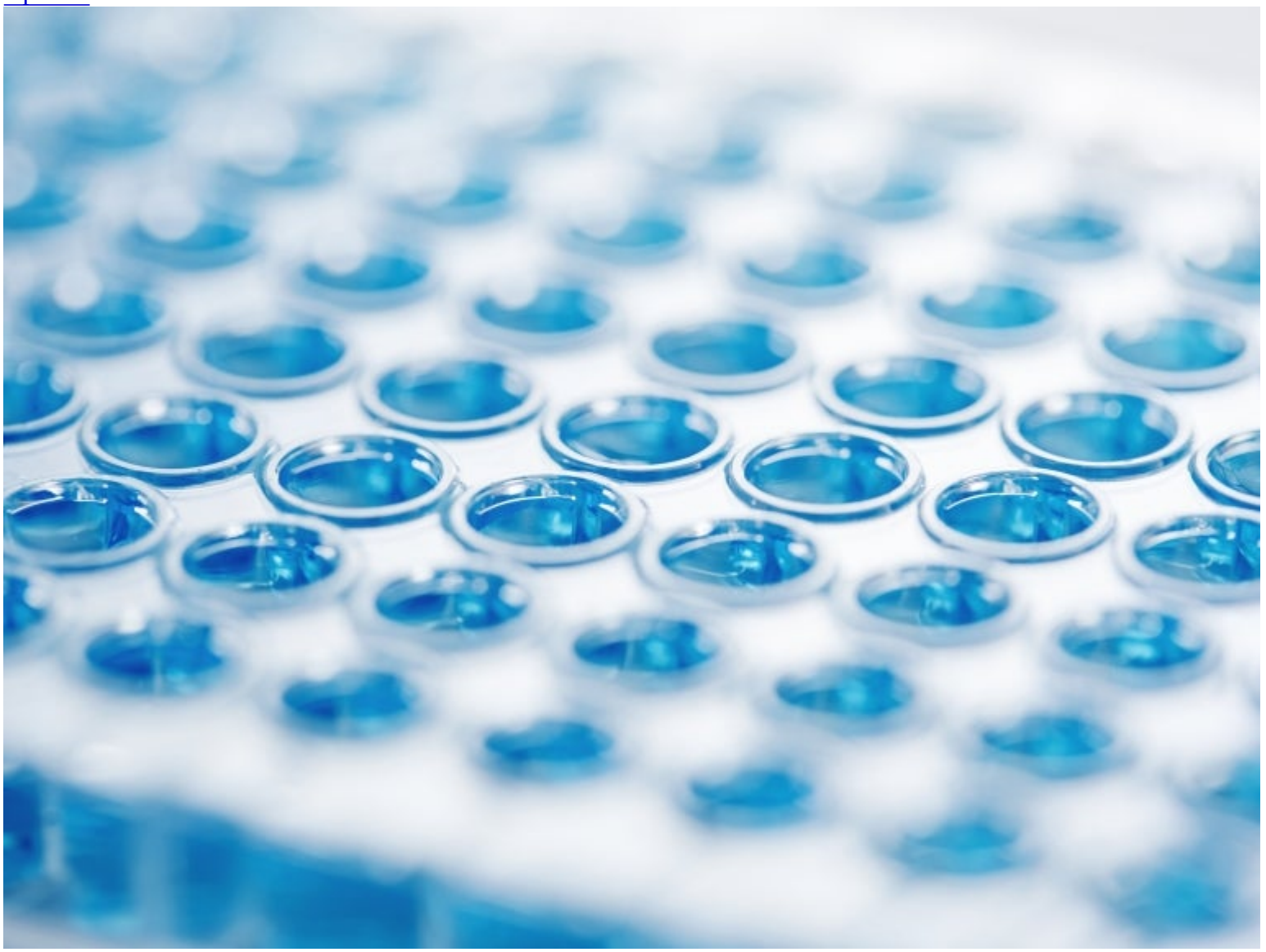
Updates



With the escalating economic turmoil created by the coronavirus (COVID-19), companies are scrutinizing the force majeure provisions in their commercial agreements.

Some companies are seeking to determine whether they can rely on such provisions to avoid or delay their performance obligations under such agreements; other companies are concerned that their business partners may invoke such provisions to suspend performance. Having spent considerable time reviewing force majeure provisions over the past few weeks, we share here our thoughts on the interpretation and application of such provisions amidst a worldwide pandemic of almost unimaginable scale.

Interpreting Force Majeure Provisions

The growing outbreak of the coronavirus has affected, and will continue to affect, businesses and economies around the world. The World Health Organization has categorized the coronavirus as a pandemic, and, in this country, California, New York, and many other states have issued state-wide "stay-at-home" orders, with more states expected to follow. The pandemic has severely impaired the ability of some companies to perform under many agreements, leading to close review of contractual provisions related to performance obligations, especially force majeure provisions.

