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The Coronavirus and Force Majeure Clauses

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Beyond the human toll of the current global health crisis, the coronavirus outbreak is having serious economic repercussions to the global economy and the supply chains on which it depends. Dun & Bradstreet reported, "at least 51,000 (163 Fortune 1000) companies around the world have one or more direct or Tier 1 suppliers in the impacted regions, and at least five million companies (938 Fortune 1000) around the world have one or more Tier 2 suppliers in the impacted region." Factory closings, transportation restrictions and general concerns about a potential pandemic are causing shortages of critical supplies and employees, and are testing the bounds and obligations of various contracts entered into between vendors and customers.

As a result of this disruption, many businesses are assessing their contracts to understand the extent of their rights, remedies and obligations with respect to their business partners. Suppliers of goods and services unable to deliver on contractual obligations are looking to see what provisions, if any, may protect them from a default. And in turn, recipients encountering delays from suppliers unable to deliver goods and services in a timely manner (or at all) are also looking to their agreements to see what rights, obligations, and remedies they may have in these circumstances.

It is prudent for businesses to review the contracts underlying their commercial relationships impacted by this global health situation. Of particular note, to the extent an agreement includes a *force majeure* clause, it usually operates to relieve one or both parties of some or all of their contractual obligations if an unforeseeable event beyond either party's control prevents or delays full or partial performance of obligations under the contract. Some parties are taking the position that performance that is impaired because of the coronavirus outbreak is excused by such provisions. For example, since early February, the China Council for the Promotion of International Trade has issued *force majeure* certificates to help China-based companies support a position that "the epidemic is unforeseeable, unavoidable and insurmountable force majeure." Ultimately, however, whether the coronavirus outbreak constitutes a *force majeure* event under a particular contract will depend on the language of the contract at issue, the relationship between the epidemic and non-performance, and applicable law.

To assess a business' rights, obligations, and remedies, whether the business is the party unable to perform or such counterparty, the following should be considered:

- **What contract provisions are relevant?** Determine whether the contract includes a *force majeure* provision, and whether there any other relevant provisions to assess. Contractual provisions to review include any breach, termination, cancellation, or repudiation terms that may be applicable under the circumstances.
- **What law governs the contract?** Determine what law governs the contract. *Force majeure* terms, and the contract as a whole, will be interpreted from a perspective of applicable law. Even if the contract does not include a *force majeure* provision, a *force majeure* concept (such as the doctrine of impossibility or frustration) could be implied under applicable law.
- **How does the contract define a *force majeure* event? Is the provision broadly written?** Assess whether the outbreak of the coronavirus, or the efforts to contain it, constitute a *force majeure* event under the contract. Examples of relevant language that may be included are "disease," "epidemic," "pandemic," "quarantine," or "acts of government." Depending on the parties' prior negotiation and drafting, a contract may either explicitly list all qualifying events, or generally define a *force majeure* event as an event beyond the parties' control, leaving more room for interpretation. Broad, catch-all language may be interpreted differently depending on the applicable law.
- **Is the coronavirus outbreak the cause of the party's non-performance?** Consider whether the party could have timely performed if the outbreak did not

occur. If other factors contributed to the party's non-performance, a *force majeure* clause may not be applicable. For example, to the extent a company takes proactive steps to avoid further spread of the coronavirus, *e.g.*, by advising workers to stay home, does the resulting inability to perform constitute a *force majeure* event?

- **Does "prevented" or "delayed" performance trigger the *force majeure* clause?** The contract may detail the level of interference a party must experience prior to invoking the *force majeure.* Determine whether the *force majeure* event must have either, for example, prevented, hindered, or delayed performance for a party to exercise its rights. Depending on how the clause is drafted, a party may not necessarily be able to claim a *force majeure* in circumstances where it was not objectively impossible to perform.
- **Does the contract require notice?** *Force majeure* clauses may be conditional upon notice requirements. If so, determine when notice is required, and how notice must be provided to a counterparty. Compliance with notice requirements and mechanisms are important, as failure to do so may qualify as a breach of the contract.
- **What obligations are excused?** Evaluate whether all of the impacted party's obligations are excused or only those that are directly related to the coronavirus outbreak. Also, consider whether the obligations of the non-impacted party are relieved as well. For example, are the non-impacted party's payment obligations tolled? Does an exclusive supply relationship become non-exclusive to allow the non-impacted party to find other sources of goods or services?
- **What are the implications of a *force majeure* event?** Consider the various outcomes that may follow a *force majeure* event. For example, the party may be relieved of liability deriving from its non-performance, performance may be suspended, the parties may renegotiate and modify the contract's terms, or the parties may terminate the contract.
- **Does a termination right arise if the *force majeure* event continues for an extended period of time?** Evaluate whether a party has a termination right if the *force majeure* event continues for a specific length of time. If so, consider how the contract quantifies the period of time, and when it begins. For example, does the relevant period begin when the non-performing party first determined it could not perform its obligations, or when it provided notice of such to its counterparty?
- **Are there alternatives to performance?** Often, parties have an obligation to mitigate damages. Consider whether there are other means through which a party can perform. If there are, a party is likely required to take reasonable steps to perform through such other means, and will not be relieved of its contractual obligations. Consider whether the party not affected by the coronavirus outbreak is

obligated to mitigate damages in some way.

Ultimately, whether a party can exercise its rights under a *force majeure* clause must be determined on a case-by-case basis. At this time, affected businesses should also assess whether disruptions to their supply chains will impact other obligations or remedies, including financing agreements, ongoing acquisitions, or the availability of business interruption or similar insurance coverage.

Proskauer's cross-disciplinary, cross-jurisdictional Coronavirus Response Team is focused on supporting and addressing client concerns. Visit our Coronavirus Resource Center for guidance on risk management measures, practical steps businesses can take and resources to help manage ongoing operations.

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