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Alerts

COVID-19, Force Majeure and Other Defenses to Contractual Performance

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Along with its significant and tragic human impact, the COVID-19 pandemic has disrupted and will continue to disrupt global, national and local commerce. Businesses in every industry have experienced, and will continue to experience, significant challenges to their ability to meet or enforce contractual obligations. These events shine a bright light on force majeure clauses – some boilerplate, others carefully negotiated – and other defenses to contractual performance.

Although the global response to COVID-19 is unprecedented, epidemic-related force majeure disputes are not. In the late 1800s, a French court considered an actor's claim that a typhoid epidemic in a city excused him from performing there even though the theatre remained open. Another court evaluated whether a cholera outbreak excused nonperformance of a food sale contract. Still another assessed whether an influenza epidemic excused a contractual commitment to deliver fabric.

In more recent times, a Chinese court affirmed that, for a month in 2003, SARS constituted a force majeure and contracting parties were not liable for losses during that period. And during the 2014 Ebola crisis, a manufacturer announced it was suspending an iron ore expansion project in Liberia due to the deadly Ebola epidemic in West Africa – a force majeure that freed both parties from liability or obligation because the crisis was beyond the control of the parties and prevented performance.

Below we provide general guidance on force majeure and other related defenses. But evaluating whether the COVID-19 pandemic triggers a given force majeure clause or related defense will be a fact-bound determination focused on the specific contractual language and the relationship and interplay between the outbreak and a party's performance or failure to perform. And the law governing the contract may result in determinations that performance excused in one jurisdiction is not excused in another.

What is a force majeure clause?

Force majeure literally means a "superior" or "irresistible" force or power. Contracting parties often include force majeure clauses in their agreements to protect themselves from unforeseeable or uncontrollable events that prevent or delay performance. These clauses, depending on their wording and applicable law, may excuse performance when an act of God or other unforeseeable event *identified or included in the clause* makes it illegal, impracticable, impossible, or sometimes even inadvisable, to fulfill the terms of the contract.

Do force majeure clauses cover pandemics such as COVID-19?

While contracts rarely identify specific viruses, they typically reference "acts of God" and may expressly reference epidemics, pandemics, disease, illness or quarantine. Even where such events are not expressly included in a force majeure provision, a pandemic such as COVID-19 could trigger other events that are identified, including, for example, an act or order of a governmental authority that renders performance illegal or impossible.

Choice of law will matter in determining how broadly a force majeure provision will be read. A party analyzing a force majeure provision should assess whether governing law frowns on boilerplate force majeure provisions and reads them narrowly. A court might also assess whether the contract's identification of force majeure events could be read as an

exclusive list of events reflecting an intent to exclude others. And some courts may be stingier in applying catch-all references to *unforeseen events* or *disasters*.

Also, keep in mind that a party's choice to include or exclude events is likely to be assessed as of the time of contracting – the absence of a reference to pandemic in a contract entered today may well be assessed differently than for a contract entered a year ago.

Finally, parties should be careful about arguing that pandemics could not have been anticipated before the recent COVID-19 outbreak (although there may be strong arguments that the global, national and local response to the COVID-19 pandemic was not foreseeable). As noted above, typhoid, cholera, influenza, SARS and Ebola have been the subjects of disputes about contractual performance. And there are numerous examples of parties anticipating epidemics, pandemics and diseases in contracts. This does not mean that a jurisdiction will not accept more general contract language to excuse performance, but it does mean that a provision that includes specific references to "epidemic" or "pandemic" will be easier to enforce than one that does not.

Might other defenses to contract performance apply where a contract does not include a force majeure provision or where that provision is narrowly drawn?

Common law defenses to contractual nonperformance, including impossibility of performance and frustration of purpose, may also be available to a party. The availability and applicability of these defenses varies by jurisdiction.

