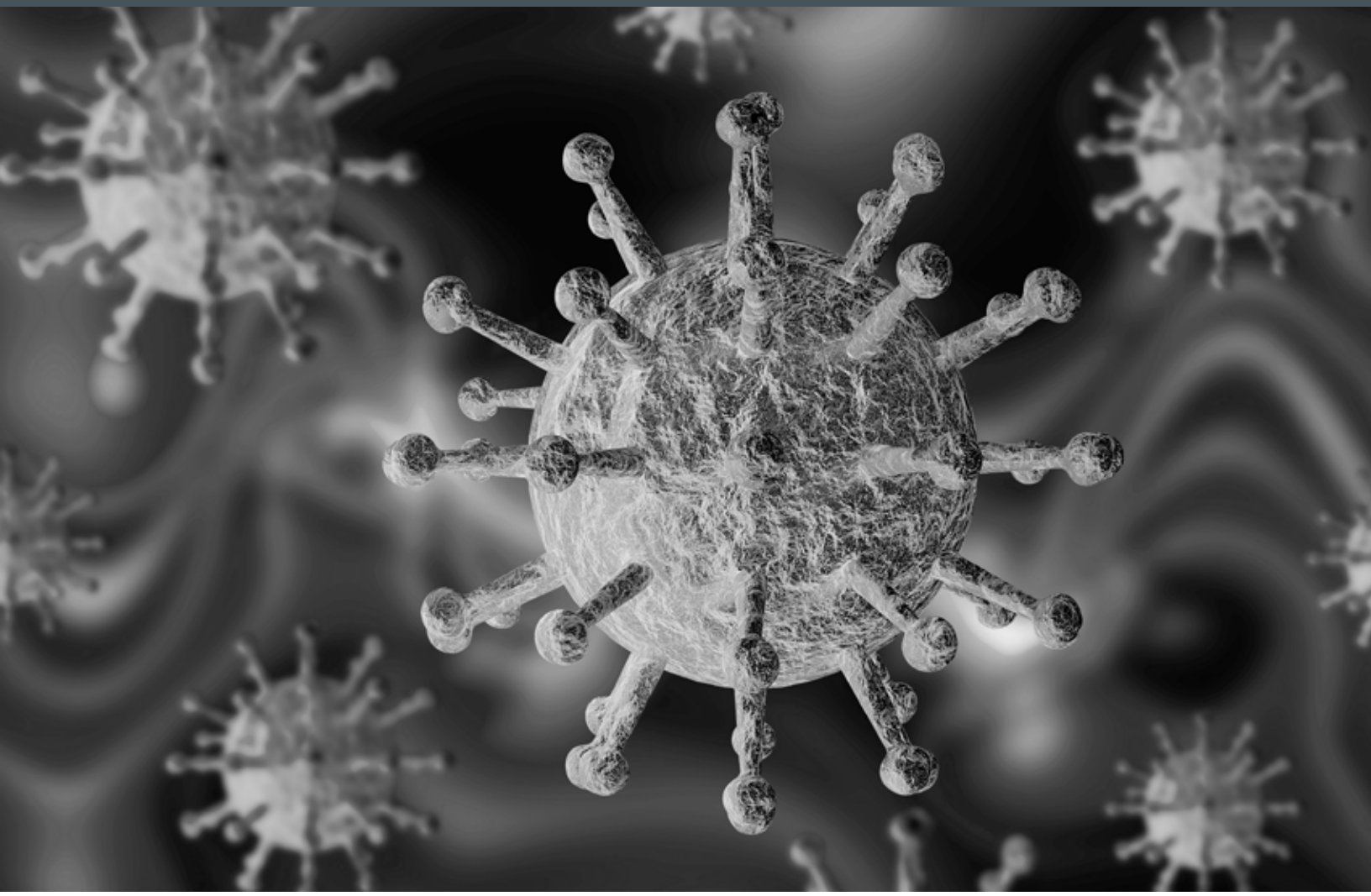

THE COVID-19 PANDEMIC AND THE CONTRACTUAL FORCE MAJEURE LANDSCAPE

Often considered mere boilerplate, contractual force majeure (FM) provisions are taking on far greater significance in light of the global economic slowdown following the spread of COVID-19. In the last 20 years, the world has been exposed to multiple destructive health crises. SARS in 2002 and 2003, Swine flu in 2009, MERS in 2012, Ebola between 2014 and 2016, Zika in 2015, and now COVID-19.

