

Covid-19's far-reaching effects

A look at the coronavirus' impact on contracts and other considerations in Malaysia and Asean

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Covid-19 as a global pandemic has massively strained public health services, disrupted global supply chains and business activities, and crashed stock markets worldwide.

Malaysia became the first Asean country to impose an aggressive 14-day movement control order (MCO) nationwide, effective from March 18, 2020 to help flatten the curve of infection. This resulted in temporary closures of non-essential businesses, educational institutions, selective governmental services and restrictions on inter-state travel.

Businesses are bound to face hardship, and it is important to stay calm, vigilant and prepared. This article is intended to be an overview of potential legal and commercial issues arising from disruptions brought about by Covid-19 to help guide businesses through these challenges.

Business contracts

Can we avoid fulfilling our contracts because of Covid-19?

There may be difficulties in fulfilling contractual obligations, given the current circumstances. Whether or not a party can delay, suspend or terminate a contract depends on whether there has been a force majeure event, or an event that frustrates the contract.

What is force majeure?

Force majeure generally refers to unforeseeable events or circumstances that hinder or prevent someone from performing a contract. In Malaysia, force majeure must be expressly provided for in the contract, and such provisions are typically found in manufacturing, supply, services and construction contracts. What constitutes a force majeure event depends on the precise wordings of the force majeure clause.

If you are considering whether Covid-19 has triggered a force majeure, you should review your contract to determine if there is a force majeure provision. If so, consider if terms such as "epidemic", "pandemic", "quarantine", "government restrictions" or "global health emergency", or catch all phrases like "events beyond the reasonable control of the party affected" could potentially apply to the current situation.

Establish that any delay or disruption in fulfilling contractual obligations is not within the reasonable foresight of the parties. While an epidemic could be reasonably foreseen, given other viral outbreaks such as SARS, it is arguable that the current unprecedented level of disruption is unforeseeable.

Establish a causal link between the outbreak or ensuing governmental actions, and the delay or failure to perform the contract.

Be careful not to wrongly declare a force majeure event. This could be construed by

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the other party as a repudiatory breach, giving the party a right to claim damages for breach.

Take reasonable steps to mitigate the effects of the delay or failure to perform. Failure to do so may undermine your ability to rely on the clause.

Check if there are specific notification requirements that apply in a force majeure event, ie, timing and how the other party is to be notified. Such requirements should be strictly adhered to.

Consider if it would be better to renegotiate or discuss with the other party on a constructive solution to deal with the disruptions, rather than ending the contract.

What if a contract does not have a force majeure provision?

If there is no express force majeure provision in the contract, check if there are any other contractual provisions that may have a similar effect. "Material adverse change" (MAC) clauses generally give buyers, lenders and investors a right to withdraw from the deal if an adverse event detrimental to the target or investment takes place. MAC clauses are typically found in transactional contracts such as property, business or share purchase agreements, and security and financing documents.

Can a contract be discharged by frustration?

In the absence of contractual provisions, parties may alternatively seek to rely on the doctrine of frustration, which applies by operation of law. In Malaysia, for a discharge by frustration to be successful, one would need to show that the event or change in circumstances were not self-induced, and renders the performance of a contract radically different from what was originally undertaken, to the extent that the court must find it unjust to enforce the original promise.

The Asean perspective on force majeure and frustration

The concepts of force majeure and frustration generally apply in Asean jurisdictions whether they are common law, civil law or hybrid jurisdictions. The requirements, however, differ across borders.

Jurisdictions such as Malaysia, Singapore,

Brunei, Myanmar and Laos require force majeure to be expressly stated in the contract in order to be recognised. With limited exceptions, the same applies for Cambodia. Other jurisdictions in Asean may not require explicit contractual provisions, and force majeure applies by operation of their respective laws.

Except for Indonesia and Cambodia, the doctrine of frustration which may be applied through the operation of various laws in Asean, could also be a possible fallback for affected parties.

Future proofing

With the lessons learnt from this pandemic, businesses would do well to review their key contracts and standard agreements and consider how these can be future-proofed.

Force majeure, MAC and termination provisions

With the benefit of hindsight, businesses should consider if future contracts should be drafted to provide more certainty of enforcement in the event of disruptions arising from an epidemic or pandemic. Businesses can also look at whether existing contracts should be renegotiated with business partners in anticipation of potential issues arising from Covid-19.

