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Polymer Advisory

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In This Issue...

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Hurricane Katrina: A Greater Force

Hurricane Katrina is recognized as the most severe natural disaster in the United States since 1900. It will be remembered for its devastation of the Gulf Coast regions, and especially for the massive flooding of the historic city of New Orleans.

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Resin makers throughout the U.S. Gulf Coast are dealing with the aftermath of Hurricane Katrina, resulting in increased resin prices and decreased availability. Within the first week of September, many major producers of certain plastics resins have declared force majeure, which literally means "greater force," announcing that their supply of products has been hindered or halted by the aftermath of Hurricane Katrina in the Gulf.

It is expected that many businesses along the Gulf Coast will invoke force majeure clauses to excuse required contract performance. However, whether a force majeure clause can excuse the invoking party from its performance of a contract depends on: (i) who invokes the force majeure clause, (ii) how carefully it is drafted and (iii) what effect Hurricane Katrina had on the performance that is sought to be excused.

The analysis of a force majeure clause always requires an examination of four elements: (i) the force majeure event, (ii) causation, (iii) the effect of a force majeure event on the performance that is sought to be excused, and (iv) the procedural requirements that must be followed by the invoking party.

A. Force Majeure Events

Typically, force majeure clauses cover natural disasters or other "Acts of God" such as earthquakes, and some man-made events, such as strikes, lockouts, riots, and governmental acts. An event does not need to be catastrophic in order to fall within the scope of a force majeure clause. Therefore, without a natural disaster, the failure of third parties, such as suppliers and subcontractors to perform their obligations, can be a force majeure event. Courts generally uphold the contracting parties' definition of force majeure. In *Kentucky Utilities Company v. South East Coal Company et al.*, the court stated that the parties were free to set forth the terms of their agreement. If the parties agreed that electric power failures constituted a force majeure event, the court would not construe such language to require an "overpowering force" in the nature of an Act of God.

B. Causation

Causation deals with the causality that connects the impact of an event to the nonperformance of the contract. Force majeure clauses are intended to excuse a party only if the force majeure event is reasonably beyond the invoking party's control and the failure to perform could not be avoided by the exercise of due care by that party. As a result, courts will not permit a supplier to invoke a force majeure clause where the delay or inability to perform was caused by the supplier. Similarly, a force majeure defense may not be available where the delay or inability to perform could have been prevented through the exercise of diligence. In *Steel Industries, Inc. v. Interlink Metals & Chemicals, Inc.*, one of a steel vendor's sources was affected by a force majeure event, however, the contract did not require the steel vendor to obtain the steel from this particular source. As a result, the

Continued on page 2

Continued from page 1

court held that a force majeure clause did not excuse the steel vendor and the steel vendor was required to fulfill its obligation to procure the steel from other sources.

C. The Effect of a Force Majeure Event

The effect of a force majeure event deals with whether the invoking party can be excused from the performance. Some contracts provide that an event of force majeure will terminate the contract, while others may provide that a force majeure event will only postpone the performance. If a contract provides that force majeure does not terminate the contract entirely, then the party invoking the force majeure clause cannot be completely excused from performance. In *Distribution Services Limited v. Hong Kong Islands Line America S.A.*, the force majeure clause only suspended the contracting party's obligation to ship the contracted goods during the period of force majeure. After the period of force majeure was over, the contracting party was required to resume performance of its obligations under the contract.

If a force majeure is declared, a supplier should be alert to any statute or regulation that requires it to allocate its diminished products among its customers. For example, in the event of force majeure, a supplier of residual fuel oil must comply with the Emergency Petroleum Allocation Act to allocate its scarce products among its users. Absent any statutory and regulatory requirements, a supplier should review its contract to see whether it carries any contractual obligation to allocate on a pro rata basis to all of its customers. Moreover, even without a specific allocation clause, if the related manufacturing or supply agreement contains a clause which provides that a buyer cannot be treated by a supplier in less favorable terms than those extended to supplier's other customers, then the supplier may still have a contractual obligation to allocate its available products among its customers. As a practical matter, this may simply be good business practice to maintain supplier-customer relationships.

D. The Procedural Requirements

Generally, a force majeure clause contains a notification clause. Such clause requires a party that wishes to be excused from performance under the force majeure clause to give prompt notice of its intention to the other party. Failure to comply with the procedural requirements of a notification clause may invalidate a force majeure claim.