As the severity of COVID-19 spreads, companies are grappling with an inability to maintain regular business operations. Governments are taking various actions, including shutting down non-essential activities, in an attempt to restrain the novel coronavirus from spreading. The rapid progression of this virus has created a situation where parties are unable keep up with contractual obligations due to a wide range of factors, which include governmental orders, social distancing, the unavailability of critical infrastructure such as ports and terminals, or supply chain issues. Undoubtedly, in an attempt to excuse contractual non-performance or potentially to terminate a contract, a FM clause will take on far greater significance than originally contemplated.

The Force Majeure Doctrine

The FM doctrine grew out of the common law and is recognized under the general maritime law and state law. Under common law, a party may utilize FM to excuse performance and/or potentially terminate a contract, where performance becomes impossible as a result of a reasonably unforeseeable event outside the parties' control. Such a reasonably unforeseeable event is called a "force majeure".

Over time, the common law FM doctrine was adapted into a standard contract clause, which is often glossed over during negotiations. The FM clause in a contract allows either party to suspend or excuse its performance if certain specified events set forth in the FM clause occur. A FM clause enables parties to be relieved from their contractual duties when performance is prevented by a FM event. If a FM event persists for longer than a specified period of time, a contractual right to terminate may arise. To trigger the FM clause, the party claiming FM bears the burden of proving that: (1) a FM event occurred, and (2) the FM event is the reason that the contract cannot be performed.

A FM clause is found in most maritime contracts. To trigger the FM clause, timely notice must be made by the party claiming FM. There must be a causal link between the FM event and the failure to perform. Some FM provisions may limit the impact of the event by distance or time.

A party may be required to show that it made a reasonable effort to mitigate the effects of the FM event. Texas State law does not, however, require the party invoking FM to demonstrate that it exercised reasonable diligence to avoid the disruption unless such reasonable diligence is expressly stated in the FM clause.

If the FM provision does in fact apply, the non-performing party is excused as long as the event continues, and termination of the whole contract may be possible if the event continues for an extended period of time as specified in the contract.

Is the Covid-19 Pandemic a Force Majeure Event?

Litigation often centers on whether a FM event exists. A FM clause will set forth a laundry list of specific FM events. Common examples of FM events include: terrorist attacks, typhoons, hurricanes, storms of unprecedented magnitude, flood, volcanic eruption, earthquake, explosion or fire, quarantine, piracy, war, and the ubiquitous "act of God." A FM clause will often contain a catchall phrase: "any event beyond the reasonable control of the parties." In relatively recent years, some contracts expressly included "epidemics," such as in the BIMCO Supplytime charter party forms.

Depending on the language of the clause, the COVID-19 virus itself may not necessarily be considered a FM event. The FM landscape may change in light of the declaration of COVID-19 as a "pandemic" by the World Health Organization (WHO) and the ensuing actions taken by governmental entities to contain the spread of the virus, which have a trickle-down effect on a business's ability to perform its contractual obligations. Courts may view governmental action taken to combat the virus as the FM event as opposed to COVID-19.

While the interpretation of the impact of a pandemic on FM clauses may be a novel issue, there are limits to the reach of a FM clause. Courts have held that generalized economic hardship or increased expenses do not constitute a FM event.

Conclusion

It is key to review all FM clauses in contracts. Before triggering the clause, the non-performing party must read the language in the contract carefully. In the COVID-19 context, key language to look for would be references to "epidemics," "pandemics", "infectious diseases," "quarantines," or the catchall phrase of "any event beyond the reasonable control of the parties."

If a FM clause is applicable,

- make sure the event fits within the FM clause,
- remember to give proper notice of a FM event (if the contract requires it), and
- make reasonable efforts to avoid the loss
- consider engaging with contractual partners to find amicable solutions to the disruptions caused by COVID-19.

FM scenarios are highly fact specific, and the application of a FM clause carries significant commercial impacts. In this highly fluid time, HFW is committed to assist our clients with the commercial and legal impact of COVID-19. For an English law FM perspective, click on the attached link for an article by HFW Partner Brian Perrott. https://www.hfw.com/Coronavirus-Can-it-be-a-Force-Majeure-event-Feb-2020 and our dedicated COVID-19 Hub https://www.hfw.com/Covid-19, designed to prepare you for what's next. The HFW global team will continue to monitor the legal and business implications and report on further developments

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