Force Majeure in Light of the Coronavirus Outbreak

By:Michael J. Cavaretta
March 16, 2020

See more related articles and posts in our: COVID-19 Resource Collection.

On January 30, 2020 the World Health Organization declared that the novel coronavirus COVID-19 outbreak constituted a public health emergency of international concern. Infectious disease experts and public officials are urging several practical measures, such as hand washing, "social distancing" and self-quarantining when showing symptoms, to prevent a potentially catastrophic spike in infections that could overwhelm medical facilities.

While taking these steps is imperative to protect public health, they have led to severe disruptions in business, including supply chain interruptions, cancellation of large and small gatherings and face-to-face meetings, and restrictions on travel. Many of these disruptions are having a significant impact on the ability of suppliers and service providers to perform their contractual obligations to their customers and clients.

If you are one these impacted suppliers or service providers, what is your exposure? If you are the customer or service recipient, what are your options?

Many of the answers to these questions will lie in the *"force majeure"* clauses of the contracts governing the commercial arrangement.

A *force majeure* clause is a contractual provision that excuses a party's obligation to perform under an agreement if the circumstances giving rise to the failure are beyond the party's control. Here is an example of the operative portion of a *force majeure* clause:

> *No party shall be liable or responsible to the other party, nor be deemed to have defaulted under or breached this Agreement, for any failure or delay in fulfilling or performing any term of this Agreement when and to the extent such failure or delay is caused by or results from a Force Majeure Event.*

While usually found in the "back of the agreement" and often perceived by laypeople as being merely "boilerplate", not all *force majeure* clauses are the same. Subtle differences could have significant repercussions.

In particular, the definition of what constitutes a *force majeure* event, and therefore what circumstances excuse a party from performing, can vary significantly. Consider the following definition (Definition One):

> *"Force Majeure Event" means (a) flood, fire, earthquake, or explosion; (b) war, invasion, hostilities (whether war is declared or not), terrorist threats or acts, riot, or other civil unrest; (c) government order or law; (d) actions, embargoes, or blockades in effect on or after the date of this Agreement; and (e) action by any governmental authority.*

Under this definition, only an occurrence that is specifically enumerated would constitute a force majeure event. Other circumstances – even if they were beyond a party's control – would not fall within the definition. So, for example, a failure or delay caused by the COVID-19 pandemic generally would not be covered. Contrast that with the following definitions (Definition Two and Definition Three, respectively):

> *"Force Majeure Event" means any act beyond a party's reasonable control.*

> *"Force Majeure Event" means any act beyond a party's reasonable control, including without limitation any of the following: (a) flood, fire, earthquake, or explosion; (b) epidemic, pandemic, or other health emergency, (c) war, invasion, hostilities (whether war is declared or not), terrorist threats or acts, riot, or other civil unrest; (d) government order or law; (e) actions, embargoes, or blockades in effect on or after the date of this Agreement; and (f) action by any governmental authority.*

In both Definition Two and Definition Three, an occurrence need not be specifically enumerated in order for it to constitute a *force majeure* event. If a party can show that the occurrence at issue was beyond its reasonable control, then the occurrence would be considered a *force majeure* event. In Definition Three, non-exclusive examples of occurrences that could constitute a *force majeure* event are provided to remove all doubt as to whether the parties expected them to be covered. (Note that Definition Three, unlike Definition One, includes "epidemic, pandemic, or other health emergency".)

Thought should be given as to whether all obligations of the parties under the agreement should be covered by the clause, or if it is appropriate to exclude certain obligations. For example, it is not unusual for payment obligations to be excluded (and therefore not excused by a *force majeure* event). On the one hand, a supplier or service provider may take the position that an exception for payment obligations is not appropriate for the obligation to pay for items supplied or services rendered prior to the occurrence of a *force majeure* event. On the other hand, if the *force majeure* event results in a failure of the banking system, then the affected customer or service recipient could hardly be expected to make payment until the banking system is back online.

Thought should also be given to what the parties' respective obligations and rights should be should a *force majeure* event occur. For example, should a *force majeure* event excuse the impacted party's obligations altogether, or merely excuse a delay to give the impacted party additional time to perform its obligations? If the latter, how much additional time should the impacted party be given? And what happens if the impacted party is unable to perform its obligations altogether, even if given additional time? Should the non-impacted party, or both parties, have the right to terminate the agreement under such circumstances?

Review should not be limited to *force majeure* clauses, however. Many agreements include provisions that trigger certain repercussion should a party fail to meet specified requirements, even if the failure doesn't rise to the level of being a breach of the agreement. For example, an agreement that grants to a party exclusive rights, like an exclusive distribution agreement or an exclusive intellectual property license, may make the exclusivity contingent upon that party satisfying certain "diligence" requirements. These may include making minimum purchases, sales, or revenue over a given period of time. The parties should consider whether and to what extent failure to satisfy such requirements due to a *force majeure* event should result in the party losing exclusivity. Also, many supply agreements are "sole source", meaning that the buyer is committing to purchase the items covered by the agreement only from that supplier. That commitment is often contingent upon the supplier being able to satisfy the buyer's requirements. If a *force majeure* event occurs that prevents the supplier from satisfying the buyer's requirements, should the buyer be permitted to purchase the item from a different supplier, at least until the *force majeure* event passes? If timely satisfaction of the buyer's requirements is critical, that may be appropriate. Examples relevant to our current situation are

the manufacture and supply of drugs, medical devices such as ventilators, and protective equipment such as masks. Often the provisions governing situations like those described above are excluded from *force majeure*. So whether it is during the drafting and negotiation of an agreement or upon the occurrence of a *force majeure* event, a front to back review of the agreement with an eye towards *force majeure* is appropriate.

As noted above, in the eyes of many business people, and even many lawyers, the *force majeure* clause was a box to be checked, not a provision requiring serious thought and negotiation. If that was ever a justifiable attitude (despite modern terrorism, increasingly wild weather, and several financial meltdowns), the current global public health crisis – affecting various individuals, markets, supply chains, health systems and countries differently – is a forceful reminder that we must all take these contractual clauses seriously.

Stay calm, stay safe, and may the Force Majeure be with you.

For questions about *force majeure* provisions or other commercial contracts-related matters, please contact Mike Cavaretta.

The author would like to acknowledge the contributions to this article by and give thanks to Riccarda Picker, Northeastern University School of Law (NUSL) LLM 2020.