

COVID-19: Managing commercial contracts

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24 March 2020

COVID-19 is having a significant impact on communities around the world, and New Zealand is now no exception. While the immediate focus for society is on the health implications of the virus, COVID-19 will undoubtedly also affect a number of existing contractual arrangements that New Zealand businesses have in place.

At a high level, the key contractual issues that are emerging due to COVID-19 stem from pressure on both supply chains and work forces. These pressure points affect the ability of parties to perform their contractual obligations and the cost of performance.

Commercial contracts often cater for unforeseen circumstances like an epidemic or an act of God by including a force majeure provision. This is a clause that provides for what will happen if the performance of either party to the contract is affected by certain unforeseen events.

As part of their business strategy for managing the impacts of COVID-19 and the associated uncertainty in markets, we are recommending that our clients take stock of their contractual relationships, likely pressure points arising as a result of COVID-19, and the contractual provisions that will be relevant to inform any discussions with contractual counterparties.

Each contract will need to be individually assessed on a case by case basis having regard to the potential implications on the client's business, the identity of the counterparty, and the goods or services that the client is either sourcing or delivering under the contract. Some key aspects to analyse include:

- Is there a force majeure provision in the contract?
- Does a pandemic qualify as a force majeure event?
- What obligations are relieved if force majeure is asserted and established? Is relief confined to just the obligations affected by the force majeure event or does it extend to all obligations under the contract? Does the contract provide for suspension of contractual obligations, the termination of the contract or some other variation mechanism?
- What is the procedural requirement for asserting force majeure? Many contracts require that the affected party (who wishes to rely on relief available under the clause) notify the counterparty promptly or within a prescribed period of time, and in some cases provide supporting evidence for the claim that a force majeure event has occurred
- Is there a prescribed period during which the force majeure period can subsist before termination rights arise for either party under the contract?
- Is there an express requirement for the parties to take all reasonable steps to mitigate the effect of the force majeure event?
- How are payment obligations affected if force majeure is asserted and established?
- What are the ongoing obligations to communicate with the counterparty during this period?
- Does the contract contain any insurance provisions that may respond to this scenario? For example, is business interruption insurance required under the contract, and would it be available in the circumstances?
- Even if the contract does not contain a force majeure clause, are there any other provisions that may be triggered or otherwise relevant? For example, suspension, variation or termination (without cause) provisions that may be available to either party.

If you do intend to rely on a force majeure clause to excuse you from performance (or if the counterparty is seeking to do so), the courts have held that the party seeking to be excused bears the burden of proving that its non-performance was due to circumstances beyond its control **and that there were no reasonable steps that it could have taken to avoid or mitigate the event or its consequences.**

Where you are the party:

- **Receiving** goods and/or services under the contract, it may be appropriate to front foot a discussion with your contractual counterparty and ask what, in these uncertain times, they are doing in the context of business continuity to ensure that they can continue to deliver under the contract
- **Delivering** goods or services under the contract, take the necessary steps to:
 - analyse your pressure points, and identify where COVID-19 may impact on your performance

- where practicable be (and show that you are) as prepared as possible to implement contingencies and workarounds to mitigate the effect of COVID-19 on your business and your ability to perform the contract.

If your contracts do not contain force majeure provisions, they may nonetheless contain other provisions that could be applied in the circumstances either to relieve performance or bring the contract to an end (such as the variation, suspension and termination provisions we have mentioned above). The contractual doctrine of frustration may also be applicable. This essentially relies on the party seeking to be excused from performance being able to establish that further performance of the contract is rendered **impossible** or **radically different** from what the parties had agreed because of a factor outside their control, for which they are not responsible. For further analysis of "frustration" see our article on this [here](#).

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