Disclaimers and exclusion clauses

Disclaimers and exclusion clauses seek to limit or eliminate liability. Businesses and organisations having higher face-to-face interaction such as event organisers, F&B outlets, malls, transportation and delivery services may wish to consider having such exclusion clauses or disclaimers in place to protect themselves against potential liability arising from any outbreak. If so, such disclaimers should be unambiguous and reasonable.

Mergers and acquisitions (M&A) and financing transactions

Due diligence, whether in the context of M&As, financing transactions or compliance, seeks to identify material legal, financial and operational risks. In conducting due diligence, there will need to be increased focus on supply chain disruption risks and also whether business continuity plans are in

place to address serious disruption arising from curbs imposed by regulatory authorities.

Businesses should closely monitor developments where certain regulatory bodies may be closed or services limited, which may impact approval applications, stamp duty payments or document registrations, which, in turn, may impact contractual time lines.

Businesses need to review completion valuation mechanisms, for example, where completion is tied to the market value of listed shares, and there is stock market disruption.

Compliance

As a result of the MCO pursuant to the Prevention and Control of Infectious Diseases Act in Malaysia, only premises that provide essential services may be opened, provided that the number of employees and customers at the premises are kept to a minimum.

Businesses should therefore be mindful to comply and not operate in breach of such restrictions. Businesses should also continually monitor any changes in the implementation of the MCO, including the updates from Malaysian authorities and agencies. There is also potential corporate liability on the company and its officers, should an employee breach the MCO.

Employers have a legal responsibility to ensure a safe and healthy workplace for their employees. Businesses should continually monitor developments, advice from the World Health Organisation and directives from their governmental and local authorities, and consider how these may impact their workforce.

Workplace health and safety systems and protocols, and preventive measures to reduce the chances of infection, should be in place, and effectively communicated to employees. In Malaysia, employees of business premises that are required to close during the MCO will be entitled to receive their wages and applicable allowances. Work from home arrangements are also permissible.

For regulatory reporting, submissions and filings, various laws require submissions of quarterly or annual reports, as well as convening of annual general meetings (AGMs). Businesses should monitor whether any respite from such obligations has been given. For example, in Malaysia, public-listed companies have been given flexibility in the submission of their quarterly and annual reports, and the holding of AGMs. Tax submission deadlines have also been extended.

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Schroders: World economy to shrink by 3.1% this year

PETALING JAYA: This year is poised to be the worst year since the 1930s and Schroders has forecast the world economy to contract by 3.1% before rebounding by 7.2% next year.

The global asset managers said the coronavirus (Covid-19) has had a severe effect on global economic activity. It forecasts a severe recession in the first-half of 2020, and even with a rebound, it will be the worst year of activity since the 1930s.

Other outfits also have predicted a recession. Earlier this week, the Organisation for Economic Cooperation and Development said it expects global growth to halve to 1.5%.

Goldman Sachs expects it to shrink by 1.0% this year.

Bloomberg Economics said it will shrink almost 2% year-on-year in the first-half, with the euro area suffering the worst back-to-back quarterly contractions in its history.

Schroders in a note released yesterday said although there was considerable support from central banks and governments across the globe, the dramatic downturn reflects the effect of shutting down large parts of the economy as the authorities attempt to suppress the virus.

"An indication of the magnitudes can already be seen in the latest data from China, where we saw falls of 20% in retail sales and 25% in fixed capital investment during the period when much of the economy was in lockdown," it said.

The process of locking down and restricting population movements to suppress the spread of the virus will result in significant hit to acidity in the second quarter in the United States and Europe, with falls in gross domestic product (GDP) of between 10% and 20% (not annualised).

"Such outcomes have rarely been seen in the post-war economies where normal fluctuations in GDP are between 1% and 2%," Schroders said.

Its forecast takes into account the monetary and fiscal policy moves around the world, and expects more.

"We see these as a safety net to cushion the economy and limit the damage from the fall. It is vital that the financial system continues to provide liquidity to firms and

households so they can withstand the impact of the collapse in activity on cash flow.

"Otherwise, a temporary hit will cause permanent damage to the supply side of the economy. If we see a widespread collapse of business, there will be little left to support the recovery," it said.

It added that lower interest rates were less important than measures to ensure banks have the confidence to lend rather than foreclose on borrowers, and liquidity continues in commercial paper and credit markets.

It also warns of the risk of the virus returning after the restrictions are lifted. That could lead to a different scenario and it could be another recession, a double dip in activity.