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U.S. tariffs: Anticipating their impact on Quebec businesses' contracts, margins and cash flow

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The tariffs imposed by the United States on certain Canadian products disrupt more than just trade. They also have tangible consequences for several Quebec businesses, affecting margins, competitiveness, continuity of operations, financing and sometimes solvency.

The impact of U.S. tariffs varies from company to company. Some businesses are able to absorb them to some extent, particularly if the exchange rate is in their favour or if competition allows them some leeway to pass on a portion of the cost to their U.S.-based customers.

Meanwhile, other companies are seeing their U.S. market access suddenly compromised, forcing them to reconsider their business model.

Ultimately, there is no one-size-fits-all solution here. In order to carry out a thorough analysis of the situation, businesses must consider their position from contractual, commercial, financial and strategic standpoints simultaneously.

Contracts, prices and U.S. market dependence

Since the first tariffs were implemented, certain strategies have proven useful in curbing exposure.

From a contractual standpoint, key actions include:

- Analyzing supply, distribution and sales contracts to determine who actually bears the tariff risk
- Reviewing Incoterms, pricing clauses, adjustment mechanisms, termination rights and *force majeure* clauses
- Realistically assessing the ability to pass a cost increase on to customers
- Assessing the extent to which the business depends on the U.S. market for both its sales and its inputs

There is, however, one legal caveat: the imposition of tariffs does not, in and of itself, grant the right to invoke *force majeure* or to terminate a contract simply because it has become less profitable.

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It all depends on the precise wording of the clause, the factual context and how predictable the risk of tariff imposition was at the time the contract was concluded.

Margins, prices and supply chains

In many sectors, businesses first feel the effect of tariffs through price fluctuations. Some companies have enough leeway to pass on the tariff burden to their U.S.-based customers by raising their prices accordingly.

In other sectors, particularly where margins are already slim or where a Canadian manufacturer's product is becoming less competitive, the impact is more severe: loss of market share, declining sales volumes and almost immediate liquidity problems.

It is often at this stage that executives must consider more substantive solutions, such as diversifying sales into alternative markets, reconfiguring supply chains, partially relocating manufacturing operations or establishing production capacity within the United States.

Businesses may also need to consider renegotiating certain financing sources or commercial terms.

While these options may be worth considering, they require time, liquidity and an execution capability, which not all companies possess.

Cash flow, financing and warning signs of financial strain

When a company is heavily dependent on its U.S. sales, tariffs can exacerbate existing issues.

Bankers look out for certain warning signs such as:

An excessive concentration of revenue originating from the United States
A persistent decline in volume or margins
Extended payment terms
Pressure on working capital
Contracts that have become inherently unprofitable
A weakened refinancing capacity

The lack of a short-term commercial alternative should also be taken seriously.

In this type of scenario, delaying action could mean missing out on solutions that were still available just a few weeks or months prior.

Restructuring and insolvency

When commercial and operational adjustments are no longer enough, the restructuring mechanisms provided for under bankruptcy and insolvency laws can offer temporary relief and facilitate restructuring.

Depending on the circumstances, this approach can be used to stabilize the situation in the short term, negotiate with creditors, revise certain commitments that have become unsustainable, preserve part of the company's value or prepare for a turnaround based on a business model that is less dependent on the U.S. market.

However, resorting to such restructuring options is not just a formality.They entail costs, constraints and risks that can sometimes pose a serious threat to a business's very survival. Before considering them, it's important to clarify core objectives, identify must-protect assets and lock down critical contracts. Mapping out how the restructuring will ripple through to shareholders, lenders, suppliers and customers is equally vital.

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While these mechanisms are often a last resort, considering them only after all other doors have closed severely limits businesses' room to maneuver.

Competition law and collaborations

Faced with tariff pressure, some companies may be tempted to partner with other players in their market to pool resources or reorganize their supply chains. The idea may be economically sound, but it must be handled with caution from a legal standpoint.

Competition law risks may arise as soon as competitors exchange sensitive information or adjust their business conduct jointly.

For this reason, any such collaboration should be carefully structured, and it is highly recommended that the parties consult a legal expert who is familiar with the applicable competition law provisions before venturing into this territory.

Mergers & Acquisitions and company valuations

Tariffs also affect company valuations and transaction dynamics.

For sellers whose products are subject to the new tariffs, the higher the tariff exposure, the more likely it is that their company's valuation will be affected or that they will defer a divestiture or acquisition in anticipation of more favourable conditions.

For buyers, the tariff issue has become a key consideration in the due diligence process. They must determine:

- What proportion of the target company's revenue comes from its U.S. sales
- Whether the target company is actually able to absorb or pass on the additional costs resulting from the tariffs that it now has to pay
- Viable workarounds
- The time and capital needed to implement them

In practice, the higher the tariff exposure and the cloudier the mitigation strategy, the more likely it is that the buyer will ask for a price reduction or demand contractual protections.

Acting before problems take root

U.S. tariffs do not pose the same risks for every company, but they present many with the same challenge: the need to act early.

For some businesses, the answer mainly lies in the contracts they have concluded. For others, it will be a matter of taking commercial, operational or transactional measures.

For the most vulnerable companies, the priority will be to preserve value and swiftly consider the available restructuring options.

Rather than simply assessing the immediate tariff impact, the key is determining whether businesses have enough time, flexibility and liquidity to adapt before problems take root.

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