In general, a force majeure provision is designed to excuse performance when it is delayed or prevented by outside events. Although oft-ignored as boilerplate language, careful review and negotiation of force majeure provisions is necessary to ensure that a party—particularly the party that will be the primary provider of services under the agreement—is protected from situations outside of its control. A typical provision (1) lists certain types of outside events that are agreed to potentially excuse a party for nonperformance, and (2) provides that a party's nonperformance due to such an event will be excused, at least for the duration of the triggering event.

Where a party invokes a contract's force majeure provision to excuse its obligation to perform under the contract, the success of such excuse depends on the obligations at issue, the precise wording of the provision, the specific outside event that is alleged to have triggered the provision, and the variations in contract interpretation rules under governing law. In some situations, an outside event may allow the affected party to delay its performance, but in other situations, the outside event may release such party from all of its unperformed obligations under the agreement.

Under most force majeure provisions, the mere occurrence of a force majeure event will often be insufficient to excuse a party's performance of an obligation; rather, depending on the precise wording of the provision, the force majeure event must somehow prevent, make impossible, make impracticable, or delay the party's performance. In other words, the force majeure event must be the cause of the party's inability to perform. Further, if the force majeure event affects some, but not all, of the party's obligations, the unaffected obligations most likely remain in effect unless the provision expressly provides otherwise.

The case law relating to force majeure provisions varies across jurisdictions, which implicates the choice of law provision, another boilerplate contract clause that is often overlooked. In the following sections, we review how force majeure provisions are generally interpreted under New York and California law.

New York Law

Under New York law, force majeure provisions are narrowly construed. The hallmark New York case on force majeure is *Kel Kim Corp. v. Central Markets, Inc.*, 70 N.Y.2d 900, 902 (1987), which involved a commercial lease for a roller skating rink. Generally, in order to excuse performance, an outside event must be expressly identified in the contract's force majeure provision as a triggering event; accordingly, if, for example, pandemics are not covered under the listed items constituting force majeure events, a party may have difficulty relying on a pandemic to excuse performance.

In the contract at issue in *Kel Kim*, the force majeure provision included a broad, "catchall" clause (i.e., ". . . or other similar causes beyond the control of such party") of the sort commonly found in these types of provisions. *Id.* at 903. Even if a pandemic is not covered by the enumerated force majeure events, the affected party could argue that it gets picked up by the catchall clause. New York courts, however, generally require that an unlisted

event must be similar in type to the listed events in order to qualify as a force majeure event. In explaining its interpretation of the catchall language in *Kel Kim*, the court explained, "The principle of interpretation applicable to such clauses is that the general words are not to be given expansive meaning; they are confined to things of the same kind or nature as the particular matters mentioned." *Id.* at 903. In other words, New York courts do not give the most expansive meaning possible to general language of excuse, so, if an event does not clearly fall within an expressly listed category, it must still be of the same general kind as the enumerated events in order for the catchall clause to have its intended effect.

California Law

California courts also tend to construe force majeure provisions narrowly. As in New York, when particular events are enumerated as force majeure events, even where unrestricted catchall language is used, a court will likely interpret the provision to capture only unlisted events that are similar to the listed events. California law, however, goes one step further: Unless a contract explicitly identifies an event as a force majeure event, the event generally must be unforeseeable at the time of contracting to qualify as such. *Free Range Content, Inc. v. Google Inc.*, 2016 WL 2902332, at *6 (N.D. Cal., May 13, 2016). When contracting parties contemplate a known risk, California courts expect parties to allocate that risk with specific provisions in the contract rather than rely on a boilerplate catchall provision. As discussed above, if an event does not fall within the expressly listed event types, a catchall would bring the event at issue within scope only if it is similar to the listed events and was unforeseeable at the time of contracting. Interestingly, as a consequence of this interpretation, it is conceivable that a California court could find that a pandemic like the one before us was unforeseeable for a contract in effect today, but having now seen the consequences of a pandemic, it may not be deemed unforeseeable for contracts entered into from this point onward.

Other Doctrines That Excuse Performance

Force majeure is not the only way that performance may be excused under a contract. In addition to determining its rights under the force majeure provision, a party seeking to avoid performance of a contractual obligation should consider common law doctrines that may excuse performance of such obligation, such as impossibility, impracticability, and frustration of purpose.

In New York, the *Kel Kim* decision discussed above also addressed the impossibility defense, which, even in the absence of an applicable force majeure provision, excuses a party's performance "when the destruction of the subject matter of the contract or the means of performance makes performance objectively impossible." *Kel Kim Corp.*, 70 N.Y.2d at 902. Additionally, the impossibility must be the result of an "unanticipated event that could not have been foreseen or guarded against in the contract." *Id.* Although the coronavirus would presumably be viewed by courts as unanticipated with respect to a contract signed prior to its outbreak, the particular facts of the situation at hand would need to be carefully reviewed to determine whether the coronavirus makes performance objectively impossible. Additionally, even if the coronavirus itself does not make a party's performance objectively impossible, a party seeking to avoid performance will want to consider whether a governmental order relating to the virus might do so (e.g., an obligation to host an event at a restaurant that has been closed as a result of a government decree shutting down all restaurants or prohibiting gatherings of more than a handful of people).

