COVID 19 and Contracts: What does your direct selling business need to know?

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Three months have nearly passed since Coronoavirus (**COVID 19**) was first reported to the World Health Organisation (**WHO**).[1] Since that time, the virus has had an increasingly adverse and unforeseeable impact on the global economy, affecting trade, travel, manufacturing and all aspects of the supply chain. Businesses are now starting to feel a very significant impact on their operations and bottom line, including those in the direct selling sector. While many direct selling businesses are well-placed in terms of having a considerable online presence and have been engaged heavily in digital social selling for some time (social distancing requirements may not be too problematic), your direct selling business should know where it stands in the event that either it, or its suppliers, begin to experience problems with performing contractual obligations.

We look at how direct selling businesses can be better prepared by ensuring that you are aware of two legal concepts:

- force majeure; and
- frustration,

which may enable the performance of contracts to be suspended or terminated.

A force majeure event or frustration. which occurs as a result of the impact of COVID 19 may impact the performance of, for example, manufacturing, distribution and supply agreements; trading terms; service agreements; event and conference contracts and employment agreements.

Force majeure

Parties to a contract can agree to include a clause (known as a “force majeure” clause) which may, if certain circumstances are satisfied, excuse a party from its obligations to perform. As Australian common law does not recognise the doctrine of force majeure, such a clause must usually be included expressly in a contract for a party to be able to rely on the clause. As a consequence, many commercial agreements include a force majeure clause so there is no doubt as to the parties’ intention should a force majeure event occur. A government ordered closure of borders may qualify as a force majeure event where it prevents a keynote speaker from attending a conference they are scheduled to appear at in a different country.

To be prepared, you should assess your commercial agreements:

- Do your commercial agreements include a force majeure clause?
- If so, what events are expressly referred to as “force majeure” events? Pandemics? Border restrictions? Government action?

[1] See the WHO’s COVID-19 dashboard here.

- What are the notice requirements? Parties are often required, for example, to provide written notice of the date when delay of performance first commenced. It is important to ensure that any notice requirements are met so that rights arising under the clause are not waived.

- Does the occurrence of a force majeure event trigger a right to terminate the contract? If so, must the event occur for a particular length of time?

If your business were to seek to rely on a force majeure clause, it is required to prove that an eligible force majeure event has occurred. It may also be required to provide evidence of the event's impact and reasonable steps the business took to mitigate the event's effects.

What about if your contracts do not contain a force majeure clause? "Frustration" may be relevant.

Frustration

The doctrine of "frustration" is recognised by Australian common law. New South Wales, Victoria and South Australia also have legislation which regulates how the doctrine works.[2] "Frustration" will occur when:

- after a contract is made; and

- without default by the parties to the contract,

a contractual obligation is no longer able to be performed because circumstances have made performance "radically different" to what was required by the contract. Accordingly, when assessing whether "frustration" has occurred, you need to consider the terms of the contract and the event(s) which have occurred to see whether performance is radically different to what the parties intended.

In Australia, frustration has been found to have occurred in connection with a wide range of contracts, including licence agreements, employment contracts, sale agreements, lease agreements and construction contracts. However, a contract will **not** be frustrated just because a change is temporary or the performance of obligations has suddenly become expensive.

If large gatherings are declared unlawful, for example, the venue contract for a direct selling company's annual conference may be frustrated. If frustration has occurred, the contract terminates automatically and the parties are unable to claim damages for non-performance because no party is at fault (in those States and Territories without specific frustration legislation). Using NSW as an example, the *Frustrated Contracts Act 1978* provides for the repayment of money paid before frustration and payment for part of all costs incurred in performing the contract which are reasonable. Accordingly, you should check what State or Territory law applies to your contracts.

What to do?

We recommend that you review your existing contracts to see what risks may arise if performance of obligations is hindered. In particular, consider how a "force majeure" event is defined and if there are

[2] In NSW, the *Frustrated Contracts Act 1978*. In Victoria, the *Australian Consumer Law and Fair Trading Act* 2010. In SA, the *Frustrated Contracts Act 1988*.

particular time/notice requirements. Ensure that notice and requirements are met so you do not inadvertently waive your rights. You should also be collecting evidence showing that a force majeure event is/has occurred and implementing mitigation strategies.

If you have any questions, please give us a call.

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