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Contractual Force Majeure Provisions and the Spreading Coronavirus

Parties should scrutinize their existing contracts to see if those contracts include a force majeure clause and to see whether coronavirus is a force majeure event.

By **David B. Saxe and Michael Mix** | March 09, 2020

The worldwide spread of the coronavirus requires lawyers to examine client contracts at risk for disruption or non-performance due to the epidemic. If the contract contains what is commonly known as a force majeure provision, a careful analysis of the clause is mandatory.

Force majeure is a "clause[] excusing nonperformance due to circumstances beyond the control of the parties." *Kel Kim v. Central Mkts.*, 70 N.Y.2d 900, 902 (1987). One of the dominant news stories of 2020 has been COVID-19, commonly known as the coronavirus. With over 100,000 confirmed cases, including over 80,000 in China, over 7,000 in South Korea, and over 7,000 in Italy, business around the world is beginning to be significantly disrupted. Parties who cannot perform their contractual obligations due to coronavirus (i.e., parties or their employees become seriously ill, or parties or their employees cannot work due to virus-related legal restrictions) may invoke force majeure. There have already been reports of Chinese companies invoking force majeure clauses in contracts in an attempt to avoid performance of their contracts. See, e.g., *PetroChina Suspends Some Gas Contracts as Coronavirus Hits Demand: Sources (https://www.nytimes.com/reuters/2020/03/05/business/05reuters-petrochina-gas-exclusive.html)*, N.Y. Times (March 5, 2020). With the increasing number of coronavirus cases around the world, including the United States, it is only a matter of time before contract counterparties outside of China attempt to argue that their contractual duties should be excused due to coronavirus.

The doctrine of force majeure is based on the common law doctrine of impossibility of performance. Under the common law, impossibility of performance is "applied narrowly, due in part to judicial recognition that the purpose of contract law is to allocate the risks that might affect performance and that performance should be excused only in extreme circumstances." *Kel Kim*, 70 N.Y.2d at 902. "Impossibility excuses a party's performance only when the destruction of the subject matter of the contract or the means of performance makes performance objectively impossible. Moreover, the impossibility must be produced by an unanticipated event that could not have been foreseen or guarded against the contract." Id. "The excuse of impossibility is generally limited to the destruction of the means of performance by an act of God, *vis major*, or by law." *Kolodin v. Valenti*, 115 A.D.3d 197, 200 (1st Dept. 2014) (internal quotation marks omitted). As such, events which could excuse performance would likely be natural disasters such as floods, earthquakes, volcanic eruptions, tornados, hurricanes, etc., assuming such disasters were unanticipated. "[W]here impossibility or difficulty of performance is occasioned only by financial difficulty or economic hardship, even to the extent of insolvency or bankruptcy, performance of a contract is not excused." *407 E. 61st Garage, Inc. v. Savoy Fifth Ave. Corp.*, 23 N.Y.2d 275, 281 (1968) (citations omitted).

The UCC also provides limited protection for a seller whose performance has been made impossible. UCC §2-615(a) states that "[d]elay in delivery or non-delivery in whole or in part by a seller ... is not a breach of his duty under a contract for sale if performance as agreed has been made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid." Similar to the doctrine of impossibility of performance, UCC §2-615 is narrow and only applies to "unforeseen supervening circumstances not within the contemplation of the parties at the time of contracting." UCC §2-615 cmt. 1.

Parties—especially sophisticated ones—frequently include force majeure clauses in their contracts. Yet, contractual force majeure clauses "provide a similarly narrow defense." *Kel Kim*, 70 N.Y.2d at 902. "Ordinarily, only if the force majeure clause specifically includes the event that actually prevents a party's performance will that party be excused." Id. at 902-03. See also *Constellation Energy Servs. of N.Y. v. New Water St.*, 146 A.D.3d 557, 558 (1st Dept. 2017) ("Force majeure clauses are to be interpreted in accord with their purpose, which is to limit damages in a case where the reasonable expectation of the parties and the performance of the contract have been frustrated by circumstances beyond the control of the parties. When the parties have themselves defined the contours of force majeure in their agreement, those contours dictate the application, effect, and scope of force majeure.") (internal citations, quotation marks, and brackets omitted). As such, contractual force majeure provisions expand the narrow applicability of the doctrine of impossibility of performance by permitting contract counterparties to specifically enumerate the acts which could conceivably excuse performance. Moreover, some force majeure clauses may not excuse a party's performance entirely, but only may suspend performance during the pendency of the force majeure event, or might provide for shipment of a lower amount of goods.

The application of force majeure to the coronavirus outbreak will depend significantly on the language of parties' contracts. Some contracts may include "epidemic" as an enumerated example of a contractual force majeure event. See, e.g., *Wyndham Hotel Grp. Int'l v. Silver Entm't*, No. 15-CV-7996 (JPO), 2018 U.S. Dist. LEXIS 52144, at *27 (S.D.N.Y. March 28, 2018) (quoting force majeure clause that includes "epidemic" as an example of force majeure event); *Aukema v. Chesapeake Appalachia*, 904 F. Supp. 2d 199, 206 (N.D.N.Y. 2012) (same); *City of New York v. R.A.M Used Auto Parts*, 43 Misc. 3d 1205(A) (Sup. Ct. N.Y. Cty. 2014) (same). In those cases, a party's performance due to coronavirus may be excused because "the force majeure clause specifically includes the event that actually prevents a party's performance." *Kel Kim*, 70 N.Y.2d at 902.

However, other contracts may not enumerate in its list of force majeure events an "epidemic" or anything else that might encompass coronavirus. In that event, under the courts' narrow interpretation of contractual force majeure clauses, performance will likely not be excused. Other contracts—such as between less sophisticated parties and/or involving smaller transactions—may not contain a contractual force majeure clause at all. In those cases, parties seeking to excuse performance due to coronavirus may attempt to rely on the common law doctrine of impossibility. However, as explained above, the common law doctrine is limited and narrow, and thus is unlikely to excuse a party's performance because coronavirus might not be considered an act of God, and is certainly not an act of law. A party may be more likely to be successful in invoking the doctrine of impossibility due to coronavirus if the United States or other countries begin to pass laws restricting travel, restricting shipment of goods, or quarantining citizens. In sale contracts, UCC §2-615 might not provide adequate protection to a seller if a court determines that non-performance due to an epidemic such as coronavirus was "within the contemplation of the parties at the time of contracting."

Parties should scrutinize their existing contracts to see if those contracts include a force majeure clause and to see whether coronavirus is a force majeure event. And going forward, parties should insist that their contracts include "epidemic" as a force majeure event in case performance becomes impossible due to coronavirus or a future epidemic. Parties should also ensure that their contracts contain a provision specifically enumerating what happens when the force majeure event is in effect (i.e., only temporarily suspending performance or providing for the supply of fewer goods).

Finally, U.S.-based parties should be aware of the risk of not being able to enforce a judgment in certain foreign countries, if a U.S. party is forced to sue a non-U.S. party for an unjustified declaration of force majeure due to coronavirus. For example, it is notoriously difficult to enforce a judgment in China. See, e.g., *In re Giant Interactive Grp.*, 279 F.R.D. 151, 164 (S.D.N.Y. 2011) (recognizing the "challenge of enforcing a judgment in China"). In light of the potential difficulty in collecting on a judgment in China, parties should consider negotiating with Chinese parties declaring force majeure instead of litigating.

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