Before invoking a force majeure clause, businesses impacted by Hurricane Katrina should carefully review the terms and conditions of its contracts to determine what relief is available under the force majeure clause, whether it should allocate products or production capacity among its customers, and how to carefully follow the procedural requirements in order to obtain the appropriate relief.

For more information, contact Yanping Wang at 216.363.4664 or ywang@bfca.com, or Megan Mehalko at 216.363.4487 or mmehalko@bfca.com.

Control Your Own Destiny: Protect Trade Secrets and Customer Relationships

Trade secrets and customer relationships are some of, if not the most, critical assets a business possesses. But are these assets adequately protected from theft? The law in virtually every state establishes the framework for protecting these assets, but it is up to each business entity to take the steps necessary to obtain the benefit of these laws. The failure to take these steps can render the existing legal safeguards absolutely meaningless. Unfortunately, businesses often wait too long before seriously addressing this vital issue.

Technological advances have enabled businesses to capture, categorize and utilize a wealth of business information, far beyond what anyone could have anticipated a few short years ago. The negative side to these advances is that employees now have ready access to information that could cause the business great competitive harm were it to fall in the hands of a competitor. For example, information systems now neatly display not only a particular customer's identity, but also detailed information regarding that customer such as the purchasing authority, what it buys, when it buys, how much it buys, packaging and shipping requirements, pricing, profit margins, special needs and preferences, and more. In the case of polymer manufactures and others having sophisticated production procedures, these information systems in all likelihood also contain technical information such as recipes, formulae, production procedures, operations parameters and sequences, and other detailed information regarding how compounds are produced. All of this information is in a form which most likely can be printed, emailed, or otherwise transferred with the touch of a button.

The Uniform Trade Secret Act ("UTSA"), adopted in Ohio and 44 other states, protects this and other information from use or disclosure outside the business, provided the business has taken reasonable steps to maintain the secrecy of that information. At its core the UTSA protects any information that derives economic value by virtue of the fact that it is not generally known and is subject to reasonable efforts to maintain its secrecy. In addition, the Computer Fraud and Abuse Act, the Economic Espionage Act, and various state unfair competition laws provide related protections.

The Uniform Trade Secrets Act ("UTSA") defines a "trade secret" to include any information which:

a) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use; and

b) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

The type of information which can qualify as a trade secret is essentially limitless. If the information is not generally known outside your business and there is value to the information because it is not generally known, the information can be recognized as a trade secret. The courts have expressly recognized many types of information as trade secrets, such as business plans, customer lists, customer purchasing data, pricing information, supplier information, product design and development information, formulae, recipes, manufacturing process

Continued on page 3

Continued from page 2

details, and marketing strategies, to highlight just a few. Even commercially available data and information may qualify as a trade secret if manipulated or catalogued in a way which makes it unique or otherwise not readily ascertainable.

The key to availing one's self of these protections is the effort a business takes to maintain the confidential status of sensitive business information. These efforts can and should include limiting access to those having a need to know, password protecting information systems, labeling documents confidential, controlling access to areas housing confidential information, implementing policies and work rules prohibiting disclosure, utilizing confidentiality agreements and noncompete agreements with employees, and utilizing confidentiality agreements with customers and suppliers that have access to sensitive information, to name only several.

A comprehensive protection plan must start with the identification of the competitively sensitive business information existing within the business. Once defined, it should then be determined who currently has access to this information and, then, who needs to have access to such information. Only then can the business make an informed and practical decision as to how and what methods of protecting the information should be implemented. The methods of protection should be designed (1) to ensure, to the extent practical, that the access to the information will in fact be limited to those having a need to know, and (2) to apprise anyone working with such information that it is confidential and must be treated as such.

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The use of Noncompete Agreements can be vital to not only protecting trade secrets, but also customer relationships. As a general rule, an ex-employee is free to exploit the customer relationships developed in the course of his/her employment with the former employer. Thus, any ex-employee not bound by a noncompete agreement is free to solicit his or her former employer's customers. This is of particular concern and importance in the area of sales. Many, if not most, state laws recognize the protection of these customer relationships as a legitimate and proper interest justifying the enforcement of noncompete agreements. Thus, any business which puts its sales (or other) employees in a position to develop close relationships with customers should seriously consider the use of noncompete agreements, in addition to protecting the confidentiality of trade secret information.