Generally speaking, the *doctrine of impossibility* applies (as the name suggests) when performance of one side of the contract has become impossible. The defense of *frustration of purpose*, on the other hand, applies when achievement of the purpose or object of the contract is frustrated, for example where a change in circumstances renders one party's performance useless to the other. Although frustration of purpose and impossibility both implicate the parties' ability to fulfil their obligations under a contract, frustration of purpose also requires a court to investigate why the parties entered the contract in the first place. Because determining the parties' subjective intent implicates thornier issues, courts have generally been more inclined to consider impossibility defenses.

Because force majeure clauses often require a showing of impossibility or frustration, courts recognize that there can be substantial overlap in applying force majeure provisions and related common law defenses. But even if a contract has a limited, narrow force majeure provision, traditional contract defenses of impossibility and frustration of performance are still in play. The exception is where the parties' express allocation of the risks of unforeseen events is read to foreclose such common law defenses.

What sources of law should I consider in evaluating claims that contractual performance may be excused?

There are a number of sources of law that a contracting party should consider in assessing the enforceability of a force majeure provision and statutory or common law defenses to non-performance. These include:

- *State common law* and *civil codes* (for example in Louisiana) that codify such defenses.
- *Industry-specific statutes* that define force majeure events and remedies when those events occur. These include Virginia's Emergency Petroleum Products Supply Act; Pennsylvania's law governing the public utility commission's role in overseeing electric distribution and generation companies/suppliers; Colorado's law governing design-build transportation contracts; and Texas' law permitting electric utilities to recover losses caused by certain unforeseen events.
- *The Uniform Commercial Code*, which includes a number of gap-filling provisions that may apply in the event of impracticability of performance (or to certain aspects of performance).
- *Foreign law, public international law and treaties*, including country-specific codes like those in France, China and Canada that recognize or limit force majeure, impossibility and frustration defenses, or, where applicable,

conventions like the United Nations Convention on Contracts for the International Sale of Goods, which covers failures to perform based on impediments beyond a party's control.

What facts matter in evaluating force majeure claims and other defenses to contract performance?

Given that these contractual and common law defenses focus on the impact of a triggering event on performance, parties must be methodical in documenting the link (or lack thereof) between a force majeure event and performance. What impact, if any, did the declaration of a pandemic or a state of emergency have on performance? To what extent should parties have anticipated such challenges? Is the pandemic being used as an excuse for an existing inability to perform that would have resulted in a breach wholly apart from the pandemic? Did the party seeking to excuse performance take reasonable steps to limit the impact of the force majeure event? These and other facts could make or break a defense.

Is notice of a force majeure event required?

A force majeure provision may include a notice requirement – for example, that a party provide notice of its intent not to perform within a certain number of days after a force majeure event. In addition to such specific notice provisions, there may be general contractual notice provisions in the contract that cover force majeure events.

Even if a contract is silent on the question of notice, a court is likely to evaluate whether reasonable notice was given. Because the impact of a force majeure or impossibility declaration is significant, a court may focus on whether a party supplied sufficient information to permit the other party to evaluate the defense and mitigate the impact of nonperformance.

Finally, a party should keep in mind that a wrongfully declared force majeure may be read as a repudiation of the contract, subjecting the nonperforming party to damages for breach.

Does force majeure or impossibility excuse performance?

The language of an agreement may specify whether a force majeure excuses performance, merely delays performance or requires some other remedy, like renegotiation of the contract's terms.

What other factors should a party keep in mind in force majeure-related advocacy?

Past precedent is meaningful, but advocates should keep in mind that the global response to COVID-19 will have touched everyone, including the judges and juries that will resolve disputes over force majeure, impossibility and impracticability claims. Courts will remember that they closed their doors, in whole or in part, to the public. Jurors will remember that they were told or even ordered not to interact with others. Everyone will recall their inability to obtain things that they wanted. Good advocates will take these things into account in crafting their arguments and in deciding when and where they should be made.

Also, given the global impact of this pandemic, courts and other fact finders are likely to have little patience for parties that do not work to resolve their disputes. In other words, good counsel may be measured not by the disputes that are won and lost but by creative legal solutions that do not involve the courts.

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As your business confronts the challenges of COVID-19, BakerHostetler is here to help. We are continuing to develop and publish information about this fast-changing environment and have developed an online resource to help address and answer legal questions, available here.

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