

COVID-19 Pandemic – What Should I Do if My Counterparty to an Important Contract is Applying Pressure to Change Our Agreement?

by Joseph Lewin

As the economic impacts of the COVID-19 pandemic continue to grow, many businesses are faced with unprecedented challenges.

As businesses struggle economically, they may face pressure from their contractual counterparties to agree to enter into or to change contracts on unfavourable terms in circumstances in which they have no choice other than to accept.

If you are faced with a situation where a counterparty to an important contract is attempting to use the impact that the COVID-19 pandemic has had on your business to its advantage in order to apply pressure to change the terms of an existing contract, or to enter into a new, less favourable, contract, what can you do?

This article is designed to help you to determine when you may be in a position in which:

- i. you can resist the unreasonable demands that your counterparty is imposing and force your counterparty to perform its contractual obligations; or
- ii. you can cancel the contract entirely.

The recourse available to you will depend on whether a legally binding agreement had been entered into already or varied as a result of the illegitimate pressure which you had no choice but to accept in order for your business to survive. In these circumstances, raising economic duress may offer a remedy.

Economic Duress

Unlike physical duress, in which threats of violence or physical harm are used to force a party to enter into or vary a contract, economic duress arises where a party is put in a position where, as a result of threats of illegitimate economic conduct, it has no alternative but to agree to enter into or vary a contract on unfavourable terms.

Economic duress may arise if you have agreed to enter into a new contract, or agreed to

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change the terms of an existing contract, as a result of illegitimate economic pressure.

One example might be where a counterparty threatens to cancel a supply contract unless the other party agrees to pay an increased price, when it had no legitimate basis for doing so, and the other party has no other practical option but to accept the new terms.

If economic duress has occurred, you have the option of terminating the contract and may be able to claim compensation from your counterparty for any loss that you have suffered as a result.

In order for economic duress to arise, the following circumstances must exist:

- i. The pressure applied must be “illegitimate”. This might be the case when the counterparty has threatened to do something that it is not entitled to do, for example, cancel a binding contract. A hard bargaining position alone is unlikely to amount to illegitimate pressure: case law indicates that the illegitimate pressure must be distinguished from “*the rough and tumble of the pressures of normal commercial bargaining*”.
- ii. The illegitimate pressure must have induced the innocent party to enter into the contract or to change / vary the terms.
- iii. The threat of illegitimate pressure must have left the innocent party with no alternative choice but to submit to the change.

As such, economic duress is unlikely to be established if the innocent party could have walked away from the contract, for example if the subject matter of the contract could have been sourced elsewhere, e.g., by engaging an alternative supplier. It is necessary to demonstrate that the counterparty has threatened to do something illegitimate, and that there was no option but to accept in the short term.

Whether or not illegitimate pressure has been applied will depend on the particular factual circumstances, and the courts will take into account several factors when determining this, including:

- a. whether there had been an actual or threatened breach of contract;
- b. whether the party applying the pressure acted in bad faith;
- c. whether the innocent party protested when the pressure was applied;
- d. whether the innocent party had any practical alternative; and
- e. whether the innocent party later did something to affirm the contract.

If you think that you have been a victim of economic duress, it is important to consider your legal options and to act as soon as possible. If you delay, you may lose the right to terminate the contract.

A. Your counterparty is applying illegitimate pressure so that you enter into a new contract or change the terms of a contract.

If you are faced with a situation where you have entered into a binding agreement which your counterparty is trying to alter in its favour by applying illegitimate pressure, you should consider whether you are in a position to refuse those changes.

If your counterparty refuses to perform its obligations and breaches the contract as a result then, depending on the circumstances, you may be able to:

1. force your counterparty to perform its contractual obligations by making a claim to the Court for specific performance; or
2. claim compensation for any loss that you have suffered from the breach.

B. You have entered into or changed the terms of a contract because of illegitimate pressure.

If you agreed to enter into or change a contract because of illegitimate pressure applied and you no longer wish to proceed with the contract, economic duress may arise which would give you the option to terminate the contract. In these circumstances, you would need to closely consider the following as soon as possible:

1. Ensure that you collect any evidence which demonstrates that you were unwilling to agree to the changes but that, given the threatened behaviour, you had no practical alternative but to accept your counterparty's demands.
2. Inform your counterparty in writing that:
 - a. your rights are reserved; and
 - b. you are only proceeding as you have no practical alternative.
3. Avoid taking steps to affirm the contract subsequently, for example, by continuing to perform the contract once the pressure from your counterparty has been lifted.

If you think you have been a victim of economic duress, legal advice should be sought before taking any steps.

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