

## Force Majeure Clauses – Why You Can Expect to Hear More About Them

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**Ben Rand:** Hello everybody and welcome to the Harris Beach podcast. In this episode we'll discuss the use and enforcement of force majeure clauses. As COVID-19 forces major business disruptions, these extraordinary act clauses are increasingly pertinent across nearly every industry. I'm joined today by Dave Clar, Rochester Partner and leader of the Firm's Corporate Practice Group and Elliot Hallak, Albany Partner and a member of the Firm's Business and Commercial Litigation Practice Group and Financial Institutions and Capital Market Industry Team. Elliot and Dave, thanks for joining us.

**Dave Clar:** Glad to be here.

**Ben Rand:** Courts have historically discouraged force majeure provisions and have strictly construed contracts in favor of performance. However, because COVID-19's a pandemic with unprecedented ramifications, the landscape regarding force majeure is likely to rapidly evolve. Before we dive into the heart of the matter, perhaps we should just discuss a little bit about what is the force majeure clause and why does it take on significance at this time?

**Dave Clar:** Thanks Ben. Let me jump in, a high level of force majeure events or circumstance is an extraordinary event, sort of outside the contemplation of the parties. So these can be acts of God, hurricanes, tornados, floods, weather-related instances, it could be war or terrorism. Sometimes these events could also be related to labor strikes. And obviously, you know, the issues and the challenges we're facing with respect to COVID-19, bring into play things like epidemics and pandemics and health crises of that nature. And then a force majeure clause in a contract is a clause that essentially says that one or both parties may be excused from performance in the event one of these identified extraordinary events prevents a party from fulfilling its contractual obligations.

**Ben Rand:** Given some of the lockdowns, stay-at-home orders and general economic instability as a result of COVID-19, what questions are you hearing from clients about this clause and what questions are you asking yourself? Perhaps Elliot, would you like to chime in on that?

**Elliot Hallak:** Yeah, sure. With about 90% of our country currently at stay-at-home orders, we are now talking about force majeure clauses, I think without exaggeration, this is something that most litigators may not have seen since their first year of law

school and for most corporate attorneys this is something that is generally a boilerplate provision in a contract that really hasn't been given more thought. And all of the sudden with the greatest pandemic of our lifetime, it has now, like you said, completely dominated the landscape and we are seeing this issue both from the corporate side and the litigation side like we never have before. Which is why as part of Harris Beach's COVID-19 response team, we thought it was important to bring together both practice areas, the litigation side and the corporate side because to deal with these force majeure clauses, you really need to address them from both practice areas and both fronts. The issues that we're hearing and seeing are very simple question of compliance that have very deep ramifications. What do I do? I've got this contract. I've got this event. We can't perform. I don't think I'm going to be able to perform. What do I do? What are my obligations? Am I going to be able to unwind or get out of this deal? At it's core, those are the questions that we're receiving from clients and the answer to that question is going to be very specific to (1) your contract and (2) your factual situation as to whether performance has really become impossible or whether there is a business disruption of some kind that has made things more difficult or delayed things but maybe not made it truly impossible and what the provisions of your contract are that may or may not allow you to have some remedy based on the inability to perform.

**Ben Rand:** Just a quick follow up question to that, is there a substantial body of law that will help guide the decisions on how that all plays out?

**Elliot Hallak:** At this point, it's something that really has not been litigated very much because this is a completely unprecedented event that, like I said, most of us have not seen in our lifetime. So, the body of law up to this point has been somewhat limited and before this pandemic, the general trend in the law that has interpreted force majeure clauses, has construed them relatively strictly in favor of requiring performance under a contract. So, for example, if you had a contract that relieved parties of their obligations for war or terrorism but does not include something like a pandemic, an outbreak, an epidemic, you might not have been able to get relief for this specific event because it was not included in your force majeure clause. There are common law theories that I know we can speak about later in this podcast, but as a general matter, up to this point, they have been construed relatively strictly and relatively in favor of requiring performance under a contract or holding a party in breach based upon the claimed impossibility based upon the event that has rendered performance impossible. Now I think at this point there is really no empirical data for this because New York State courts effectively remain closed at this point, with the exception of emergency filings, so New York State law has not developed at any point since this pandemic started, but I do expect as that as time goes on this is going to be a rapidly evolving area of law and we're going to see a lot of decisions and given the gravity of this event, I think, my expectation is going to be that these clauses are going to be more liberally applied and also the common law theories of impossibility of performance and practicability and/or frustration of purpose are

going to be used as means to excuse parties from performance based upon the impossibility resulting from the pandemic.

**Ben Rand:** So Dave it occurs to me that there's probably implications going forward too in terms of contracts and how they're drafted. So, in light of COVID-19, is there some specific drafting advice that you think clients need to know or that you'll be giving to clients with respect to clauses in their commercial contracts?

