



Professional Perspective

# Preparing for Covid-19 Contract Disputes

*Hyongsoon Kim, Anthony T. Pierce, Eric Gambrell,  
and Robert H. Pees, Akin Gump*

Reproduced with permission. Published April 2020. Copyright © 2020 The Bureau of National Affairs, Inc.  
800.372.1033. For further use, please visit: <http://bna.com/copyright-permission-request/>



# Preparing for Covid-19 Contract Disputes

Contributed by *Hyongsoon Kim, Anthony T. Pierce, Eric Gambrell, and Robert H. Pees, Akin Gump*

Contractual issues loom as companies wrestle with the problems arising from the spread of Covid-19, the disease caused by the new coronavirus. Overshadowed by government-mandated shutdowns, supply chain constraints, and health concerns—challenges that companies struggle to address in real time—the prospect of potential litigation may appear to be on the distant horizon, especially at a time when some court systems are limiting filings. But it is important to prepare properly, both from a legal and factual perspective, for litigation.

This article offers seven key points to consider in preparing for potential litigation regarding contractual obligations:

## Formulate a Game Plan

As business teams review contracts company-wide, they should prioritize the contracts based on impact to the company and/or the highest risk. Then consider the company's goal for each contractual situation. Does it make the most sense to void the contract, modify or defer obligations or simply perform? Which partners might be approached to negotiate new or modified deals? Is it possible to ask for a reduction in fees or deferral of payments? Are there any contracts where the situation requires immediately going into court or arbitration to seek relief?

## Maintain Consistency

Businesses should develop a plan now to avoid inconsistencies in their positions in seeking to enforce or avoid contractual obligations. This can be especially difficult in the present chaotic and constantly changing situation. Such difficulties can be compounded when the attorney handling leasing contracts is not the same attorney handling supplier contracts or customer issues. Nonetheless, a business should try to develop a global framework and a shared internal understanding of how Covid-19 is affecting its company, and make sure its internal and external communications are based on that common understanding.

For example, does the company seek to enforce contracts against its suppliers (who might be arguing force majeure or impossibility)? At the same time, does it anticipate seeking to use force majeure or impossibility to avoid obligations under commercial leases? Counsel can help to navigate these issues; there may be multiple clear and viable legal reasons, including the express provisions in the various contracts, the applicable law, and the particular associated facts, why a party can avoid obligations under one contract but the counterparty cannot avoid their obligations under a different contract. It is important to maintain consistency of internal and external communications from a factual perspective, in anticipation of possible future litigation.

## Use Every Tool

Whether seeking to have contractual obligations enforced or excused, a business should make sure to use every tool in its toolbox. Most companies are (rightly) focused on contractual provisions such as force majeure clauses, which explicitly excuse a party from fulfilling their contractual obligations. Most companies are also aware of common law defenses such as impossibility (or, in some jurisdictions, impracticability) and frustration of purpose.

However, it is important to review other potential tools as well. For example, Uniform Commercial Code §2-615 can excuse or delay contractual performance where commercially impracticable. See also Cal. Comm. Code §2615(a). Additionally, some states, such as California, have also separately codified the contractual defense of impossibility. See [Cal. Civ. Code §1511\(2\)](#).

## Consider Mitigation

A party seeking to make use of force majeure or doctrines such as impossibility to avoid contractual obligations typically will have to demonstrate that they used reasonable efforts to mitigate the impact of the current crisis. For example, is the shutdown temporary? Can performance merely be postponed, instead of being avoided entirely? Has the business attempted to obtain alternate supply before telling a customer it cannot ship their product? If attempting to cancel a vendor contract, are there alternative measures to take before cancelling such as postponement of delivery or substitution? Under

California law, for instance, a party seeking to invoke a force majeure clause must take reasonable steps to ensure performance. See *Nissho-Iwai Co. v. Occidental Crude Sales*, 729 F.2d 1530, 1540 (5th Cir. 1984) (discussing California law).

## Jurisdictional Differences

Jurisdictional differences are important not just for companies reviewing pre-existing contracts but also for companies seeking to modify or create new agreements that account for the current crisis or a potential future crisis.

For example, New York courts tend to excuse performance only where it is truly or objectively impossible. California courts, on the other hand, will sometimes excuse performance that is impracticable due to “excessive or unreasonable expense.” *Vernon v. City of Los Angeles*, 45 Cal.2d 710, 717-720 (1955).

Additionally, as noted above, certain jurisdictions have added their own statutory gloss to doctrines such as impossibility. *Cal. Civ. Code §1511(2)*, for example, excuses performance when prevented or delayed “by an irresistible, superhuman cause.”

## Consider Dispute Resolution

In addition to reviewing the force majeure clauses in contracts, businesses should also review the contract's dispute resolution clause. Depending on the language of such clause, the business may be required to arbitrate or mediate defenses such as frustration of purpose or impossibility. Knowing the likely forum may impact how and whether to choose to resolve or litigate a dispute over contractual obligations.

Further, in drafting new contracts in the age of Covid-19, consider how the business would prefer to resolve a dispute over contractual obligations. Would it be more likely to seek to enforce such obligations? If so, it may want to include a provision carving out a right to seek emergency relief, either from a court or—in light of the current widespread court closures—a pre-determined arbitral panel. When the business would prefer to avoid such obligations, it may want to include a mandatory cool-down period in which the parties attempt to negotiate a resolution before seeking any affirmative relief.

And when a business dispute arises, consider the option of non-binding mediation, which can sometimes function as a turbocharged negotiation that saves time and expense. Even if a contract does not require mediation, the parties can agree to engage a neutral third-party to mediate the dispute at any time, even after the commencement of a lawsuit. Many judges will be urging litigants to pursue the resolution of business disputes through mediation and negotiation.

## Ensure Insurance Position Consistency

With input from insurance brokers and, in some instances, from outside policyholder-oriented legal counsel, businesses should arrange for the review of insurance policies, including business interruption policies, and understand how the terms of such policies impact contractual positions. For example, insurance policies may limit coverage to or exclude specific events from the scope of coverage; a government-mandated shutdown might qualify for coverage, but health-related issues might not. Communicating with a customer about the reason for invoking force majeure, could create evidence relevant to a future insurance coverage fight.