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Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Crafting Robust Force Majeure Clauses

By **Alan Howard and Luke van Houwelingen** (March 26, 2018, 2:31 PM EDT)

Alan Howard

Luke van Houwelingen

After a recent deadly 7.5 magnitude earthquake hit Papua New Guinea, ExxonMobil Corp. shut down a local natural gas facility out of concern that critical field infrastructure and a pipeline were damaged. Amid uncertainty about when the $19 billion liquid natural gas facility might be able to reopen, it has been reported that Exxon declared force majeure in an attempt to protect the company from any liability due to its inability to fulfill supply obligations.

In December 2017, multinational chemicals company INEOS invoked force majeure on shipments of crude oil, natural gas and condensate after discovering a crack in one of its major pipelines in the North Sea, and last November, German chemical company BASF SE declared force majeure after a fire forced it to shut down a vitamin production facility. By invoking force majeure, these companies sought time to make necessary repairs without breaching their contractual obligations.

The traditional notion of a force majeure event is one that cannot be anticipated or controlled, such as a natural disaster, a terrorist attack or a similar unforeseen occurrence that prevents, either permanently or temporarily, standard business operations or the timely delivery of products and services. In such circumstances, a contract's force majeure clause may excuse the declaring party from its contractual obligations. Channeling this notion of force majeure, some lawyers adopt "boilerplate" language of an "Act of God" clause instead of tailoring force majeure provisions to their clients' actual risks.

A growing body of recent case law features decisions which turn on the precise force majeure language in the parties' contract, as a reflection of how the parties chose to allocate the risks associated with categories of events which could disrupt or defeat the purpose of the contract. Even the historical prerequisite of unforeseeability is no longer a constant, as parties specifically identify categories of events which they agree may constitute force majeure. They may expressly say that a force majeure event under the contract may be foreseeable or unforeseeable, and courts in some states also decline to read an unforeseeability requirement into a force majeure provision that is silent on the question.

A key aspect of force majeure clauses is the extent to which performance must be impeded to trigger their application. Unlike common-law doctrines which may be invoked to excuse performance, such as

impossibility of performance or commercial impracticability, a clearly articulated standard in a contractual clause avoids vague standards and inconsistent judicial applications which plague those doctrines.

The most common and most clear impairment standard is “prevent,” under which performance must actually be foreclosed. Under this standard, the ability to perform the contract, even at great expense, means that the excuse of force majeure is unavailable. Courts have even found that extreme economic impact which threatens a company with bankruptcy does not constitute force majeure if the party is physically able to perform. On the other hand, recent cases demonstrate that parties may specifically incorporate in their force majeure provision events or impairment standards which excuse performance when it merely would be overly expensive or unprofitable.

Absent such express language, the general rule is that changes in market conditions or economic hardship are insufficient to establish force majeure, even if they are the result of some unforeseen or uncontrollable event. For example, in the aftermath of the Sept. 11, 2001, terror attacks, Clear Channel Communications Inc. was sued for canceling a convention at the Outrigger Wailea Resort in Hawaii. While the events of Sept. 11 certainly were unforeseen, and the resulting travel concerns of prospective attendees which led to wholesale cancellations made the convention an economic nonstarter, performance of the contract for hotel rooms was not impossible. Performance had become only “economically inadvisable,” which did not constitute force majeure.

With this in mind, counsel must try and anticipate potential scenarios in which the parties’ performance and the cost of performance will be impacted, and carefully draft the contract to reflect the parties’ intent with respect to allocating those risks. This is true whether the client is the buyer or the seller of the goods or services governed by the contract. Scrutinizing the potential risk a company might face based on the nature of its particular industry should be the first step when drafting these clauses. Extreme weather events brought on by climate change, and factors like volatile markets and evolving government regulations, mean that explicit, comprehensive force majeure clauses may be ever more critical in protecting a contractual party.

Environmental regulations provide a good illustration. Some regulations, such as a ban on specific products, if adopted after contract execution, likely would constitute a force majeure event which prevents performance, and thus, performance by the party subject to the new regulation would be excused. On the other hand, other regulations, such as more stringent emissions standards, do not physically prevent performance but merely make performance more expensive. Under traditional notions of force majeure, as well as standard force majeure clauses, these regulations would not excuse performance by the impacted party. The party that must comply with the regulations assumes the risk that these regulations will change.

Understanding this, it is incumbent on a party which may be impacted by future changes to regulations affecting its business to anticipate, and try to protect itself against, such changes. For example, a contract may provide that in the event of specified changes in environmental regulations which materially increase the cost of a party’s performance or even make performance impracticable, that party will have the option to decline future performance. There would likely be a cost for such protection, but this is precisely the type of negotiation and risk allocation that is necessary.

Lawyers can help protect their clients by avoiding the default of standard force majeure text, and spelling out the intent of the parties in unambiguous terms. While it is impossible to anticipate and

address all contingencies, lawyers can best serve their clients by using clearly defined and precise language to mitigate performance and even economic risks.

Alan Howard is a partner in Crowell & Moring LLP's New York office, where his practice focuses on litigation and arbitration matters domestically and internationally. Luke van Houwelingen is counsel in Crowell & Moring's Washington office, where he practices in the antitrust group.