

Civil Litigation: Developing a strategy for pandemic-driven commercial litigation



By **THOMAS KNAB**

Businesses must protect their contract rights and position themselves to prosecute and defend commercial and contract claims that arise during, and because of, the business disruptions caused by the response to the COVID-19 pandemic. Businesses must assert those rights, such as the obligations to give,

and respond to, notices of breach, and understand the role that force majeure and related legal defenses will play in the litigation of those claims.

In April 2020, a lawsuit was filed in Delaware state court that provides a good example of how parties will approach contract litigation flowing from the impact of the government's stay-at-home directives. The case, *SP VS Buyer LP v. L Brands, Inc.*, was brought by the buyer of a controlling interest in the Victoria's Secret clothing business. The parties signed the Transaction Agreement on Feb. 20, 2020, after the public became aware of COVID-19, but before governments began to restrict business operations to combat the spread of the virus. On April 22, 2020, the buyer terminated the Transaction Agreement and filed its lawsuit asking the court to declare that the termination was valid under that contract.

The buyer's complaint claimed that because it was offering to pay \$525 million to acquire a controlling stake in a global business, it negotiated for a detailed set of obligations imposed on the seller with respect to the conduct of the Victoria's Secret business between the signing and the closing. Among the several seller's representations, warranties and covenants in the Transaction Agreement cited in that complaint, the seller covenanted that it would

continue to conduct the Victoria's Secret business "in the ordinary course consistent with past practice." However, less than a month after the signing, the seller closed all of the approximately 1,600 Victoria's Secret and PINK stores, and then "voluntarily" (and without the buyer's consent) took actions such as furloughing most of its employees and failing to pay rent for its U.S. retail stores.

The buyer asserted that these actions materially breached the Transaction Agreement and caused several of the seller's representations and warranties "to become false" and incapable of performance at closing. The buyer argued that what remains of the Victoria's Secret business after the seller's actions is not what it agreed to purchase. The buyer further alleged that the Transaction Agreement allocated to the seller essentially all the risk that a materially adverse event (including a pandemic) could prevent it from performing its obligations under that contract.

The seller countersued the next day. Its complaint alleged that the buyer was in breach of the Transaction Agreement and demanded specific performance of that contract and a declaratory judgment that the purported termination was invalid. The seller asserted that the parties were aware of COVID-19 when they negotiated the Transaction Agreement and agreed in writing that the buyer would bear the risk of any adverse impacts "stemming from such a pandemic" including changes to the Victoria's Secret business. The seller said it had satisfied or would be able to satisfy all conditions precedent to closing, and characterized the buyer's claims as pretextual, made in the service of an unlawful demand for a reduction in the purchase price.

It will be fascinating to see how these competing claims are resolved, but equally interesting is how the parties positioned themselves for litigation as they saw how the pandemic was going to affect the deal. On

April 2, 2020, the buyer contacted the seller to advise that it had not consented to the seller's actions (closing its stores, etc.) and was concerned that the seller would not be able to meet the conditions of closing. That same day, the seller responded that while the pandemic had affected the retail industry of which it was a part, it was not in breach of the Transaction Agreement and expected to be able to meet the closing conditions early in its fiscal second quarter and perhaps as soon as May 2, 2020 (but also confessed to looming problems with one of its lenders).

On April 7, 2020, the buyer contacted the seller to advise that it believed that the seller's actions put it in material breach and asked for information on how those actions would affect the Victoria's Secret business, ostensibly to help the buyer determine its next steps. On April 8, 2020, the seller denied that it was in breach and said it would "evaluate and respond" to the request for information. By April 13, 2020 letter, the buyer again alleged material breach, and again pushed the seller to provide the requested information, but this time in connection with "informed negotiation" over a reduction in the purchase price. The seller's April 14, 2020 response rejected the idea of a reduction in the purchase price and justified its closing of the stores and other actions as necessary and consistent with the retail industry's response to COVID-19. Finally, the buyer responded with its April 22, 2020 termination notice.

This exchange shows that once the seller took what it felt were necessary actions, the buyer applied consistent pressure on the seller to state its position on the claim of material breach and provide either assurances that it would be able to perform at closing or an admission that it could not. Perhaps the buyer's intention from the start of the exchange was to try to maneuver the seller into a concession on the purchase price, but at minimum, the

buyer “teed up” the termination option with a paper trail intended to ultimately convince a court that its termination was not only permitted by the contract but entirely reasonable.

Therefore, this case offers valuable lessons

on how a business must address percolating breach of contract disputes — arising from the pandemic or otherwise — if it hopes to favorably resolve those disputes, in litigation or through direct negotiations.

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