

COMMENTARY

Navigating uncertainty: Legal options for manufacturers confronting tariffs

By Daniel J. Ferris and Derek R. Boyd

Pursuant to a series of Proclamations issued by President Trump, tariffs recently went into effect on all steel and aluminum articles imported into the United States from countries other than Argentina, Australia, Brazil, and South Korea. Exemptions granted to Canada, Mexico, and European Union member countries expired on May 31.

Negotiations addressing exemptions are ongoing, and the countries to which they apply may change over time. In addition, individual companies may also apply for exemptions. The authority for the tariffs is contained in the Trade Expansion Act of 1962, which empowers the executive branch to investigate the effect of imports on national security and to impose duties or other import restrictions on trade as a result. 19 U.S.C. § 1862.

The duties imposed by the tariffs are set at 25 percent for steel and 10 percent for aluminum. The affected articles include a wide variety of raw and semi-finished products, all of which are specifically identified in the Harmonized Tariff Schedule published by the U.S. International Trade Commission. They currently include iron and nonalloy steel ingots, semi-finished products, flat-rolled steel, bars, coils, angled sections, and wire, as well as unwrought aluminum and aluminum bars, rods, profiles, wires, plates, sheets, strips, foil (flat rolled products), tubes, pipes, tube and pipe fittings, castings, and forgings.

Anticipation of the tariffs was enough to contribute to increases in steel prices in the months leading up to the official announcement, and the last-minute exemptions issued to a number of impacted countries, as well as the view that the tariffs are being used as leverage in negotiations relating to U.S. trade agreements, have contributed to widespread uncertainty about the precise effect the tariffs will have on prices over time.

At a minimum, however, the tariffs will impact many companies involved in manufacturing, including the automotive industry, and could cause supply-chain disputes between manufacturers and suppliers of steel and aluminum components. Many companies are parties to long-term, fixed-price contracts for the supply of components, and such arrangements are directly impacted by significant fluctuations in raw material prices. Suppliers of steel

and aluminum products may determine that these contracts are no longer profitable as written following an increase in the market price of steel and aluminum and may wish to renegotiate contract prices as a result.



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Legal options

When negotiations fail, supplier cost increases may lead to litigation. The complex nature of the contracts involved in such cases can lead to unpredictable outcomes. When a supplier threatens to stop shipment due to rising costs that make existing contract prices a losing proposition, the first legal option is often a request by the purchaser for a temporary restraining order and/or preliminary injunction from a court. The goal of such an approach is to maintain the status quo while the litigation is pending, which can be critical when a supplier's products are necessary to keep assembly lines running. Such injunctions are often sought and granted emergently and can force the supplier to operate at a loss on a particular contract while the parties and the court resolve the underlying dispute.

Conversely, courts will sometimes order a supplier to keep supplying parts, but only if the buyer pays increased prices until the case is resolved. A court's decision to grant an injunction is discretionary and is only a temporary solution pending a final decision. Still, this initial decision can be of monumental importance and can help to drive a settlement one way or the other.

Unfortunately for hard-hit suppliers, the outcome in such cases is frequently enforcement of the original contract terms. In extreme cases, a party may be able to avoid its obligations under the contract due to the impossibility of performance, but American courts almost never excuse a supplier's performance on this ground simply because a raw material price increase has made the contract unprofitable. After all, while a supplier may lose money as result of the price increase, it is not "impossible" for it to continue to perform.



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for "acts of God" such as natural disasters or other enumerated exceptional circumstances. The application of a particular provision would depend on its specific terms, but courts in the U.S. rarely find that such provisions are a basis on which to excuse performance unless a party is actually unable to perform its contractual obligations due to events outside its control.

As noted above, however, the tariffs do not literally prevent a supplier from performing. Likewise, contract reformation is generally unavailable in the context of a raw material price increase. Typically, reformation is only available where the contract does not reflect the parties' intentions due to mistake or fraud. A change in circumstances, such as a material price increase, could have been anticipated by the parties and would generally be considered insufficient by an American court.

While the tariffs only apply to goods imported to the United States, they affect suppliers based abroad that export steel or aluminum. American companies doing business abroad should be aware that other legal systems, in particular those based on a civil code, may be more receptive to arguments relating to hardship or unforeseen circumstances. As such, where contracts involve parties operating in certain foreign jurisdictions, remedies to compensate parties for increasing material costs are more likely to be available.

A severely-impacted supplier may resort to contemplating bankruptcy to avoid operating at a loss. Indeed, the threat of bankruptcy may offer some leverage to negotiate a price adjustment. Although bankruptcy is a more lenient and widely-used remedy for financially-distressed companies in the United States than it may be in other jurisdictions, it necessarily has far-reaching and unpre-

dictable consequences and is almost always a measure of last resort. An aggrieved supplier may also look to "hardship" or "force majeure" provisions. These provisions are found in many contracts and excuse performance

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Price fluctuation agreements

It may be beneficial for parties to try to avoid disputes stemming from material price increases caused by tariffs and other factors by addressing price increases prospectively. One option is for the parties to utilize a raw material price fluctuation agreement. Such agreements allow the component price paid by a manufacturer to adjust periodically based on changing market prices for raw materials. These agreements typically tie the price for raw material components to a given published index, which will depend on the commodity involved. This built-in adjustment mechanism allows the parties to automatically adjust the final price paid for goods based on changes in raw material costs.

Specifically, the commodity indices that provide pricing information for the articles affected by the recent steel and aluminum tariffs typically provide a snapshot of the real-time prices paid by a selection of purchasers. Whether or not a particular index will accurately reflect the material price increase experienced by a particular supplier may depend on the composition of the pricing samples in the index and the extent to which they reflect national versus international prices. While they may not perfectly account for price increases experienced by specific suppliers, including those resulting from tariffs, price fluctuation agreements are a powerful tool that can help parties reduce the risk of a sudden supply chain disruption and litigation.

In addition to helping avoid disputes stemming from tariffs, price fluctuation agreements also serve to avoid disputes following price changes caused by other destabilizing events. Parties may include language addressing price fluctuation in a manufacturing contract or they may subsequently enter into a price fluctuation agreement.

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