Coronavirus on Commercial Contracts: Will Force Majeure Clauses Offer Protection?

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As the infection rates and global death toll from the coronavirus (COVID-19) continue to rise, the economic impact and repercussions to the global economy are becoming more pervasive. The effects of the recently-declared pandemic have already hit hard, with nearly 75% of U.S. companies reporting supply chain disruptions. A Dun & Bradstreet whitepaper reported that more than 90% of all companies globally with Tier 1 (direct) suppliers in impacted regions were headquartered in the U.S. Additionally, the paper found that at least 51,000 companies worldwide have one or more Tier 1 suppliers in impacted regions, while at least 5 million companies have one or more Tier 2 suppliers in impacted regions.

Businesses are experiencing significant disruptions in their supply chain with shortages of staff and supplies, delays in production, and restrictions on the transport of products. Such disruptions raise the inevitable fate that many suppliers, manufacturers, distributors, and vendors may be unable to fulfill pre-existing contractual obligations. Whether businesses may be able to avert disastrous financial losses may depend on the fine print contained in many contracts: a *force majeure* clause. A *force majeure* provision in a contract excuses parties from performing their contractual obligations when unforeseen circumstances beyond their control make performance commercially impracticable or impossible.

The language of the *force majeure* clause is essential. Boilerplate provisions often cover natural disasters, fires, "acts of God", war, threats of terrorism, civil disorder or disturbance, labor strikes, and acts of government. Some provisions contain 'disease' and 'epidemic' as covered events. Other *force majeure* clauses have broad catch-all provisions, such as "any other circumstance beyond the reasonable control of the Parties." Courts tend to interpret *force majeure* clauses narrowly, enforcing the provision only for those conditions specified therein. For those companies whose *force majeure* clauses cover disease and epidemic, coronavirus will almost certainly fall under those categories. Broader phrases like "acts of government" could be argued as applicable to circumstances where mandatory quarantines or limitations on activity have been ordered and are the cause of the party's inability to perform. Once a determination has been made as to whether coronavirus is a triggering event, the remainder of the clause's

language must be carefully examined.

Interestingly, the World Health Organization has stated that, "the likelihood of an infected person contaminating commercial goods is low and the risk of catching the virus that causes COVID-19 from a package that has been moved, travelled, and exposed to different conditions and temperature is also low." For businesses engaged in logistics and supply chain operations, the disease itself may not be a triggering event, but a reduction in workforce may. In circumstances where company-wide quarantines are implemented for social protective measures, assertion of the *force majeure* clause may not apply as qualifying under the condition of "disease." Thus, it is essential that the language of the clause be closely examined.

Some clauses excuse the nonperforming party from all liability as a result of the *force majeure* event, while other clauses hold the party liable for any expenses incurred as a result of its nonperformance. Another important consideration is whether there are conditional requirements to the *force majeure* clause. Some clauses may require that notice be given to a counter party advising of any anticipated noncompliance within a certain time frame. Failure to provide any required notice could constitute as a breach of the agreement, or may hinder party's entitlement to seek *force majeure* relief. Other considerations may include whether the contract provides for exclusivity. If a party is unable to perform its obligations under an exclusive supply contract, can the non-impacted party purchase goods from an outside vendor? In such a case, the non-impacted party should ensure that it may do so without being potentially liable for breach.

If a contract does not have a *force majeure* clause, businesses may still find protection under the Uniform Commercial Code (UCC). Section 2-615 of the UCC protects a seller's delay in performing or non-performance where delivery is "impracticable." A delay in delivery or non-delivery, in whole or in part, will not be considered a breach of seller's duty under a contract for sale if performance has been made impracticable due to either (1) the occurrence of an event, the non-occurrence of which was a basic assumption underlying the contract, or (2) compliance, in good faith, with any applicable foreign or domestic governmental regulation or order. Under the UCC, the seller whose performance has been impaired must provide reasonable notice to the buyer of the delay or non-delivery.

It is important to note that increased costs alone do not excuse performance. Comment 4 to UCC 2-615 provides that, "increased cost alone does not excuse performance unless the risk in cost is due to some unforeseen contingency which alters the essential nature of the performance. Neither is a rise or collapse in the market itself a justification, for that is exactly the type of business risk which business contracts made at fixed prices are intended to cover. Additionally, where an unforeseen event renders a seller's continued performance contingent upon seller incurring additional burden or expense (e.g., increased transportation costs to transport goods), the seller is required to cover and meet

its contractual obligations notwithstanding the higher costs. Where the impracticability affects only a part of the seller's capacity to perform, he must allocate production and deliveries among his customers, and may do so in any manner that is fair and reasonable.

While the UCC does provide some relief to sellers, its protection is not absolute. Thus, having a well-drafted *force majeure* clause will become increasingly important. As the global reach of the coronavirus continues to expand and its effects reverberate, the commercial impracticability considered by *force majeure* clauses and the UCC may become easier to invoke. Concerned businesses should carefully assess its contractual provisions and seek legal counsel when impracticability of performance arises.