation among customers, suppliers, governments, employees - members of the supply chain must be nimble
- Focus is on making products and performing services, meeting customer demands, paying employees
 - The goal is “business as usual” or as close as can be achieved in a challenging environment
- “Essential” designations and *force majeure* events
 - Potential conflicts between government-mandated remedies (e.g. shutdowns, shelter-in-place) versus government-declared essential supply and services (e.g. healthcare and defense)
 - Parties to consider the underlying cause for the *force majeure* and whether “essential” services can be performed safely and practically

Practical considerations - priorities and decisions

- Allocating resources
 - Suppliers may be forced to prioritize customers and end-markets, allocating resources to some, potentially to the detriment of others (e.g. distributing food and medical supplies over non-“essential” goods)
 - Businesses may need to exercise *force majeure* remedies selectively
- Risk of performance
 - Unlike some “classic” *force majeure* scenarios, with COVID-19 parties must weigh the risk of performance
- Power of relationships
 - Parties with strong relationships tend to work together to find solutions; mutual trust and investment is valuable in times of uncertainty
 - Parties with greater negotiating power may have more options
- Long-term consequences
 - Decisions made during the COVID-19 crisis may bring risk of claims in the future

Practical considerations - looking forward

- *Force majeure* will never be the same again
 - What may have been considered boilerplate, standard language intended to cover one-time, temporary events will become a focus of attention
 - Parties will have a heightened sensitivity to global events and government-imposed restrictions that may require reallocation of priorities or resources
- Coordination and collaboration
 - COVID-19 emphasizes the need for alignment of priorities and remedies across the supply chain; parties will be increasingly sensitive to being “stuck in the middle”
- Global, interconnected, supply chains
 - The value and efficiency of the multi-layer, global supply chain will not be diminished; COVID-19 demonstrates how interconnected we are as a global economy, and we expect this will continue

Q&A

COVID-19 resources

1. Access all our materials on our topic center:

[COVID-19 Topic Center](#)

2. Register your interest in our other webinar topics related to coronavirus [here](#)
3. Get in touch with one of us or via COVID19@hoganlovells.com



www.hoganlovells.com

"Hogan Lovells" or the "firm" is an international legal practice that includes Hogan Lovells International LLP, Hogan Lovells US LLP and their affiliated businesses.

The word "partner" is used to describe a partner or member of Hogan Lovells International LLP, Hogan Lovells US LLP or any of their affiliated entities or any employee or consultant with equivalent standing. Certain individuals, who are designated as partners, but who are not members of Hogan Lovells International LLP, do not hold qualifications equivalent to members.

For more information about Hogan Lovells, the partners and their qualifications, see www.hoganlovells.com.

Where case studies are included, results achieved do not guarantee similar outcomes for other clients. Attorney advertising. Images of people may feature current or former lawyers and employees at Hogan Lovells or models not connected with the firm.