HOT TOPIC

# COVID-19, *Force Majeure* and the Impossibility of Performance: US and UK Perspectives



**Tom Canning**
*Partner*
tcanning@milbank.com
+44 20.7615.3047


**Jacqueline Chan**
*Partner*
jchan@milbank.com
+65 6428.2433


**William Charles**
*Partner*
wcharles@milbank.com
+44 20.7615.3076


**Aled Davies**
*Partner*
adavies@milbank.com
+81 3.5410.2851


**Allan Marks**
*Partner*
atmarks@milbank.com
+1 424.386.4376


**Daniel Perry**
*Partner*
dperry@milbank.com
+1 212.530.5083


**Jed Schwartz**
*Partner*
jschwartz@milbank.com
+1 212.530.5283


**Nicholas Smith**
*Partner*
nsmith@milbank.com
+1 202.835.7522


**Justen Fleming**
*Special Counsel*
jfleming@milbank.com
+81 3.5410.2852


**Brenton Culpepper**
*Associate*
bculpepper@milbank.com
+1 212.530.5626


**Dan Hooks**
*Associate*
dhooks1@milbank.com
+1 212.530.5541


**Vasiliki Katsarou**
*Associate*
vkatsarou@milbank.com
+44 20.7615.3282


**Joseph Richmond**
*Associate*
jrichmond@milbank.com
+65 6428.2578


In managing the volatility and uncertainty caused by the COVID-19 pandemic, industries have continued to grapple with complex legal and commercial challenges, from manufacturing shutdowns, interrupted supply chains and quarantines, to dislocated labor markets and restrictions on trade and movement, including the practical shutdown, or near shutdown, of substantial portions of the world economy.

Moreover, governments have intervened to provide liquidity and emergency relief to credit markets and vulnerable industries and to preserve payrolls. Nonetheless, pandemic-induced economic uncertainty has led many companies, lenders and investors to seek guidance on their rights with respect to contractual obligations, especially in the key area of *force majeure* provisions.

> **"Force majeure seeks to protect parties to a contract from being held to performance obligations which, due to events outside of their own control and expectation, they cannot fulfill."**

## FORCE MAJEURE IN THE UNITED STATES

The concept of *force majeure* seeks to protect parties to a contract from being held to performance obligations which, due to events outside of their own control and expectation, they cannot fulfill. An assessment of a party's right to invoke a *force majeure* clause requires a review of the contract at issue. However, *force majeure* clauses are interpreted narrowly and often are difficult to invoke.

Courts generally assess the following criteria when assessing a party's reliance on *force majeure*: (i) whether the event is force majeure under the contract; (ii) whether nonperformance was foreseeable and could be mitigated; and (iii) whether performance is impossible. Courts narrowly apply *force majeure* to the events enumerated in the contract. *Force majeure* clauses often list the specific events (e.g., floods, fires, and earthquakes) and/or categories of events (e.g., natural disasters, terrorism, and government actions) that can potentially excuse performance under the contract.

Even if the event giving rise to nonperformance is within the scope of the *force majeure* clause, a party generally must also demonstrate that (i) the event was unforeseeable, and nonperformance could not be mitigated, and (ii) performance is impossible, not simply economically challenging.

## FORCE MAJEURE CLAUSES

As with all contractual disputes, courts generally begin their analysis of *force majeure* clauses by looking at the terms of the agreement and the intent of the drafting parties. Courts construe *force majeure* clauses narrowly and will generally only excuse a party's nonperformance if the event that caused the party's nonperformance is specifically enumerated. When an event is not specifically enumerated in the *force majeure* clause, but there is a general catchall provision in the clause, the catchall provision is "not to be given expansive meaning." Instead, it is "confined to those things of the same kind or nature as the particular matters mentioned." Generally, courts also require that the event must be unforeseeable.

Even if an event in question fits within the delineated events that could potentially excuse performance under the *force majeure* clause, the nonperforming party still must establish that the event in question actually prevented, hindered and/or delayed its performance under


the contract. *Force majeure* clauses often contain provisions requiring parties to exercise reasonable diligence to avoid or overcome the *force majeure* event and its consequences, failing which performance will not be excused under the *force majeure* clause. But even in the absence of such provisions, New York courts appear to still require parties to make such a showing. Other jurisdictions, including Texas, have held that such a showing need only be made when expressly required by the *force majeure* clause.

## COVID-19 AND THE SCOPE OF FORCE MAJEURE

Whether COVID-19 or the governmental actions taken to contain COVID-19 are within the scope of a *force majeure* clause depends on whether those events are listed or are of the same type of events listed in the clause. Courts construe *force majeure* clauses narrowly and will generally only excuse a party's nonperformance if the event that caused the party's nonperformance is specifically enumerated. When an event is not specifically enumerated in the *force majeure* clause, but there is a general catch-all provision in the clause, the catch-all provision is "not to be given expansive meaning." Instead, it is "confined to those things of the same kind or nature as the particular matters mentioned." For example, a *force majeure* clause listing floods, fires, and earthquakes likely would not include COVID-19 because disease and government action are not expressly listed. However, a *force majeure* clause listing natural disasters, terrorism, and government actions may include the government action taken to contain COVID-19, but likely would not include COVID-19 itself.