In this era of unprecedented mobility, it is a matter of when, not if, a key employee with extensive exposure to, and knowledge of, trade secrets will join a competitor. If that employer has taken the steps necessary to protect its confidential, trade secret information, it will be in position to take action to restrain any threatened use or disclosure of that information. Conversely, an employer which has failed to take such steps risks being rendered powerless to prevent a competitor's exploitation of those most valuable secrets. This is truly an area where a business can, to a large extent, control its own destiny.

For additional information on this topic, contact Mike Buck at 216.363.4694 or mbuck@bfca.com.

Mother Nature Strikes Again

Note: A far more extensive analysis of this issue is found in Mr. Blubaugh's recently-published article, *The Perfect Storm: The Parameters of a Successful "Act of God" Defense in Freight Claims*. Please contact him for a copy.

Like every other business in the region, those involved in the polymer industry in Louisiana, Mississippi, and Alabama are dealing with the aftermath of Hurricane Katrina. At worst, entire facilities may be deemed "totaled." At best, many months will pass before power, water, natural gas, and communications are fully restored and facilities are otherwise operational. One challenge that many companies will face is responding to or prosecuting claims for damage to, loss of, or delay to freight in transit.

Federal and state law provide that a shipper cannot prevail in a freight claim against a carrier if an "Act of God" caused the freight damage, loss, or delay in question. An "Act of God" is generally defined as a sudden, unexpected, and unavoidable manifestation of the forces of nature. Whether a particular natural event constitutes an "Act of God" turns on several factors. These factors generally include:

1) the severity of the natural occurrence causing the damage,

2) the reasonable predictability of this natural occurrence,

3) the lack of human agency in the damage to the freight, and

4) the reasonableness of any precautions taken by the defendant.

The quintessential example of a successful "Act of God" defense arises in the context of hurricanes. For instance, in the case of *In the Matter of the Complaint and Petition of International Marine Development Corp.*, 328 F.Supp. 1316 (S.D. Miss. 1971), a variety of plaintiffs made claims for property damage and catastrophic personal injuries caused by Hurricane Camille. The court described the singular nature of the storm:

"Hurricane Camille, which was the greatest natural disaster in the history of the North American continent and caused more devastation and destruction to the Mississippi Gulf Coast… than any hurricane of record, with unprecedented wind velocity in excess of 200 miles per hour, a tide rise of 30' or more, and a tidal surge of at least 22', is the most classic case and striking example of what is characterized as an Act of God. This freak of nature was of sufficient velocity and destructiveness to overcome all reasonable preparations..."

Id. at 1330. As a result, the court found that none of the claimants could establish liability against the various defendants.

However, a storm does not have to rise to the level of a hurricane or be of continental significance in order for it to constitute an "Act of God." Rather,

Continued on page 4

Continued from page 3

the specific features of any storm can be sufficient to make it an "Act of God." In *American International Insurance Co. v. Vessel SS Fortaleza*, 446 F.Supp. 221 (D. P.R. 1978), the district court analyzed whether a storm that struck a vessel en route to Puerto Rico constituted an "Act of God." The court cautioned against a mechanical approach in which one simply measures the force of the winds or the height of the waves to see if a storm amounts to an "Act of God." The court identified a number of additional factors that must be reviewed in assessing a storm: (1) the duration of the storm, (2) the size of the vessel, (3) the wave intervals, (4) crossing seas, (5) structural damage, and (6) "other" unidentified considerations. *Id.* at 226. The court found that the storm in question, which involved winds of "full storm force" and "unusually short" wave intervals, constituted an "Act of God."

The case of *Noritake Co., Inc. v. M/V Hellenic Champion*, 627 F.2d 724 (5th Cir. 1980), involved an even more modest weather system:

"On June 15, 1976, the Port of Houston area experienced severe, flash flooding from heavy rains. Though the weather bureau had predicted only a 15% chance of rain that day, the port area received some 13" of rain within a few hours, while a local airport received less than 2"."

Id. at 726. The shipper in *Noritake* sued for damage to 152 cardboard cartons of dinner sets that were damaged in a flooded warehouse. The trial court found that the unexpected storm system constituted an "Act of God" and the Fifth Circuit affirmed.

