

CLIENT ALERT

Business Disruption in a Pandemic: Termination or Suspension of Contract Performance?

Apr.27.2020

Many businesses have issued notices to and/or received notices from a contracting party invoking force majeure, or a similar doctrine to excuse non-performance, based on a COVID-19 related business disruption. However, it is not always clear that the party issuing the notice is permitted to either suspend performance or terminate the contract because of a force majeure event.

It is important to know whether the business disruption may result in suspension or termination in your circumstances (and if the former, for how long), since this will likely affect substitution and supply considerations, as well as your response to the notice.

Below are guidelines to consider in assessing whether a contract can be completely terminated in the event of force majeure, or whether the contract only permits performance to be suspended temporarily, and how to determine when and how suspended performance should resume once the force majeure event ends.

1. Review the contract.

A force majeure clause may explicitly spell out the consequences of triggering force majeure. For example, the clause may allow for:

- **Immediate termination:** “Either party may terminate this Agreement in its entirety, and without liability, due to Force Majeure . . .”
- **Suspension:** “In the event that any party is prevented, interrupted, or delayed in the performance of its obligations hereunder . . . said party shall be excused from the performance of its obligations hereunder, but only while and to the extent that it is actually so prevented, interrupted, and/or delayed.”
- **Immediate termination or suspension:** “The Party subject to the Force Majeure Event shall not be liable to the other Party for any damages arising out of or relating to the suspension or termination of any of its obligations or duties under this Agreement by reason of the occurrence of a Force Majeure Event. . .”
- **Suspension followed by possible termination:** “Each Party shall be excused from liability for the failure or delay in performance of any obligation under this Agreement by reason of any Force Majeure event . . . should the event(s) of force majeure suffered by a Party extend beyond a four-month period, the other Party may then terminate this Agreement by written notice to the non-performing Party . . .”

Generally, courts will enforce the terms of the contract and construe the force majeure clause narrowly. If the clause provides for termination and does not mention suspension, then the contract likely will be terminated, with no option to resume performance after the force majeure event ends (absent renegotiation).

However, even if the force majeure clause only allows for suspension, courts in some jurisdictions may allow a party to rescind the contract (*i.e.*, cancel the contract and restore the parties to the positions they were in before the contract, to the extent possible) if a contract's purpose has been wholly frustrated. Frustration of purpose may be invoked when the fundamental reason for the contract has been frustrated by an unanticipated event beyond the parties' control.

2. Check governing law.

In the absence of a force majeure clause, a party may be permitted to suspend performance or terminate the contract based on the doctrines of frustration of purpose, impossibility, or impracticability. In most jurisdictions, either delay in performance or complete termination may result from invoking these doctrines, depending on the circumstances surrounding the business interruption.

If the contract is one for the sale of goods, the Uniform Commercial Code (U.C.C.) provides a buyer with two options after receipt of a seller's notice of material or indefinite delay due to impracticability: either: (1) terminate and discharge any unexecuted portion of the contract; or (2) modify the contract by agreeing to take the available quota in substitution. If the buyer fails to modify the contract within a reasonable time not exceeding 30 days after receipt of the notification, the contract lapses with respect to any deliveries affected.

3. Review the notice.

The notice from the party invoking force majeure, impossibility or frustration of purpose may provide insight on whether that party intends to suspend or terminate the contract and, if the former, when the party expects to resume performance. For example, a notice that states that the invoking party anticipates a two-month delay in performance and plans to provide periodic updates on the situation indicates the party likely intends to resume performance, not terminate the contract.

You should review the notice, paying particular attention to whether the relief sought comports with the contract's terms. In your response letter, you can object to any inconsistencies with the contract's terms, request any necessary clarification, and/or outline your revised expectations for performance, including as to timing of future performance.

4. Consider how long suspension may be permitted.

There often will be ambiguity as to how long non-performance can be excused in cases of suspended performance. Also, in some cases, suspension may eventually lead to contract termination, even if the force majeure clause does not expressly allow for termination; for example, if the contract term ends during the force majeure period.

Courts generally require the non-performing party to seek reasonable ways to limit the scope or duration of its non-performance. Whether the non-performing party has made sufficient efforts will be a very fact-specific inquiry. Both parties should keep records regarding efforts to resume performance in case a dispute about those efforts arises. A party may be in breach of contract if it fails to resume performance after the force majeure effects have ended.

5. Consider what happens when the parties resume performance.

Contracting parties should also review their contract terms to determine whether non-performance during the force majeure period must be made up after the force majeure period has ended and how the force majeure period affects the contract term.

Where the contract terms are ambiguous or conflicting, courts construe the relevant terms in light of the entire contract and consider the parties' intentions and purpose of the contract. For example, if a supply agreement requires monthly deliveries over a set period of time, the buyer may not be required to accept late makeup deliveries under the theory that requiring the buyer to do so is contrary to the purpose of the contract—to ensure that the buyer has a steady supply of goods.

The contract term is generally not extended by force majeure unless the contract provides otherwise, because courts recognize and give effect to the parties' intention to limit a contract to a set timeframe. Parties, however, can extend the term of the contract by renegotiation.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

John L. Murino

Partner – Washington, D.C.
Phone: +1 202.624.2663
Email: jmurino@crowell.com

Luke van Houwelingen

Partner – Washington, D.C.
Phone: +1 202.624.2583
Email: lvanhouwelingen@crowell.com

Emily Alban

Counsel – Washington, D.C.
Phone: +1 202.624.2718
Email: ealban@crowell.com