**Dave Clar:** Absolutely, and something we've sort of already started, as Elliot alluded to, historically, the force majeure provision has been under negotiated, often times seldom touched by the parties after the initial draft of the contract in which it appears. You know I think one thing that will become important is whether or not there's a specific reference to the force majeure event. Courts will look at does the event qualify as a force majeure event, was it foreseeable and could it be mitigated in any way, and was performance actually and truly impossible? And what's sort of unique about the challenges presented by COVID-19, is in a lot of respects it has made performance more difficult but not necessarily impossible. There's an awful lot of government mandates forcing people to stay at home and work but that doesn't necessarily mean that businesses can't be operating and folks can't be performing remotely. So is performance truly impossible, or not? New York courts will also look at is the specific event listed? So from a drafting standpoint, to answer your question more directly, I think it will be important to list pandemics, epidemics, viral outbreaks, those sorts of descriptions to cover this type of event. You probably can't find a contract drafted and signed more than six months ago that had any specific reference to coronavirus or COVID-19 and very few even referenced on a broader nature, the concept of a health outbreak, disease outbreak, viral outbreak or specifically, an epidemic or a pandemic. We have ever since this became an issue been including language very specific to cover this particular scenario or any comparable scenario, such that there is no question as to whether or not the event itself is listed and a possible trigger for excuse of performance. However, that's just the first bar and once it's listed there's still the relatively high bar for invoking the clause, which is, was the risk foreseeable and is performance truly impossible?

**Ben Rand:** Do you have any expectation, or if you had to guess, that COVID-19 could very well provide grounds for asserting the clause that would allow a party to walk away from a transaction?

**Dave Clar:** I think we certainly expect that there will be situations where, for example, a business was deemed to be non-essential and therefore under some sort of government mandate or edict or regulation that prevented that business from operating, that that would truly sort of make and render performance impossible. And if performance in that respect is impossible and the force majeure clause arguably lists an event that covers the coronavirus then I think there would be at

least the possibility of invocation of the force majeure clause as a valid excuse for nonperformance.

**Ben Rand:** It occurs to me Dave that in any sort of contractual matter, communication is very critical. How critical would you say at this time that flexibility might be in terms of both sides of the contract working out some of the impacts of this event?

**Dave Clar:** That's a great question and it's very interesting. We've had a number of clients who are looking at this concept, excuse of performance due to the occurrence of a force majeure event from both sides. For example, you may have a manufacturing company with its work force forced to work remotely, and its processes are delayed, its production is minimized, and its ability to satisfy its contractual obligations to get products designed, manufactured and shipped on time, has been compromised. By the same token, their customer may not be in a position to accept delivery of those goods for some of the same reasons. Their factory may not be ready for the new piece of equipment, they may not have the folks in place for installation, for training on new equipment. They may no longer have the need for goods or products because their customer base has slowed down. So the economic slow down that we are experiencing sort of has buyers and sellers both caught up in this. So absolutely communication becomes critical due to the uncertainty of how the courts may actually treat some of these force majeure clauses and whether or not they will render them effective or not. A lot of that can be avoided with good communication and the parties may find themselves fairly aligned in terms of a revised schedule or delayed performance.

**Elliot Hallak:** To build onto Dave's point, I think it's very critical for people to address these issues early and up front as soon as you can both from a business and a public relations standpoint as well as from a legal standpoint because one of your obligations in invoking a force majeure clause is that you've taken all attempts to avoid or mitigate the consequences of the impossibility of performance, which is why our litigation team and our corporate team have been working together with clients to help message this to either their suppliers, or their consumers or whoever they're contracting with. It's very important to deal with those issues up front. If you think you're going to be in a position where you're not able to perform at some point, you might still be able to perform now, but that might become impossible later, if your supply chain runs out or if your purchaser on the other side dries up, you want to address those issues as early as you can. It's very important for businesses to get that message out to their consumers, the people that they contract, let them know we're okay now, we're still open, we want to do business, however, there may come a time where it does become impossible, despite our best efforts. You provide that notification to somebody up front that's carefully drafted and you give them the opportunity to potentially mitigate some of the effects and the advanced notification that you may in fact not be able to perform under this contract despite your best efforts. It's just very sound practice as a business to remain in contact with your customers and tackle these issues up

front early as soon as you think you're going to run into an issue with performance.

**Ben Rand:** It does sound to me like there are a million and one different permutations of this question and so I'm just wondering if you see it sort of being litigated on a case-by-case basis or do you think there's a need for some sort of legislative guidance to help put down some rules to help make the application more uniform?

