Alert

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COZEN O'CONNOR

Contracting to Avoid Force Majeure Litigation in the Midst of the COVID-19 Pandemic

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We all know by now we are in the midst of a pandemic. Many businesses are either receiving or giving notice of their inability to satisfy contractual obligations due to the various government orders and shut downs. They are doing so largely in reliance upon *force majeure* clauses. Our prior publication addressed the propriety of reliance on these provisions. This article will address how to prevent future *force majeure* disputes now that we foresee the risk posed by COVID-19.

What is *force majeure* you ask? Quite literally, it means "superior force" in French. In contractual parlance, *force majeure* is a nuclear contractual termination option rarely invoked — and narrowly construed — that typically permits suspension or negation of contractual obligations due to an unforeseen "act of God" or specified qualifying event that renders performance physically or legally impossible by no fault of your own. Note that legal impossibility is different, and more extreme, than merely contract performance that is more difficult or unprofitable. Exercising this option requires the claimant to strictly adhere to the letter of the contract in terms of, among other things, the definition of qualifying events, required notice provisions, and any mitigation obligations.

Ultimately, *force majeure* clauses are intended to permit escape if something completely unforeseeable and outside a contracting party's control happens — like, for a timely example, a worldwide pandemic causing international government and business shut downs and wide-spread quarantines. For *force majeure* to excuse nonperformance, some correlation must be drawn between the occurrence of the event and the obligation of the non-performing party.[1]

What about *new* contracts?

Now that we know about COVID-19 and the pervasive shelter-in-place orders that brought most of the world's economy to a screeching halt, the "event" is arguably no longer unforeseen. It is no longer something for which we cannot plan ahead. While we still do not know how long this will last or when the economy will reopen, we do know that current interruptions, slow-downs, shortages, and personnel issues are impacting our business capacity and performance. Our knowledge and understanding of these issues in advance of undertaking contractual obligations creates a minefield ripe for future business disputes.

That is precisely why we must carefully negotiate *force majeure* clauses when entering into new business deals. The application of *force majeure* is an issue of contract interpretation governed by state law. While jurisdictional interpretation varies, it is safe to say that the vast majority of courts across the United States construe these clauses quite narrowly, according to their plain meaning. For example, the Superior Court of New Jersey relied upon New York law in refusing a *force majeure* defense on the basis that under the plain language of the contract, one pipeline's interruption did not contractually preclude the defendant from using other sources of gas to fulfill its contractual obligations.[2]

Thus, how a party contractually defines a *force majeure* event to include, or exclude, performance issues arising out of COVID-19, will ultimately dictate the availability of this contractual provision as a means to exculpate performance obligations.

To illustrate precisely how careful negotiation and drafting can prevent disputes and litigation, let's use this exemplar provision:

> Neither Party shall be liable for any loss, failure, or delay in the performance of its obligations under the terms and provisions of this Agreement to the extent that such loss, failure, or delay results from any of the following unknown and/or unanticipated events: fires; explosions;

> floods; storms; acts of God; pandemics; governmental acts, orders or regulations; hostilities; civil disturbances; strikes; labor difficulties; machinery breakdowns; transportation contingencies; difficulty in obtaining parts, supplies, or shipping facilities; delays of carriers; or any other cause beyond the reasonable control of the respective Party.

What if I want to ensure performance irrespective of COVID-19?

As mentioned before, we are all aware of our current situation. Arguably therefore, COVID-19 delays can no longer be considered "unknown or unanticipated." However, given the narrow construction that courts employ in enforcing these provisions, if companies are entering into a contract in the midst of this pandemic, the performance of which they need to guarantee, they might consider adding a belt and suspenders to our exemplar *force majeure* clause as follows:

> Notwithstanding the foregoing, any loss, failure, or delay arising out of or related to the COVID-19 pandemic shall not constitute a force majeure event.

What if I need the ability to suspend or terminate my obligations due to COVID-19?

If, instead, two companies need to enter into an agreement, but need to be able to suspend or terminate it if the situation does not improve or worsens, they might modify the language like this:

> Neither Party shall be liable for any loss, failure, or delay in the performance of its obligations under the terms and provisions of this Agreement to the extent that such loss, failure, or delay results from any of the following unknown and/or unanticipated events: fires; explosions; floods; storms; acts of God; **pandemics, including but not limited to further deteriorations arising out of COVID-19 which cause delays in performance for more than 90 days following execution of this agreement**; governmental acts, orders or regulations; hostilities; civil disturbances; strikes; labor difficulties; machinery breakdowns; transportation contingencies; difficulty in obtaining parts, supplies, or shipping facilities; delays of carriers; or any other cause beyond the reasonable control of the respective Party.

What if this is a long term contract, and I want protections against future pandemics?

Perhaps the parties are willing to take on the risk of performance associated with this year's COVID-19 pandemic; however, they need to protect their business interests in a longer-term contract to contemplate future pandemics, or even a resurgence of COVID-19. In that circumstance, they might consider amending the language as follows:

> Neither Party shall be liable for any loss, failure, or delay in the performance of its obligations under the terms and provisions of this Agreement to the extent that such loss, failure, or delay results from any of the following unknown and/or unanticipated events: fires; explosions; floods; storms; acts of God; **pandemics, including but not limited to a resurgence of COVID-19 in 2021 or thereafter**; governmental acts, orders or regulations; hostilities; civil disturbances; strikes; labor difficulties; machinery breakdowns; transportation contingencies; difficulty in obtaining parts, supplies, or shipping facilities; delays of carriers; or any other cause beyond the reasonable control of the respective Party.

As these examples hopefully demonstrate, specificity as to what constitutes a *force majeure* event is key. The more specific the parties to a contract are, the more likely they will avoid a dispute in the first place, and, if litigation becomes unavoidable, that a court will support their business interest.

In addition to what constitutes a *force majeure* event, commercial agreements may provide for a range of potential consequences, including performance and/or cost relief, liability for damages and termination. They also typically require notice, which must be provided in a very specific manner and within a very specific timeframe. Additional obligations, for example, mitigation efforts, may be included that require compliance in order to take advantage of the provision. Strict compliance with all of these provisions is necessary in order to avoid a claim that the contract was breached, preventing a claim under the *force majeure* clause.

In sum, companies negotiating commercial agreements in today's environment should proactively

consider the appropriate allocation of risk and consequences of further business deterioration resulting from the coronavirus outbreak. These considerations will help the parties negotiate *force majeure* provisions to best protect their interests and avoid disputes and litigation down the road. For companies in current contract negotiations, we recommend a careful review of the *force majeure* clause by a practitioner experienced with these issues in your jurisdiction.

Nothing in this article is intended to provide legal advice pertinent to any specific situation, as the facts and circumstances of each business deal are distinct and unique and these provisions are construed narrowly according to state law.

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[1] *See*, e.g., *Brooks v. Calloway*, 318 U.S. 120, 123 (1943).

[2] *See, Hess Corporation v. ENI Petroleum US, LLC*, 435 N.J. Super. 39 (2014).