Of course, one must keep in mind that all heavy weather conditions do not constitute "Acts of God." See *Security Insurance Company of Hartford v. Old Dominion Freight Line, Inc.*, 2003 WL 22004895 (S.D. N.Y. 2003) (freight is not lost due to an "Act of God" merely because it was stolen during a storm). Indeed, carriers are sometimes charged with knowledge (both actual and constructive) of storms and weather patterns that might once have been unpredictable. For instance, in *National Starch & Chemical Company v. M/V "Monchegorsk"*, 2000 WL 1132043 (S.D. N.Y. 2000), a shipper shipped a large quantity of starch products from Thailand to Maine. While the products were being loaded into a Cyprian cargo vessel's various holds simultaneously, rain began to fall. Many of the bags became wet and, in fact, water was found pooling on top of many of them. The court rejected the defense that the rain was an "Act of God" because the carrier was or should have been aware of the weather risks native to the region. See also *Louis Dreyfus Corp. v. M/V "MSC Floriana"*, 1998 WL 474092 (S.D. N.Y. 1998) (carrier did not establish that storm was "Act of God" because no persuasive evidence was introduced that 20 mile per hour wind is particularly unusual or unexpected in area).

As the foregoing cases indicate, the successful application of the defense turns on the severity of the event, the reasonable predictability of the event, the lack of human agency in the event, and the reasonableness of the carrier's precautions. One must perform the necessary historical research in order to have a context by which to judge the significance of the particular event. As this year's weather has shown, the future can hold any number of meteorological surprises.

For additional information on this topic, please contact Marc Blubaugh at 614.223.9382 or mblubaugh@bfca.com.

Upcoming Events

October 6, 2005
Maximizing Shareholder Value
This conference, geared to senior executives and investment advisors in the plastics industry, is being held at the Hyatt Regency Chicago. Benesch is sponsoring this day-long event with Plante & Moran and the Society of the Plastics Industry. The morning discussion will provide an overview on how plastics companies can maximize shareholder value through operational techniques, unique infrastructure, and transactional positioning. Benesch's Richard Lillie will deliver the keynote address on "When a Good Offense is the Best Defense - Dealing with Regulatory Agencies." The afternoon will focus on how to enhance the value of your company's infrastructure by improving human resources and compensation strategies, intellectual property practices, and other assets. Finally, the day will address transactional issues including valuation, succession strategies, and exit strategies.
For more information, contact the Society of the Plastics Industry at 773-380-0808 or email Patti Gillespie at pgillesp@socplas.org.

October 7, 2005
Mid-America Plastics Partners, Inc.
As the plastics industry continues to segment itself into the "haves and have-nots," partnering continues to become increasingly prevalent. Driven by the need to differentiate, grow, globalize, innovate, and reduce costs, successful companies will look to alliances to remain competitive. Rob Marchant will speak on "Creating Competitive Advantages - Differentiate through Strategic Alliances" at this half day session being held at the Holiday Inn Montrose.
For more information, contact Megan Thomas at mthomas@bfca.com or 216.363.4174.

October 18-20, 2005
Plastics Encounter Southeast
Don't miss the only show in the Southeast this fall where you can:
- See the latest technology in action
- Make valuable contacts with processing, design and management professionals
- Attend conferences sponsored by The Society of the Plastics Industry (SPI) and the Industrial Designers Society of America (IDSA), and seminars by Compuplast and Paulson Training
- View two unique product galleries in the same location -- the SPI Structural Plastics Division's Design Gallery and the IDSA Idea Gallery
- Unwind and talk casually at complimentary networking receptions

Megan Mehalko, co-chair of Benesch's Polymer Group, with Matt Jamison of PMCF, will be presenting on succession planning and exit strategies. See www.plasticsencounter.com for more information.

December 1, 2005
Transportation Conference
This one-day conference addresses a range of challenges faced when transporting goods. Insurance issues, supply chain strategies, hazmat issues, and more will be covered. The conference will be held at the City Club of Cleveland and followed by a networking reception.
For more information, contact Megan Thomas at mthomas@bfca.com or 216.363.4174.

March 5-8, 2006
Plastics News Executive Forum
Save the date for this popular and informative annual conference. Information will be posted on www.plasticsnews.com as the forum approaches.

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