

FORCE MAJEURE AND IMPRACTICABILITY
FOR COMMERCIAL TRANSACTIONS AMID COVID-19

The COVID-19 global pandemic is having widespread impact in virtually every market, causing supply chain delays/cancellations, parts and goods shortages, labor shortages and facility limitations. For many businesses, these impediments were neither foreseeable nor avoidable, or at the very least, would be impractical to overcome. Many companies buying or selling goods as part of their businesses face difficult decisions compounded by the uncertainty of what to do next.

This article generally discusses the rights and obligations of companies conducting commercial transactions of goods within their businesses and the impact of “force majeure” declarations arising out of COVID-19. Three potential situations are: (1) your company as seller cannot fulfill an existing purchase order to a buyer; (2) your company as buyer received notice from a seller that it cannot fulfill an existing purchase order; and (3) your company as seller received notice from a buyer that it will not accept delivery of goods. While this article specifically addresses transactions in goods governed by the Uniform Commercial Code (“UCC”), the contract principles discussed herein may be generally applicable to other types of commercial contracts and leases.

In all situations, the analysis begins with the contractual agreements between your company and the other party. These may take the form of master agreements governing each and every transaction between the parties or may be specific to purchase order(s) sent by the buyer. A purchase order generally contains or incorporates terms and conditions governing the transaction. Absent specific contract language, the UCC (or potentially the International Chamber of Commerce regulations for international transactions) may fill any gaps and provide additional remedies for such transactions.

There is no one-size-fits-all analysis. The governing contract documents, applicable laws, and the facts underlying each individual transaction must be analyzed together on a case-by-case basis by a trained legal professional. The information provided in this article does not, and is not intended to, constitute legal advice; instead, all information, content, and materials herein are for general informational purposes only.

Key Situations:

Situation One – Your Company as Seller Cannot Fulfill an Existing Purchase Order to a Buyer:

- If your company is a seller of goods and a customer sent a purchase order timely acknowledged by your company, your company’s obligations are first dependent upon the specific contract language between the parties.
- If the contract with your customer does not include a force majeure term, then other sources such as the UCC or other applicable law, may excuse your inability to fulfill the order.

- In general, if your company is unable to satisfy customer orders due to COVID-19, it should provide written notice of such inability to the affected customers. This notice will trigger the customer's right to terminate or modify the terms of the contract.
- A "force majeure notice" or "commercial impracticability notice," is generally required to trigger force majeure protection under force majeure clause or under the UCC. While there is no legal requirement for such notice to bear any particular name or be in any particular form, the notice must generally include: (1) information on the occurrence of the coronavirus outbreak in a certain location, (2) the impact on the business, (3) inform the buyer that there will be delay or non-delivery, and, (4) when allocation is required, a statement of the estimated quota to be made available for the buyer so the party receiving the notice is aware of what happened and can begin to seek measures to mitigate the damages. Such notice should be given immediately when it first becomes practically possible.
- *If it is certain that a customer's order will be delayed, not filled entirely, or cancelled:*
 - Review the customer contract and applicable terms and conditions for terms relating to force majeure or impracticability.
 - Prepare a specific notice of force majeure/impracticability to be sent to that customer. Specifically reference the purchase order number(s), dates of those order(s), and items ordered. Specifically state the impact of COVID-19 on the customer's order.
 - If the order will be delayed, advise the customer of the time frame for filling the order.
 - If the order will be limited, state what supply is available and what the customer will receive from that supply.
 - If cancelled, state the order will be cancelled.
- *If your company is still able to effect partial deliveries (vs. complete cancellations):*
 - The UCC requires your company to fairly and reasonably allocate production and deliveries among customers (i.e. your company cannot favor certain customers over others). In performing this allocation, however, your company may consider the needs of regular customers who do not have a pending purchase order as well as your company's own requirements.

Situation Two – Your Company as Buyer Received Notice the Seller Cannot Fulfill an Existing Purchase Order:

- If your company is a buyer of goods and receives a written notification from a seller indicating it is unable to satisfy your order due to COVID-19, swift action should be taken in response. Under the UCC, upon receipt of a supplier force majeure notice, your company will have a reasonable time – not to exceed 30 days – to terminate or modify its order upon

notice to the supplier. Your contractual agreement may set forth different time limits and options for taking action.

- Under the UCC, a seller's notice triggers a limited set of options for the buyer and requires that buyer take action within a limited period of time, not to exceed 30 days. Once the buyer receives the notice from the seller, the buyer has two options: (1) *terminate the unexecuted portion of the contract* or (2) *agree to take the buyer's allocation in substitution of the contracted-for quantities*. The buyer must exercise one of these options within a reasonable time not to exceed 30 days. If the buyer does not take action, the contract will "lapse." This generally means that the seller will be excused from performance, although it could mean that the contract is merely suspended while the force majeure event is in place. If it is the latter, then the seller's obligation to sell – and the buyer's obligation to buy – may return once the force majeure is cleared. Therefore, it makes sense for the buyer to take prompt action in response to notice to eliminate uncertainty.

- *If your company receives written notice declaring the seller cannot fulfill its obligations:*
 - Determine if notice constitutes formal notice of force majeure or impracticability with respect to specific UCC orders.

 - If the notice is a formal notice of force majeure, ensure that timely action (usually within 30 days) is taken to terminate or modify order upon notice to supplier as necessary.

 - Consider damages to obtain suitable "cover" or substitute goods not supplied.

Situation Three – Your Company as Seller Received Notice the Buyer will not Accept Deliveries Pursuant to an Existing Purchase Order:

- Whether a customer can declare force majeure to terminate a purchase order or refuse delivery of goods depends on whether the purchase order grants this right. There is no gap filler provision in the UCC permitting a customer to declare its own force majeure to reject delivery of goods.

General Recommendations:

- In all cases, seek to reach terms that are mutually-acceptable. Put any modifications in writing and have all parties execute the agreement as modified. This approach will help keep supplier/customer relationships intact during and after COVID-19. Unilateral action will damage the relationship, invite disputes and create the potential for future litigation.

- Preserve all evidence related to declaration of force majeure, including but not limited to documents related to quarantines of individuals or goods, notices of sea, land, or air-related delays or cancellation, notices of factory shutdowns, cancelled permits and licenses, government regulations or any other documents related to your company's inability to perform its contractual obligations.



- Mitigate damages by taking all reasonable actions to lessen the impact of the force majeure event. Your company cannot allow damages to mount without taking reasonable action to avoid damages.
- Review and file claims under business interruption or other applicable insurance policies.

It is important to have a trained legal professional review your company's contractual dealings so timely action can be taken to minimize the negative impact of the COVID-19 pandemic on your business. Please feel free to contact your Momkus LLC attorney with questions or concerns. Our office is operating at 100% and we've been designated as an "essential service" during the crisis; your calls and emails will receive prompt attention, even if we can't personally shake your hand.