## CONTRACTS WITHOUT A FORCE MAJEURE CLAUSE

Courts are likely to refuse a party's *force majeure* claim if the underlying contract does not include a *force majeure* clause. In such a circumstance, a party may look to common law tools to excuse nonperformance, such as the doctrines of impossibility and, where available, impracticability.

## ECONOMIC HARDSHIP AND FORCE MAJEURE

Economic hardship does not generally provide enough basis to exercise *force majeure*. Absent express contractual provisions to the contrary, economic factors or financial hardships generally do not constitute *force majeure* events that excuse performance under a contract. However, the specific terms of the contract at issue and jurisdiction governing their interpretation may provide a basis for considering economic hardship when exercising *force majeure*.

## OVERCOMING A FORESEEABILITY REQUIREMENT IN POST-COVID-19 CONTRACTS

A party exercising a *force majeure* claim generally must establish that the event giving rise to nonperformance was unforeseeable, depending on jurisdiction. If COVID-19 is the event giving rise to nonperformance, a party likely will face difficulty in excusing performance pursuant to a *force majeure* clause if the contract was executed after the World Health Organization declared COVID-19 a pandemic because COVID-19 would be deemed a foreseeable risk. On the other hand, because the COVID-19 situation has continually changed over the course of the year, as has the response of different national, state, and local governments, a party may be able to argue that the particular consequence of these responses was not foreseeable.

## FORCE MAJEURE IN THE UNITED KINGDOM

The concept of *force majeure*, a civil law derived term, has no universally applicable meaning under English law. Rather, it is to be assessed on a contract by contract basis, applying normal principles of contractual interpretation/construction.

A customary *force majeure* clause in a contract will provide contractual relief to a party affected by an event or circumstance which: (i) is beyond the reasonable control of the affected party; (ii) is not the result of any act, omission or delay of the affected party; (iii) could not have been reasonably foreseen, avoided, or reduced by the exercise of reasonable measures; and (iv) causes or results in that party not being able to perform its obligations (other than the obligation to pay money) under the contract. The contract will also typically have a non-exhaustive list of events or circumstances that would constitute a *force majeure* event (provided that the above general conditions are satisfied) such as acts of nature (sometimes referred to as acts of God, such as earthquakes, tsunami and epidemics), acts of man (such as war, industrial action, piracy, riot and sabotage) and governmental action (such as change in law, regulations and expropriation). "Disease" or "epidemic" are frequently listed as one of the specific events or circumstances that may constitute *force majeure* (as long as the general requirements of the *force majeure* provision are satisfied), or the COVID-19 outbreak may be caught by a more general term such as "act of God," or simply as an event or circumstance beyond the affected party's reasonable control.

Although this list of events or circumstances is neither exhaustive nor conclusive, it should be noted that the principle of ejusdem generis often operates to narrow construction of such a clause when a party is trying to argue that an additional, unlisted event falls within the definition.

## MAKING A FORCE MAJEURE CLAIM

To make its claim, the affected party would need to establish that the outbreak is contemplated as a *force majeure* event as an "epidemic" or an "act of God" or, if relevant, that the restrictions placed upon companies and citizens by a government in order to help contain the outbreak, are contemplated by the *force majeure* definition as "governmental action."

Some issues that may be encountered are:

- (i) whether the outbreak could have been reasonably foreseen given the precedents for other major epidemics impacting global supplies, including the unrelated SARS outbreak in 2003;
- (ii) where the affected party may not have been directly impacted by the outbreak but rather impacted by the subsequent governmental action to contain the outbreak. In this case, the affected party would have to show that governmental action (for which the contractual relief may differ relative to an act of God *force majeure*) constitutes a *force majeure* event;
- and (iii) where the affected party is not directly affected by the outbreak but yet is unable to perform an obligation under its contract (the affected contract) because its supplier is claiming *force majeure* due to the outbreak. In this case, the affected party will need to show that the supplier's claim for *force majeure* meets the standards under the affected contract, and that the affected contract expressly allows a *force majeure* claim when the affected party's performance is impacted by a *force majeure* event somewhere else along the supply chain. This is often referred to as 'chain *force majeure*.'

It is worth noting in this regard that the English courts have held that a failure of performance due to the provision of insufficient financial resources, or loss of market due to the event, is unlikely to amount to *force majeure*. Accordingly, a change in economic/market circumstances due to the outbreak affecting the profitability of a contract or the ease with which the parties' obligations can be performed, is perhaps unlikely to be regarded as being a *force majeure* event.

*To read more about force majeure and the COVID-19 pandemic from the US law perspective click here, and from the English law perspective click here.*