



UNDERSTANDING FORCE MAJEURE AND HOW IT MAY IMPACT YOUR CONTRACTS DUE TO COVID-19

By Sherrie M. Flynn

The outbreak of the COVID-19 virus is having significant impacts on companies, including disruption of supply chains and performance of delivery obligations. As a result, some companies may desire to be excused from their contractual obligations due to these events to avoid losses that may arise from inability to perform to contract terms. This article discusses contractual issues resulting from the pandemic, including force majeure clauses, and impossibility, impracticability and frustration of purpose as legal excuses for nonperformance.

What is Force Majeure

Force majeure is defined as “unforeseeable circumstances that prevent someone from fulfilling a contract.” Force majeure clauses in contracts are intended to allocate risk between the parties when events make performance impossible. A force majeure clause frees both parties from obligation if extraordinary events prevent one or both parties from performing. These events must be unforeseeable and unavoidable, and not the result of a party’s actions. Hence they are considered “Acts of God.”

Examples of typical events that can trigger a force majeure clause include unpredictable natural disasters such as earthquakes, floods, or hurricanes, and riots or acts of war. So, can the COVID-19 pandemic constitute a force majeure event? It depends.

What if You Cannot Fulfill Your Contract Due to COVID-19

If you are a party in a contract and cannot perform due to the effects of COVID-19 (e.g., your business is ordered closed by the government, your employees cannot come to work as they are ill or caring for others affected by COVID-19, etc.), you should review your contract to see if it contains a force majeure clause, which is one of those common clauses that many view as boilerplate, but important in many contracts. If so, review the language of the clause to see what specific events are identified as triggering the right to cancel a contract. If it has specific language that includes an epidemic, pandemic or public health emergency, your force majeure clause may permit you to use the clause to terminate or suspend a contract. If, however, your clause includes broad, “catch-all” wording, such as “Acts of God”, then COVID-19 may or may not be considered a force majeure event as courts generally interpret force majeure clauses narrowly.

Once you have identified whether your contract may cover COVID-19, you must still show how COVID-19 has actually caused your failure to perform and that you took reasonable steps, in good faith, to “mitigate” (decrease) or avoid the effects of the force majeure on your contractual performance. Courts will also look to see whether the force majeure clause has notice requirements and, if so, whether you provided proper notice.

In any case, do not make a determination on your own regarding whether the force majeure clause in your contract excuses your performance. Instead, seek the advice of counsel.

What to Do if Your Contract Does Not Have a Force Majeure Clause

If your contract is silent on force majeure, all hope is not lost. In some cases, a party's performance may still be excused based on principals of impossibility, impracticability, or frustration of purpose. Generally, these excuses are also narrowly interpreted and applied by courts.

For example, contractual obligations can be excused if it becomes impossible to perform them because the promisor becomes incapacitated or dies. Impossibility may include quarantine or illness due to COVID-19. Additionally, if an irreplaceable good or component is contaminated because of COVID-19, performance may be excused if the good or component was required for performance. Performance may also be impossible in regions where there is a state-imposed "shelter-in-place" order due to COVID-19.

Performance may also be excused when a party can demonstrate that a supervening event has caused performance to become so difficult and expensive that it becomes impracticable, even though it may be technically possible. For example, if a company cannot secure raw materials without extreme difficulty and excessive and unreasonable expense due to COVID-19 causing shutdowns in supply, performance may be excused as impracticable. Impracticability does not apply, however, if the COVID-19 event merely renders performance more expensive.

Frustration of purpose is a limited excuse that applies when the main purpose for entering into the contract is destroyed due to a supervening event, and both parties knew of the purpose for entering into the contract. For example, if a company was contracted to provide security services for an event, but the event was cancelled due to COVID-19, the doctrine of frustration of purpose may excuse performance.

Steps to Take Once You Have Identified You Cannot Perform

Now that you have identified that COVID-19 has prevented your company from performing under an existing contract – such as your supplier has cancelled its contract, your employees cannot come to work, you are under a government order for your business to close, etc. – you should let your customer(s) know as soon as possible. Let them know the reasons you cannot perform. If there is a force majeure clause in your contract that applies, let them know you are exercising your rights under the contract. If no such clause exists, still let them know a legal reason your company cannot perform.

Your customer may complain about breach and damages they may be suffering because your company cannot perform, but issues of who is right and wrong will have to wait until the pandemic is history. You will at least have preserved your right to be excused from performance once business resumes.

Conclusion

As is stated above, because force majeure clauses are defined narrowly, it makes sense to employ legal counsel to help you review your existing contracts and determine if they include such a clause that may excuse performance in your circumstances. In addition, now that you know

what a force majeure clause can do in your contracts, you may want to start including such clauses in your future contracts. It can only help if you do so.

If you have questions concerning the applicability of a force majeure clause or other defenses for non-performance of a contract, contact the author at (559) 248-4820 or sflynn@ch-law.com.



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