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COVID-19: Force Majeure

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What's the Problem?

With everything from travel bans and event cancellations, to disrupted supply chains – our lawyers are routinely being asked to weigh in on the legal consequences of non-performance under otherwise enforceable contracts. Whether parties are excused from performing contract obligations that have been impacted by Coronavirus will typically be a question of “force majeure.”

Force majeure clauses typically provide that where no party is at fault – i.e. where the event or condition is beyond a party's control (typically events like an act of war, natural disaster, or an “act of God” are enumerated) and interrupts that party's performance – the failure to perform under the contract is excused without liability to either party.

What to Consider?

The critical facts to consider are:

1. Review your critical contracts. Do they contain force majeure provisions? If so, review the contents carefully for breadth and scope. Beware of notice requirements and other predicates, for example, if a declared state of emergency is required. Also check for governing law – is it US law or a substantively equivalent common law system – or a civil code country?
2. Formulate a prevention, mitigation, and response plan. Consider having a designated “force majeure” czar to keep your messaging consistent. If invoking force majeure, make sure your other statements and representations to your counterparties are not seen as admissions or a waiver of rights.
3. Don't assume that force majeure applies – take care that you are not repudiating a contract that does not have force majeure provisions or where performance is not causally connected to Coronavirus. Remember force majeure is not a cure-all (no pun intended). Parties are still required to use best efforts and mitigate losses.

Does Coronavirus automatically trigger force majeure? This is a question specific to the contract itself – for example, does the contract's clause expressly refer to a pandemic, epidemic, disease, or public health emergency? If so, Coronavirus could very well qualify. Does the clause refer to “acts of Government,” “government regulations,” or other actions that make it “illegal” or “impossible” to act pursuant to the contract? Then perhaps a travel ban that frustrates performance qualifies.

That said, force majeure clauses vary greatly, and many force majeure

provisions are, unfortunately, not very specific about particular events and only contain generalized categories.

Typically, courts have read force majeure provisions narrowly. For example, courts have rejected as a force majeure event a foreign government flooding the US market with cheap imports, sudden changes in market conditions, union strikes and unseasonable weather. That said, the Coronavirus, and the efforts taken by governments to contain its spread (travel bans, forced quarantines, etc.), are novel and unprecedented enough that in some cases Coronavirus may be interpreted as a force majeure event.

Bear in mind that contract clauses are not read in isolation to the other provisions of the contract, and this applies also to a force majeure provision. Other clauses may also address the party's obligations in the event of unexpected circumstances – i.e. a "take or pay" supply contract – which is itself devised to allocate risk for unforeseen events. Such a contract may be interpreted differently than, for example, a mere output contract.

Also bear in mind, this analysis applies to common law countries. In civil law countries (where force majeure in fact originates), the respective civil codes set out the requirements of invoking force majeure. Hence when reviewing your contract, pay specific attention to any governing law provision. Reportedly, the China Council for the Promotion of International Trade (CCPIT) has issued thousands of "force majeure certificates" to Chinese companies that have claimed that their ability to perform contracts has been prevented by the Coronavirus, which may prove determinative in litigation under Chinese law.

If a contract does not have a specific force majeure clause, is one implied? The answer is likely no. In common law countries, force majeure is a creature of contract and failure to include such a provision will likely be implied as an intentional exclusion of the provision.

There are background concepts in the law, such as the "impossibility" or "frustration" doctrines, but these are narrowly construed and difficult to invoke – i.e. the event typically must (1) be not reasonably foreseeable and (2) radically change the contract terms from what the parties agreed to. Merely escaping a bargain that has turned bad because it is harder to perform is not enough.

As for implied terms, in civil law countries, the opposite is often true. For example, in China, under Article 180 of the General Rules on the Civil Law and Articles 117 and 118 of Chinese Contract Law, force majeure applies automatically to commercial contracts governed by Chinese laws.

What sort of contract obligations are covered by force majeure? The two key concepts to keep in mind are causation and mitigation. First, did the Coronavirus epidemic in fact cause a delay or non-performance? The fact that a supplier is located in China, for example, should not be enough. Rather, it would need to be shown that the supplier had shut down, which caused a delay in manufacturing of [x] days, which led to a delay in

delivery of [x] days, which will result in delayed performance of [x] days. Second, were there commercially reasonable steps that the party could have taken to avoid or overcome the event, such as by seeking parts and materials from unaffected areas or unaffected manufacturers? More expensive or more difficult is not enough – and a failure to perform only tenuously connected to Coronavirus will also not be enough.

Do not overlook the other conditions that are part of the application of the force majeure in the contract: contracts will often specify that, if an event of force majeure has occurred, it will only apply to excuse a party's performance if the affected party provides adequate notice to the other party (which often has a time limit and requires specificity as to the impact and duration of the event). Even without an express requirement, delay in providing notice could give rise to equitable principles such as waiver or laches. In addition, there is often limiting language (performance will be excused "on a day-for-day basis," or "only to the extent reasonably necessary") around the excused performance itself.

Suspend or terminate the contract? In some cases, the relevant contract will specify what the remedy is – suspension or termination. Some contracts may have a continuation provision, stating that a force majeure event that continues for a certain period of time gives rise to a right of termination. In other cases, force majeure may give rise only to a suspension of the required performance. Carefully review the relevant language – particularly for unintended consequences – if your intent is not to terminate the entire contract.

Will insurance cover force majeure? The losses arising out of a party's inability to fulfill its contractual obligations because of Coronavirus could give rise to an insurance claim (for example Business Interruption Coverage) – depending on your policy's specific terms and conditions. Refer to our insurance related content for more specific questions concerning coverage.

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