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COVID-19 and Understanding Your Force Majeure Clauses.

The China Council for the Promotion of International Trade has currently issued at least 4,811 force majeure certificates due to the COVID-19 pandemic. These certificates qualify the coronavirus outbreak as a force majeure event and certify that a party's partial performance or failure to perform under an agreement be excused if there is a force majeure clause in the agreement. According to a Xinhua state media report, the total contract value for the agreements associated with the certificates is an alarming 373.7 billion Chinese yuan (equivalent to US$53.79 billion). Unfortunately, for many U.S. businesses impacted by the economic hardships caused by COVID-19, these force majeure certificates will be of little use if their contracts are governed by U.S. law. Companies should understand the impact and application of their existing force majeure clauses to COVID-19.

A typical force majeure clause releases obligations and liability if an extraordinary event occurs. These events are usually limited to events like war, fire, natural disasters, civil disorder, strikes or labor disputes, acts of God or other circumstances beyond a party's reasonable control. When these unanticipated circumstances arise, the force majeure clause may be invoked to relieve the parties from their contractual obligations or to terminate the contract with no further liability from either party.

Far too often, force majeure clauses are an afterthought during the contract negotiation process. Although seemingly unimportant when the parties are trying to close a deal, these clauses have substantive impacts to the business when unanticipated events occur. As the spread of COVID-19 disrupts global supply chains and results in the imposition of emergency rules and regulations, it becomes imperative for companies to prepare themselves for impending commercial disputes.

As a historical example, the SARS virus outbreak in 2003 resulted in many companies asserting force majeure clauses. Northwest Airlines famously relied on the force majeure clause in its labor contracts to lay off employees without notice, asserting that the SARS virus caused its air traffic to Asia to significantly decline. Not surprisingly, the Aircraft Mechanics Fraternal Association, an independent aviation union, claimed the layoffs were an immoral exploitation of the provision and challenged Northwest Airlines' legal justification by filing a class-action grievance. The arbitration board held that while a number of the layoffs were justified by force majeure events, a certain subset of mechanics were unjustifiably laid off, and Northwest Airlines was ordered to rehire those mechanics. The takeaway from this is that a force majeure clause may not apply uniformly to different circumstances.

While the SARS virus resulted in many companies revising the force majeure clauses in their contracts to include "global epidemics" as triggering events, the Northwest Airlines example shows that COVID-19 should be carefully analyzed in its specific impact to different industries. In addition, other contract provisions will alter the legal analysis about whether a specific force majeure clause can be invoked. For example, certain jurisdictions may interpret "acts of God" or "epidemic" differently, so the governing law provision will have an effect on whether the force majeure clause may be invoked. Moreover, force majeure clauses are drafted with specific terms that impact their interpretation. For example, a force majeure clause that does not specifically cite "disease" or

“epidemics” may nonetheless have an all-inclusive catch-all phrase (such as “any similar event beyond the reasonable control of a party”) that would lead to the COVID-19 pandemic qualifying as a force majeure event.

Just as companies must take a proactive approach to their employees’ health and safety with respect to COVID-19, companies should also take a proactive approach to the other business effects of COVID-19. If a company’s obligations have been affected by COVID-19 in any capacity, the company should consider certain practices in anticipation of any disputes and to prepare for the possible invocation of a force majeure clause, including, but not limited to the following:

- keeping detailed records of COVID-19’s impact on its business functions and on any inability to perform the company’s contractual duties;
- documenting COVID-19’s impact on the company’s supply chains, such as its vendor’s inability to secure raw materials, parts, components, or disruption to the capabilities of the vendor’s suppliers or independent distributors;
  continuously evaluating the current events of COVID-19 and how the incident is affecting governments and the company’s industry. The situation is changing day-by-day, and keeping abreast of the current events will allow the company to quickly reassess its obligations and liabilities;
- reviewing both existing customer agreements and vendor agreements, to analyze the legal obligations and liabilities of all parties under the agreements. Force majeure clauses are each drafted differently and should be interpreted by legal counsel. Companies should also keep in mind notice provisions within its agreements, so that it does not inadvertently run afoul of its obligations to notify the other party; and
- reviewing insurance coverages and whether the company’s current insurance covers business interruption related to COVID-19.

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