

Ukraine Crisis: What it Means for English Law-Governed Contracts for the Supply of Goods and Services

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The worldwide supply chain is under increasing pressure from the continuing conflict in Ukraine. A growing list of companies are required to suspend or exit operations in Russia as Western sanctions render performance of contractual obligations illegal or in breach of public policy. However, for some companies it is simply a matter of it no longer being commercially viable to continue doing business in Russia.

All businesses with operations in Russia will need to review their supply contracts to assess the implications of the war and consider the best way to comply with their contractual obligations and, if necessary, take steps to protect their position.

There are a number of key considerations for English law-governed contracts for the supply of goods and services:

1. Termination

- Not all supply contracts will contain a termination clause that allows a party to terminate at will. For example, a contractual right to terminate may only arise where there has been a breach of a material term of the contract (for example non-payment).
- In the absence of a breach of a material term, a company that wants to terminate a supply contract because it no longer wants to do business in Russia must seek to rely on alternative methods of termination.

2. Force majeure arising from disruption

- A force majeure event refers to the occurrence of an event that is outside

the reasonable control of a party that prevents or delays a party from performing its obligations under a contract. It is an agreed allocation of risk between the parties on the occurrence of a specific intervening event.

- You will need to consider the scope of the force majeure clause (i.e., does it expressly anticipate the war), whether there are any exclusions for foreseeable events and the extent to which the war has affected your ability to perform under the contract (and whether it was the sole cause of any such non-performance).
- A party's ability to terminate the contract for a force majeure event depends upon the terms of the agreement and force majeure provision. It is not uncommon for a force majeure clause to only limit a party's liability to the extent its failure to perform the contract is caused by the occurrence of a force majeure event – it does not provide a right to terminate the contract.

3. Frustration arising from war as supervening event

- The English law doctrine of frustration refers to the common law right to terminate a contract following the occurrence of a supervening event for which neither party to the contract is responsible.
- The supervening event renders the performance of such contract either impossible or of a radically different nature (as compared to what the parties envisaged when they entered into the agreement).
- This is a high threshold, and the nature of the supervening event and your assessment as to the possibility of future performance of the contract in the new circumstances will be scrutinized by the court. Additional cost, hardship and delay are not of themselves sufficient to frustrate a contract (although for delay, this may be a question of degree).
- The inclusion of a force majeure clause may (if it has been carefully drafted) displace the doctrine of frustration.

4. Illegality arising from sanction / export controls

- The doctrine of illegality may apply to commercial parties whose contracts are affected by government sanctions imposed against Russia and certain Russian entities, since English law provides that neither party can enforce a contract where both parties are aware that performance of the contract would involve committing an act that is either illegal or against public policy.

5. MAC triggered

- Your contract may include a Material Adverse Change (MAC) clause that is

aimed at addressing unforeseen or unpredictable events which affects one party or both parties to a contract.

- MAC clauses have rarely been considered by the English courts, but the interpretation of the clause will follow the usual English law principles of contract law, and the burden of proof will be on the party seeking to rely on the clause.
- A MAC clause that refers to the deterioration in a counterparty's business prospects may be more easily triggered than one that requires a proven deterioration in the counterparty's financial position as a result of the MAC event (i.e., the war).

6. Other contractual clauses

- You should consider whether the war could trigger any other contractual term in your supply contract. For example, the war could trigger a price escalation clause which has been designed to ensure that a contract does not become too financially onerous on one or both parties. Or perhaps the war has caused liquidity issues for your counterparty that has triggered an insolvency event thereby giving rise to a contractual termination right.

Actions

- You should review your contract carefully to check whether performance is still required and whether you have a contractual or common law right to terminate the contract.
- If the counterparty does not mutually agree to the termination of your contract, litigation risk arises from the potential that you may be sued for damages for repudiatory breach of the contract on the basis of termination without grounds (or on incorrect grounds).
- In assessing the litigation risk, you should consider whether there are any limits on liability in the contract or there are steps that can be taken to mitigate any potential damages claims, for example, providing a grace period for the counterparty to transition to a new supplier.

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