

## **LANGUAGE OF CONTRACTS WILL DETERMINE THE OUTCOME OF LITIGATION ARISING FROM COVID-19**

The lockdown amidst the COVID-19 pandemic has hit the ability of many business organizations to honour contractual obligations towards their lenders, suppliers, clients and other parties. In an interview to MVIRDC World Trade Center Mumbai, Mr. Dipti Lavya Swain\*, Partner, HSA Advocates explains the legal recourse available for companies that are unable to meet their contractual obligations under this circumstance.

Mr. Swain points out that courts may not be able to rewrite a contract and therefore the language of the existing contracts will be a driving factor for courts to decide whether or not the contract had contemplated such an extraordinary situation.

Mr. Swain is a legal specialist in corporate restructuring and mergers & acquisitions. He is also an advisor on Energy Laws, Insolvency & Bankruptcy Code, Data Laws, Startups enterprises etc. He has been the Managing Partner of DLS Law Offices and Partner at Luthra & Luthra Law Offices.

### **Excerpts of the interview:**

#### **1. Many commercial entities have invoked force majeure, frustration of contract as they are unable to meet their contractual obligations amidst the nation-wide lockdown to combat COVID-19. How will this impact the corporate world?**

Yes, force majeure is the talk of the town globally, including in India. A force majeure event is the occurrence of an extraordinary event (generally explained in the contract) which is beyond the control of any of the parties to such contract thereby impacting the ability of the party to perform its part of the contract.

Most contracts between parties generally have a force majeure clause, however, it also depends on the nature of an underlying transaction. For example, debt transactions generally don't allow benefit of force majeure to borrowers. Similarly, large infrastructure and energy contracts or supply contracts generally have detailed force majeure clauses. While governments worldwide including in India have acknowledged that COVID-19 is a prima facie or clear case of force majeure private contracts may not be the same. Critical aspects are the definition of force majeure which outlines what constitutes a force majeure, trigger events and next steps in case of a force majeure (for example notice requirements) and what are all the consequences of triggering the same. It is for this reason that a dispute may arise since in most cases, one of the parties is likely to not like the happening of force majeure, leading to differences and thereafter litigation.

In India and in many other common law countries, unless the contract provides for a force majeure situation, it cannot be automatically triggered. In the current COVID-19 scenarios, the other options that Indian firms have is frustration of contract which may ultimately lead to termination of such contract, which again may provide the desired consequences since parties may only be looking out for temporary solutions.

In case an Indian company has executed a contract without a force majeure clause with a foreign party and such a contract is governed by Indian laws, the affected party may invoke 'frustration of contract' under Section 56 of the Indian Contract Act, 1872 after careful analysis and seeking advice from lawyers on the impact of the same. The nuances and complexities will increase in case such contract is not governed by Indian laws and legal advice must be sought on how to handle such situation. Parties must therefore make careful analysis and seek legal advice before taking any steps to invoke force majeure.

## **2. Are courts likely to acknowledge COVID-19 as a force majeure event?**

Yes, courts in India and elsewhere are most likely to acknowledge COVID-19 as a force majeure event. In fact, most courts have also suspended regular court hearing days and resorted to e-filings and hearing of only urgent matters.

However, it is important to note that courts may not be able to rewrite a contract and therefore, as I mentioned, the language of the existing contracts will be a driving factor for courts to decide whether or not the contract had contemplated such situation and the consequences that are being desired by the concerned parties.

## **3. The government has introduced many amendments and provided relaxations in the provisions of IBC law to prevent firms facing liquidity crisis from going into insolvency process. Would you like to suggest further policy measures to provide relief to distressed firms in this circumstance?**

Yes, Government of India has announced various measures to handle the current crisis brought about by COVID-19, including under the Insolvency & Bankruptcy Code, 2016.

The Ministry of Corporate Affairs vide a notification dated March 24, 2020, has increased the threshold for initiating the insolvency resolution process from Rs 1,00,000 (USD 1,300) to Rs 1,00,00,000 (\$130,000) under Section 4 of the IBC.

The Government is also considering suspension of certain important provisions of the IBC like Sections 7, and 10, for a period of six months, which will disable the financial creditors, operational creditors and promoters from initiating insolvency proceedings against companies (corporate debtors).

There could be other measures also, such as exemption from IBC, with or without the applicability of time, being provided to certain types of companies such as startups, or companies in certain sectors such as renewable energy. Lenders in most situations are going to be hit in case of such exemptions and since the PSU lenders in India have some of the largest exposure to these areas, the government will have to eventually capitalise such lenders. Since these will carry large repercussions, existing data must be analysed for consequences prior to bringing about such policy measures.

## **4. Do you feel the COVID-19 will force many small and large companies to file for bankruptcies? Which are the sectors that may be the worst affected by the crisis and how?**

Yes, many small as well as large companies are under financial distress due to disruptions in their supply-chains, revenues and business because of COVID-19. Many of these firm may come under corporate insolvency resolution process (CIRP).

Unfortunately, most sectors are affected by COVID-19 and it is only the test of resilience, market spends and innovative business models that a business will have to pass in order to sail through the crisis period. Sectors in the non-essential goods and services space are the worst hit since lockdowns have dampened their business plans and efforts. As a result, despite government's efforts and advisories,

there is a possibility of job losses leading to lower purchasing power of individuals and create a cyclical effect on the economy. Legal documentation and analysis will therefore be key to every business in the current scenario as well as in the future.

Even sectors in the essential goods and services space which seem to be on the run due to lockdowns everywhere are facing financial crunch owing to several economic factors and therefore it is hard to say that a particular sector is doing well.

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