

CLIENT ALERT

Business Disruption and Commercial Contracts (Part 2): What Is The Actual Cause Of The Disruption?

April 1, 2020

Force majeure and related doctrines may allow a contracting party to suspend or terminate performance when certain unforeseeable events that are beyond the control of the parties occur, such as a global pandemic or government action or prohibition. However, the mere existence of a force majeure clause and qualifying event may not excuse non-performance if that event is not the *actual* cause of the business disruption.

Review your contract and the considerations below for a preliminary assessment as to whether the cause of your business disruption may be covered by your contract's force majeure clause.

1. How do you determine the cause of the disruption or non-performance?

While it may seem obvious that COVID-19 is the reason for many business disruptions, in some cases the actual cause of the business disruption is an effect of the pandemic rather than the pandemic itself. For example, business disruptions may be caused by the following effects of the pandemic:

- Government-forced closures in response to COVID-19
- Self-imposed company closures, without government order, due to general COVID-19 safety concerns
- Lack of access to machinery
- Worker shortages due to illness
- Decline in consumer demand
- Supply shortages due to heightened demand caused by COVID-19

Consider the direct cause of your business disruption and whether it is the pandemic itself or an effect of the pandemic. Some effects of the pandemic are sufficient to invoke force majeure and some are not. This depends, in part, on the specific language in your contract.

2. Does the force majeure clause cover the cause of the disruption?

Courts in most jurisdictions construe force majeure clauses narrowly, such that only events specifically listed in the clause may excuse non-performance – particularly where the event was foreseeable.¹¹ This is especially true where the event relied upon is not one that would traditionally give rise to an impossibility defense, such as decline in demand or other changes in market conditions.

Examples of specific contract language that may cover business disruptions caused by COVID-19 include:

- Public health-related language (e.g., “. . . by reason of flu, epidemic, pandemic, serious illness or plagues, disease, emergency or outbreak. . .”)
- Government action-related language (e.g., “. . . by reason of restrictive governmental laws or regulations. . .”)

If the claimed force majeure event is too attenuated from the reason for non-performance, non-performance may not be excused. For example, courts have held that a force majeure clause that covers a specific event does not excuse non-performance due to worsening economic conditions resulting from that event. At the far end of the spectrum, force majeure will not cover the buyer’s desire to allocate funds for other operations, even if they are needed because of the event. So, even if your force majeure clause specifically covers a pandemic, you need to analyze the proximate cause of the excuse for non-performance.

Force majeure clauses that expressly encompass both direct and indirect results of the force majeure event may cover a broader range of circumstances.

Examples of such language include:

- “. . . directly or indirectly arising out of . . .”
- “. . . whether caused directly or indirectly . . .”

3. Does the force majeure event render performance impossible or simply more difficult?

The party invoking the force majeure clause will also need to demonstrate impossibility or, in some jurisdictions, excessive and unreasonable difficulty, expense, injury, or loss. Most force majeure clauses contain explicit language capturing this element, requiring that the event “prevent or delay” a party’s performance.

While the threshold for impossibility or impracticability differs by jurisdiction, courts generally will not excuse performance that is simply more costly or less profitable due to the occurrence of the force majeure event. Consider whether the business disruption could have been avoided or mitigated by use of alternate available options or additional expenses or resources.

* * *

The cause of a business disruption may not be as clear-cut as it seems at first glance. The above considerations will help you determine the actual cause of a business disruption, and whether it may be covered by your force majeure clause.

¹ However, if the event is not specifically listed in your force majeure clause, it may still be covered by a catch-all provision. See [further discussion on foreseeability and catch-all provisions here](#).

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

Bryan Brewer

Partner – Washington, D.C.

Phone: +1 202.624.2605

Email: bbrewer@crowell.com

Mark A. Klapow

Partner – Washington, D.C.

Phone: +1 202.624.2975

Email: mklapow@crowell.com

John L. Murino

Partner – Washington, D.C.

Phone: +1 202.624.2663

Email: jmurino@crowell.com