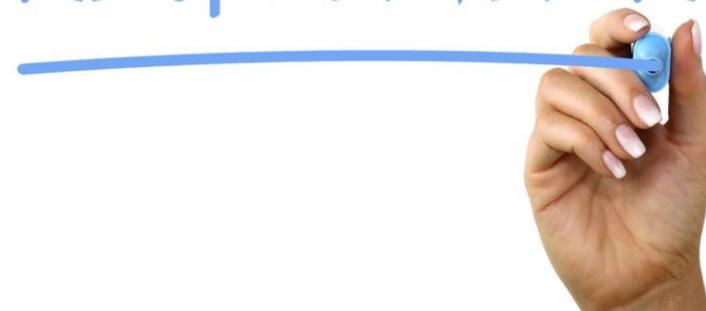


De Jure

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**The Covid-19 effect on Contract
Negotiation**

NEGOTIATION



The unforeseen coronavirus pandemic as we all know has disrupted personal lives as well as businesses. The concern is not only limited to the meltdown of the stock market or shortage in manufacturing and supply chain but also towards the performance of commercial contracts. Contracts like transaction agreements, supply and manufacturing contracts, lease and license agreements, lease arrangements, project finance and construction agreements, amongst others are likely to be affected by the lockdown imposed due to the Covid-19.



Events like the Covid-19 pandemic change the course of society for many years to come. Medical science has

advanced at lightning speed, however, it has not yet offered protection from Covid-19 and is unlikely to offer total protection from a possible future pandemic. The ultimate question that arises is: what happens next, and how to legally prepare for it?

A lot can be and must be done on the personal front in terms of legally protecting oneself. Contractually speaking however, the difficulty faced by many companies and individuals in combating the non-performance of existing contracts makes us ponder over the future of contract drafting and negotiation. In light of the present crisis, and the unfolded arguments to and fro as regards the fulfilment of a contract, makes it interesting and perhaps absolutely necessary to revisit certain clauses. In this article, we put forward the key considerations that would need to be borne in mind for negotiating and drafting a few, if not all, important clauses typically considered in transaction contracts.

Material Adverse Change (MAC)/ Effect ("MAC Provision")

This is perhaps one of the most featured and important provision of an agreement. Certain agreements that have a conclusion date, a MAC Provision is important up unto the date the transaction is concluded. For on-going agreements however, a MAC Provision remains important until the end. Let us begin with the meaning of a MAC Provision. A MAC Provision in an agreement is usually an event, development or a situation which if occurs, or is reasonably expected to have occurred, brings about a material adverse effect, on the validity and enforceability of the agreement or on the assets, liabilities, business, financial condition or operation of the entity in concern ("**Target**"). MAC Provision allows an acquirer/ investor to walk away from a transaction if an event occurs, which brings about a negative change in the Target. MAC Provision also absolves a party to a contract to not fulfil its end of the obligations, if the benefit derived by such party under the agreement, is hindered. In both cases however,

careful drafting of the agreement and the MAC provision within the Agreement are paramount, in so much so, MAC provision is not a legal protection but a contractual protection.

As such, in the current scenario what is being asked repeatedly is *whether a pandemic like the Covid-19 can be covered as a MAC and therefore affecting the agreements in question?*

The answer to this question is not simple and is certainly not standard. Whether Covid-19 would qualify as a trigger under a MAC Provision will have to be assessed along with the express language of the agreement and thereafter the essence and the very nature of the agreement. The MAC Provisions should not only be defined accurately to cover its inclusions but should also be drafted craftily to cover its exclusions. Certain businesses may very heavily be impacted by a pandemic such as Covid -19 and at the same time, certain businesses may not be. Yet again a pandemic like Covid-19 may bring to a standstill how one

party enjoys its rights under an agreement, while yet another party under a different arrangement and a different agreement may totally be unaffected by a pandemic situation such as Covid-19. Would it then be enough to draft a MAC Provision the same for all industries, all agreements and all arrangements or should it be drafted differently keeping in mind the actual impact each inclusion of the definition will have on the parties to the contract and more specifically their arrangement?

An interesting case with a much awaited verdict is the Victoria's Secret deal which is currently under a 'MAC' war. Sycamore Partners (purchaser) that had agreed to acquire a majority of Victoria's Secret from L Brands is citing Covid-19 pandemic as a reason to back out of the deal and terminate the acquisition agreement. Currently, a lawsuit has been filed in Delaware, USA by Sycamore Partners claiming L Brands had breached the terms of the deal, while L Brands countersued by claiming that Sycamore Partner's attempt to end the deal was invalid as the MAC Provision in the acquisition agreement carves out

specific exception to certain acts of god, including a pandemic. It will be interesting to see the outcome of this particular dispute.

Force Majeure



Another very important provision/ clause of most agreements and that has been the centre of discussion during this pandemic is 'Force Majeure'. Force Majeure means 'causes you cannot prevent and for which you are not responsible'.

The biggest challenge faced by certain parties due to the Covid-19 crisis is in performance of various contractual

obligations. When approached by these parties, it became extremely important to examine the force majeure clause in the contract in question, as the implication of the clause largely depended on the wording of the clause than the situation itself.