California law recognizes impossibility as a defense to a breach of contract claim when the breaching party's performance was prevented or delayed by an "irresistible, superhuman cause." Cal. Civ. Code § 1511. The

California Supreme Court has interpreted "irresistible and superhuman cause" to mean "those natural causes, the effects of which cannot be prevented by the exercise of prudence, diligence, and care." *Fay v. Pac. Imp. Co.*, 93 Cal. 253, 28 P. 943 (1892); *Ryan v. Rogers*, 96 Cal. 349, 353 (1892). For a party seeking to excuse performance under a contract governed by California law, the analysis should take into account this common law doctrine in addition to the contract's force majeure provision, if any.

Analyzing a Force Majeure Provision

As noted above, the precise wording of a contract's force majeure provision will be essential to determining whether such provision excuses a party's performance. Consider, for example, this fairly typical force majeure provision:

Neither party to this Agreement shall be responsible to the other party for non-performance or delay in performance of its obligations herein due to acts of God, acts of government, wars, riots, strikes, or other labor stoppages or shortages, or other causes beyond the control of the parties that make it impossible for the non-performing party to perform.

At first glance, this appears to be a broad, sweeping provision: The enumerated list includes a variety of force majeure events and ends with a catchall clause. Yet a party seeking to rely on this language to suspend its performance due to the coronavirus may face objections from the contract's counterparty, on several grounds.

First, the objecting counterparty is likely to point out that none of the expressly listed items qualifying as force majeure events includes "epidemics," "pandemics," "disease outbreaks," "public health emergencies," or any other term that would cover the coronavirus. Although the above provision does include "acts of God," the counterparty may argue that New York, California and possibly other jurisdictions tend to interpret enumerated items in a force majeure provision narrowly, such that the term "acts of God," while covering natural disasters, may not cover pandemics (biblical plagues notwithstanding).

Second, depending on the applicable law, the objecting counterparty may argue that the catchall clause is inapplicable, on the theory that the enumerated events are not sufficiently similar to the coronavirus such that the virus would be a qualifying force majeure event. In California, the counterparty may also question whether the unlisted event was truly unforeseeable. After all, the counterparty is likely to observe, that while they are (fortunately) very uncommon, this is not the first pandemic in history.

Finally, the objecting counterparty may note that the above-quoted provision requires that the event at issue "make it impossible" to perform, which is a more difficult standard than impracticability or, better yet for the non-performing party, no standard. Thus, subject to the specific underlying circumstances and the applicable jurisdiction, a party seeking to use the coronavirus to invoke the force majeure provision can expect to receive resistance from the counterparty that is demanding performance.

Whether pandemics are covered by the force majeure provision is not the end of the inquiry; many force majeure provisions, like the one quoted above, expressly enumerate "acts of government" or "governmental orders" as force majeure events. Given the number of state and local governments that have very recently declared states of emergency and restricted a wide range of activities (e.g., "stay-at-home" orders and mandatory closures of "non-essential" businesses), the party seeking to be excused from performance under the above-quoted force majeure provision could argue that such a governmental order constitutes a covered "act of government" if the party can

show that such governmental order makes performance impossible. As pandemic-related government orders and decrees become more sweeping and restrictive on a daily basis, it may be that a party that today desires to suspend its performance will find that tomorrow it is in fact unable to perform.

Additional Considerations Regarding Force Majeure Provisions

In addition to determining whether a triggering event has occurred, there may be other clauses in a force majeure provision that will impact the ability of a party to successful invoke the provision to excuse its performance. As examples:

Is there an obligation to provide notice? Some force majeure provisions include an express provision requiring the party seeking to have its performance excused to provide notice (often prompt written notice) to the other party that a triggering event has or is likely to occur. Failure to provide such requisite notice could defeat a party's effort to suspend performance due to a force majeure event.

Is there a duty to mitigate? Even if a triggering event has occurred, the force majeure provision at issue may expressly require the affected party to take affirmative steps to mitigate the impact of such nonperformance on the other party. If such an obligation is imposed, the party seeking to invoke the force majeure provision will need to consider what mitigation steps would need to be undertaken—or, for that matter, could be undertaken, given the circumstances.

Does the non-affected party have a right to terminate? Some force majeure provisions include a right for the non-affected party to terminate the agreement if the affected party's performance is suspended for more than a specified period of time (e.g., 14 days, 30 days, 45 days, etc.). If such a right is incorporated into the force majeure provision, the party seeking to suspend performance will need to consider the likely duration of the force majeure event, and whether the non-affected party may ultimately be in the position to terminate the contract.

The coronavirus outbreak is a stark reminder of the importance of force majeure provisions, which are so often dismissed as mere boilerplate. To the contrary, these provisions should be carefully drafted and negotiated, taking into account the applicable law, the relevant industry and the unique nature of your deal and the services to be performed. We separately offer guidance on how to address the special circumstances of the coronavirus in key provisions of to-be-negotiated contracts in a related update that can be read here. In addition, please see our earlier updates on force majeure considerations from a litigation perspective and on contractual considerations in the wake of COVID-19.

Please stay safe and healthy.

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