**Elliot Hallak:** Well there certainly have been quite a few Executive Orders and one of the clauses that is often seen in a force majeure clause is government action and government action can resolve the issue very clearly as to whether or not contracts are in fact possible to perform. It remains to be seen because we are in unchartered territory right now as to whether there's going to be legislation on this particular issue. But my expectation is that this is going to be heavily litigated and it's going to be litigated on a case-by-case basis. As David mentioned before, you're going to have many situations where a contract may not be physically impossible but it's just going to be more difficult to perform. We've gotten calls from people who may have taken out loans or leases and they may not be able to take possession of a property right now but does that make it impossible for the entire contract to be performed? There are other instances that seem to be more clear, you might have booked a venue for a particular date and there's a government regulation that precludes public gatherings and it's clear that that is impossible to perform based on a government regulation that says this place can't be open, this event can't go forward. So we're gonna see many different factual scenarios that are going to get litigated in the court. There are some that are going to be more clear inability to perform. I think, unfortunately, there are going to be some parties that seek to take advantage of the inability to perform, or a temporary business disruption to try to avoid their obligations under a contract as a whole. So I think courts are going to look at this on a case-by-case scenario and like Dave said, will see whether performance has really become impossible or whether it just has been delayed for a period of time. And as David mentioned, force majeure clauses have not had the complexity that I think they will have following this event, where some of the more complex ones might have provisions in there that talk about a time limitation for impossibility or notice requirement for impossibility and some of them are very short and just simply say that in the event of certain events, like an act of God, war, terrorism, government action, disease, that neither side has any liability. So I think we're gonna see a lot of development on the contractual side. I think we're going to see it litigated heavily on the court side and it remains to be seen whether there's any legislative guidance other than the Executive Orders that we're seeing that would really control whether performance is impossible but it remains to be seen whether there's any kind of blanket relief that's provided to people based upon this pandemic and an innate ability to perform at the legislative level.

**Ben Rand:** We alluded to it a little earlier in our section about communication, but are there other things that client ought to be doing now to prepare in terms of evaluating the force majeure clause and how to enforce it and/or defend against it?

I think the best thing that clients and businesses can do is reach out to their attorneys, reach out to us, let us know what your current situation is because if you feel like you're going to be in a situation where either your business or somebody that you do business with is unable to perform, we're able to position you as best we can, give you guidance, help you with notifications in advance that can put you in the best posture in the event there is a dispute that arises based on the inability of either yourself or the party that you contract with to perform under their contract.

**Dave Clar:** I think the one thing, Ben, that we can do, and that our clients should be doing, is performing a risk assessment. Understanding what contract you have, whether or not those contracts have force majeure clauses in them, or not. If they do, what do those clauses specifically say? And then sort of marrying up the lingo and the documentation analysis with, as Elliot suggested, sort of the lay of the land with respect to the ability of the client to perform its obligations. And in particular, as we look at an assessed risk, you know that force majeure clause may or may not exist in the contract. It will depend on the governing law of the contract as to how specific the events need to be in terms to offer coverage. It will also speak to, as Elliot indicated, is there a notice requirement, is there a mitigation obligation, does the event have to be foreseeable, or not? And also, will a force majeure event excuse performance for a period of time so that your performance will be delayed for the duration of the event, or does it provide one or both parties the ability to terminate and trigger any sort of damages associated with termination, based on that? So there's an awful lot of nuance to the discussion. And I think right now it's important to take a global risk assessment with respect to contractual obligations that you have in terms of performance or receipt so that you can start to evaluate what can be done proactively in terms of reaching out to customers or clients and providing notification.

**Ben Rand:** Just as one final question to both of you – it sounds like both from a client and an attorney standpoint, we're in the thick of this already in terms of making these evaluations, are there some other ways that our teams are helping clients navigate this evolving area of law, or are there areas that you think we will be needing to look at into the future?

**Dave Clar:** Yeah, I think in addition to sort of the risk assessment looking backwards, certainly on a going forward basis this particular clause will get a lot more attention, probably be the subject of more intense negotiation and certainly this is an area that Harris Beach is already actively involved and engaged with its clients in putting together sort of best practice language around force majeure provisions in contracts in light of the situation we're in, relative to the coronavirus.

**Elliot Hallak:** And just to build on what Dave said I think it's also important when you're contemplating the messaging that you might send to customers on these events, it's important to run these issues through counsel too because in the event of a dispute you should be prepared that any notice that you provide to the party that you're contracting with is likely to end up as an exhibit in a litigation, so it would be wise to take a few moments with your counsel, look at the message you're sending. We always try to strike the balance between your business and your public relations concerns as well as making sure that the message is not going to be harmful and is going to help bolster your legal position in the event of a dispute and really find that right balance in the messaging. So it's very important to have your counsel involved as early as you can even if it's just for some kind of consult to make sure that you're best positioning yourself when these events arise and they will arise with more frequency as this pandemic evolves. And also, like Dave said these things are going to get quite a bit more attention and there's going to be a lot more clarity in these clauses going forward as to which party bares the risk in the event of another event like this. It's going to be given attention like it never has before and it's important that you get the right counsel and know what side of the risk you're going to be baring in the event we have another event like this, performance becomes impossible.

**Ben Rand:** It makes a lot of sense. Thank you both for joining us today and thanks everybody for listening. For more information including how to contact Dave and Elliot, please visit our COVID-19 response page at [www.HarrisBeach.com/COVID19](http://www.HarrisBeach.com/COVID19).

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