Ultimately, whether Covid-19 is a force majeure event depends on a case to case basis. If the force majeure clause has a wide meaning, it would be difficult to interpret whether Covid-19 would trigger as a force majeure event. However, if the clause uses the words like 'pandemic', 'epidemic', or 'any other situation making the business impossible', it may be argued strongly to be categorised as a force majeure event.

And yet the occurrence of a situation that comprises force majeure cannot be conclusive evidence that the force majeure event has triggered, if the effect of such situation is not adverse.

As such, while drafting an agreement and including a force

majeure clause and a definition that lists what exactly would cause a force majeure, one must carefully study the industry being dealt with, and include in the definition the events that would actually affect that industry and leave out events that may have no bearing on the industry. Likewise, the nature of contract and the end means of a contract must also be studied.

Please see [here](#) another article authored by our Firm on force majeure.

Change in law



The Government of India has already introduced various measures, laws and guidances regularly to try and control

the spread of Covid-19 affecting health as well as businesses. It is a good time to ponder upon the use of the 'change in law' clause. A 'change in law' clause entitles either party to terminate or renegotiate the contract, in the event of a change in law which makes either party unable to perform its contractual obligations.

In the landmark judgment of *Energy Watchdog v. Central Electricity Regulatory Commission* [(2017) 14 SCC 80], the Supreme Court held that the change in law includes all laws in force in India. This broad interpretation by the Supreme Court becomes a valuable precedent for agreements having the provision for 'change in law'.

Such a provision can be negotiated to provide for a way to allocate the increased costs incurred and suffered by the respective parties. The parties may even mutually agree upon a threshold limiting the increased costs suffered by a party due to change in law.

Where the party is ineligible to qualify for the force majeure clause or even frustration of contract under the Indian Contract Act, invoking a detailed and well worded change in law clause would be beneficial for such a party. It should become an important provision especially in long term contracts related to infrastructure, construction, project finance, and employer-contractor based contracts.

Conditions Precedent

Conditions Precedents are a set of events that must either occur or be met with by either party before the parties can close on a transaction.

Considering the pandemic situations, negotiating conditions precedents will depend primarily on the deal certainty, meaning how certain the parties are to close the deal successfully after executing the transaction documents. Deal certainty largely depends on the period between signing and closing (Long Stop Date). The purchaser would want to keep the Long Stop Date closer

to the execution date and the Target would want to extend the Long Stop Date. To tackle this situation, the Target should negotiate to include lesser Conditions Precedents to decrease the burden on the Target and increase the deal certainty. To have fewer conditions precedents the parties should negotiate depending on what conditions are in the control of the Target and what are not in its control. Having said that, parties will have to keep in mind conditions which are not in its control but are mandatory for a deal to come through (like regulatory approval, approval from lenders, etc). The Target may also look to move certain conditions precedents to conditions subsequent, if feasible.

Long Stop Date

When a transaction is nearing the closing stage, the parties may face difficulty (especially the Target) in acquiring regulatory, Governmental, or third party approvals, in the event regulatory authorities, government departments, concerned offices, or banks are shut down

due to any political, environmental, or health related crisis. The parties may also fail to fulfil its pre-closing obligations, covenants, and conditions precedent due to a lockdown scenario. Many M&A transactions in India are implemented by using the scheme of amalgamation which required the functioning of Courts. However, in a situation like this, the Courts and Tribunals were either shut or were only hearing urgent cases which delayed the implementation of such schemes. The lockdown restrictions may also affect the stamping and registration of contracts. Certain conditions like obtaining a valuation certificate or completing the due diligence may also take more time than expected.

Given all of the above, the parties (particularly the purchaser) may consider negotiating to extend the Long Stop Date or include a provision in the definition for mandatory extension of the Long Stop Date exclusively in case of pandemics or alike catastrophes, apart from the general term usually present to extend the Long Stop Date mutually agreed upon by the parties.

Representations and Warranties



Representations and warranties are nothing but statements of facts made by one party to a contract to another, before or at the time of signing the contract. If there is any breach of representations and warranties made by any party, the other party can claim for damages for any loss that it may suffer due to that breach.

Certain precautionary measures to keep in mind while negotiating representations and warranties, considering the present crisis are set out below:

- the receiving party must evaluate the risks originating due to the crisis and could accordingly ask for specific

and intensive representations and warranties, especially since the lockdown may have interfered with the process of due diligence (on-site visits, procuring documents, lack of working staff);

- the party giving the representations and warranties on the other hand, should focus on including specific knowledge and materiality qualifiers and consider disclosing detailed facts concerning the crisis in its disclosure schedule.

Indemnity

If the Covid-19 pandemic continues for much longer, we believe that the seller-friendly market will soon turn into a buyer-friendly market. This will change the way indemnity clauses are negotiated. Generally speaking, there is some degree of trust between an investor and the Target but with Covid-19 and its implications, we might see a significant dent in the trust.

On the other note, the indemnity insurance will become a famous product especially for the Target. A Target may look to explore various policy coverages to mitigate losses arising out of loss of operations or productivity.

Conclusion

In these testing times, the day to day life of a human to functioning of a company, everything has been impacted and the entire nation has been put into an ever stretching lockdown. The pointers put forward by us are for a few important clauses which parties to a contract may consider to negotiate in light of Covid-19. However, the precise details of any commercial contracts lies in the context of their relationship and external circumstances and the view set forth are general in nature and matters of opinion.

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