

Anticipatory Breach of Contracts May Become More Common in a Time of Uncertainty

Article

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The term “anticipatory breach” or “anticipatory repudiation” does not come up very often outside of the courtroom, but in this time of COVID-19 and disrupted supply chains around the world, it deserves a closer look. Anticipatory breach occurs when a party to a contract demonstrates, either through its words or its actions, that it does not intend to comply with one or more of its obligations in the contract. Falling behind on performance in terms of time, quantity, quality or other measure does not, by itself, equate to anticipatory breach. The anticipatory breach comes in the *definite and unequivocal* refusal, either through actions or words, of a party to fulfill its obligations under the contract. Anticipatory breach usually comes up in the sale of goods, but can also apply to services.

A party faced with anticipatory breach by the other party does not have to wait until the other party actually *fails* to perform (and damages actually start to accrue), but may immediately seek appropriate legal relief. This is a definite advantage in a time of uncertainty. Article 2 of the Uniform Commercial Code (UCC) provides remedies for a party faced with anticipatory breach or repudiation by another party in the context of sales. First, the “aggrieved” (*e.g.*, wronged) party can wait for performance by the repudiating party for a commercially reasonable time. Keep in mind that the meaning of “commercially reasonable” during a pandemic such as COVID-19 may be dramatically different from its meaning during other less extraordinary times. Second, the aggrieved party may resort to any remedy for breach, even though the aggrieved party has notified the repudiating party that it would await the repudiating party’s performance and has urged the repudiating party to retract its intention to breach. Finally, the aggrieved party may suspend its performance of the contract in addition to suing.

An example of anticipatory breach in the context of the current pandemic would be a scenario in which “Supplier” and “Customer” are parties to a contract where Supplier provides Customer a critical medical part for Customer to use in manufacturing Customer’s medical equipment. Demand for Supplier’s parts goes through the roof during the COVID-19 pandemic and Customer learns through Supplier’s online blog post that Supplier is immediately and indefinitely allocating

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all of its current and future production of the critical part to fulfill a different customer's orders under a more lucrative contract. Can the Customer rely on the Supplier's blog post to claim anticipatory breach to protect itself and seek relief? Under this example, assuming the blog post was genuine, the answer is probably yes. If, however, the Supplier still intends to fulfill the Customer's order, but is only temporarily delaying performance, the issue becomes murkier.

There are a variety of reasons why a party doesn't hold up its end of the bargain —particularly when that party finds itself in economic difficulty or made a bad deal. Often, a party may find paying damage is simply easier or more cost effective than performing. That is little comfort to a business that absolutely relies on performance and stands to lose business in turn when a critical supplier or contractor repudiates prior to performing their obligations. Also many contracts contain limitations on consequential or indirect (*e.g.*, lost profits) damages, making the outcome of a breach even worse. We may well see more of this behavior as supply chains are stretched and shortages and other limitations arise due to the novel coronavirus and the various attempts by governments to limit the spread of the virus by limiting travel and interaction.

But what about force majeure, which allows a party to escape its contract obligations under certain circumstances involving unforeseen circumstances beyond the control of that party? My colleagues Alex Kay and Joe Tierney have posted an excellent article on force majeure. There is something of a fine line between a party seeking to use force majeure (a creature of contract interpretation and case law) to excuse performance and being guilty of anticipatory repudiation (enshrined in statute in the UCC) on the other. A non-performing party to a contract will often attempt to rely on a force majeure clause to excuse its failure to perform. But not every contract contains a force majeure clause and even if such a clause is present, circumstances sometimes arise which bring nonperformance of a contract outside of the scope of force majeure. Many force majeure events are also often narrowly tailored as the result of the back-and-forth negotiation process in contracting. What then? If a party to a contract conclusively establishes that it will breach by failing to perform, the wronged party may treat the contract as being rescinded and sue for damages, without having to wait for the real damage to be done.

What can a business do when faced with a contract partner showing signs of being unwilling or unable to perform? Here are some important things to do:

- Identify critical supply or services provided by other parties.
- Be aware of potential breaches in those contracts that may not be excused by force majeure (*g.*, indications that a supplier or customer is abnormally delayed in performance or in apprehensive about living up to their contractual obligations)
- Identify ways to mitigate damages promptly once a party repudiates its performance. Mitigating damages is a critical part of obtaining a remedy for

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anticipatory breach.

- Document all instances of communication from another party demonstrating unwillingness to uphold its contract obligations.

As current domestic and international situation continues to become more complex and uncertain, keep in mind the possibility of seeking remedies for anticipatory breach of contract by another party. Businesses should immediately revisit or have their legal team review their largest and most important contracts for critical supplies and services to anticipate how the business can protect itself from another party's failure to perform.

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