

CLIENT ALERT

Business Disruption in a Pandemic: Does COVID-19 Excuse Non-Performance of a Contract?

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COVID-19 is rapidly evolving and has disrupted and will continue disrupting business operations in many important ways. But does it activate force majeure clauses in your contracts? The answer is, of course, it all depends. Watch this space for further guidance, as we are starting a series on contract disputes related to the COVID-19 pandemic.

The following five steps should serve as a starting point to evaluate the efficacy of a force majeure clause in the face of a global pandemic. Ultimately, this question is likely to be a complex, nuanced and highly fact-specific inquiry based on the specific terms and conditions of the contract, governing law, the factual circumstances, and other factors.

In conducting the following five step analysis it is important to understand whether your company will seek to use the force majeure provision to avoid an obligation under the contract or whether the other party to the contract will seek to use the force majeure provision as a defense to your company's attempt to enforce a right under the contract.

1. What does the clause actually say?

Not all force majeure clauses are the same – not even close. Thus, the very first step in your analysis should be to read the clause. Your clause may exclude certain types of situations, like unprofitability. Your clause may specifically include a pandemic or infectious disease as a force majeure event. Your clause may be drafted to provide only limited events are force majeure events and thus the clause likely will be interpreted narrowly. The exact wording matters a great deal.

2. What is the cause of the disruption?

You need to ask yourself if the pandemic has created the disruption, or if there may be an intervening factor, such as a third party's response to the pandemic, that is the cause of the disruption. Potential reasons for a disruption may include the following:

- An aspect of the COVID-19 disease itself
- Government action or prohibition in response to COVID-19 (*e.g.*, many states have limited business operations to essential business only) renders performance of the contract unlawful or impossible
- Shortage of labor, due to illness or quarantine or some other COVID-19-related cause, renders performance of the contract impossible
- Significant decline in demand or material drop in potential profitability of the business metrics supporting the agreement due to COVID-19 or related events
- Cancellation of an event obviates the need for performance of the contract (*e.g.*, event marketing and advertising)
- Curtailment of transportation modalities or facilities
- Shortage of supply and/or raw materials required to perform under the agreement

Force majeure may or may not apply in each situation.

3. What is the governing law?

If your contract does not include a force majeure clause, you will need to consider the law governing the interpretation of the contract. Does the pandemic or a government action in response to this type of force majeure event, render contract performance impossible, impracticable, or radically different from what was contemplated when entering into the contract?

Each jurisdiction has different predispositions about force majeure. Some jurisdictions may imply those terms into contracts even if there is no such clause. Other jurisdictions may interpret those clauses narrowly. And most jurisdictions will have an incomplete body of case law about what the clause means in specific situations, including during a national medical crisis. Not to mention jurisdictions outside the United States bring a variety of different standards and even statutes applicable to these situations.

4. What steps should or must we take to protect ourselves?

Is there a notice requirement? What about timing? Importantly, consider how any writing reflecting the problem may later be characterized given the actual words of the clause and the governing law. Think strategically about the operational needs and legal risks and possibilities that the business faces. Consider how the arguments you are making in this dispute could impact other corporate disputes, including those in which the roles may be reversed. Be sure to collect documentation relied upon and keep correspondence and emails between the parties.

5. What rights do we have given the other parties' actions?

Can we stop performance ourselves? The occurrence of a force majeure event may or may not be, in and of itself, sufficient to excuse non-performance. Whether or not non-performance is excused will depend on a careful reading of the clause itself and an analysis of the applicable law. Can we sue in court for damages or to secure a right to performance or non-performance? Again, possibly. Some contracts require a dispute resolution procedure before going to court. Some contracts require mediation. Some contracts call for binding arbitration in a particular forum instead of in court litigation.

This is obviously just the start of the analysis. Please watch this space for continued guidance.

Also, please see our checklist for force majeure in corporate contracts [here](#).

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

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

Emily Alban

Counsel – Washington, D.C.

Phone: +1 202.624.2718

Email: ealban@crowell.com