

## Force Majeure and the Coronavirus (COVID-19)

Alert

03.12.2020

By Susan Warshaw Ebner, Christina Arnone, Zane Gilmer, Sharon Markowitz, Christy Milliken and Hailey Perkins

Generally speaking, entities that enter into contracts are bound to perform them. However, as matters evolve, the impacts of natural and man-made problems arising from the coronavirus (COVID-19) are being felt by customers, their contractors, and suppliers. Who bears the costs of such impacts and are there possible defenses or routes to recovery of costs? Force majeure provisions may prove to be a sword and a shield for addressing such impacts.

### I. “Force Majeure” Concept and Provisions

The concept of “force majeure” is that a party’s performance of its contractual obligations may be excused where performance is prevented or frustrated due to an unusual event that is beyond the contracting parties’ control. However, force majeure clauses come in different shapes and sizes. Depending on how they are drafted, they may excuse for nonperformance where a set threshold has been exceeded or in only a limited set of circumstances.

#### A. Commercial contracts

Commercial contracts may contain general or customized force majeure clauses that broaden or restrict the types of triggering events and mitigation that may excuse performance. For example, the majority of force majeure clauses include triggering events caused by an “act of God.” An “act of God” is commonly defined as “[a]n overwhelming, unpreventable event caused exclusively by forces of nature, such as an earthquake, flood, or tornado. The definition has been statutorily broadened to include all natural phenomena that are exceptional, inevitable, and irresistible, the effects of which could not be prevented or avoided by the exercise of due care or foresight.” ACT OF GOD, Black’s Law Dictionary (11th ed. 2019) citing 42 U.S.C. § 9601(1). However, an individual force majeure clause may specify additional factors that,

## Force Majeure and the Coronavirus (COVID-19)

if present, will excuse contractual obligations, such as government regulations, war, disasters, strikes, civil disorders, and acts of terrorism or other similar emergencies. The bottom line is that force majeure clauses often vary and the language must be evaluated to determine if a party can rely on it to excuse nonperformance.

### B. Government Contracts

Federal government contracts also may contain force majeure provisions that excuse a contractor's nonperformance where it is caused by an occurrence beyond the contractor's "reasonable control" and without its "fault or negligence." For example, FAR 52.212-4 Contract Terms and Conditions – Commercial Items provides:

a. Excusable delays. The Contractor shall be liable for default unless nonperformance is caused by an occurrence beyond the reasonable control of the Contractor and without its fault or negligence such as, acts of God or the public enemy, acts of the Government in either its sovereign or contractual capacity, fires, floods, epidemics, quarantine restrictions, strikes, unusually severe weather, and delays of common carriers. The Contractor shall notify the Contracting Officer in writing as soon as it is reasonably possible after the commencement of any excusable delay, setting forth the full particulars in connection therewith, shall remedy such occurrence with all reasonable dispatch, and shall promptly give written notice to the Contracting Officer of the cessation of such occurrence. [Emphasis added.]

Similarly, FAR 52.249-8 Default (Fixed-Price Supply and Service) may excuse a contractor's nonperformance due to, inter alia, epidemics, quarantine restrictions, or freight embargoes and the contractor could not obtain the needed supplies or services from others in sufficient time to meet the contract schedule:

a. Except for **defaults** of **subcontractors** at any tier, the Contractor shall not be liable for any excess costs if the failure to perform the contract arises from causes beyond the control and without the fault or negligence of the Contractor. Examples of such causes include (1) acts of God or of the public enemy, (2) acts of the Government in either its sovereign or contractual capacity, (3) fires, (4) floods, (5) epidemics, (6) quarantine restrictions (7) strikes, (8) freight embargoes, and (9) unusually severe weather. In each instance, the failure to perform must be beyond the control and without the fault or negligence of the Contractor.

b. If the failure to perform is caused by the default of a subcontractor at any tier, and if the cause of the default is beyond the control of both the Contractor and subcontractor, and without the fault or negligence of either, the Contractor shall not be liable for any excess costs for failure to perform, unless the subcontracted **supplies** or services were obtainable from other sources in sufficient time for the Contractor to meet the required delivery schedule. [Emphasis added.]

## Force Majeure and the Coronavirus (COVID-19)

In addition to these established provisions, individual government contracts may include customized provisions that excuse specific types of force majeure events or delays.

Government contracts also may provide affirmative relief mechanisms where nonperformance, injury or damage arises in certain situations. For example, a government contract may be negotiated to include specific indemnification provisions that provide a vehicle for recovery where the contractor performs high-risk contracts and the potential for injury or damages is significant. See, e.g., FAR 52.249-14 Excusable Delays (Apr 1984); FAR 52.250-1 Indemnification Under Pub. L. No. 85-804 (Apr 1984).

### C. The Uniform Commercial Code (UCC)

Subject to definite terms and provisions in the contract, the UCC acts as a gap-filler and may provide guidance where situations arise under government contracts. Typically, force majeure clauses may limit a party's requirement to achieve substitute performance. Without a force majeure clause, UCC §§ 2-613 through 2-615 provide assistance in sales contracts that become impracticable due to no fault of either party. Section 2-613, for example, provides for the avoidance of a contract if goods suffer a total casualty through no fault of either party before the risk of loss passes to the buyer. Sections 2-614 and 2-615 contemplate avoidance of a contract due to commercial impracticability, which excuses nonperformance arising from circumstances beyond the nonperforming party's control.

Thus, depending on whether and to what extent your contract (or subcontract) contains force majeure or excusable delay provisions such as the above, you may be able to assert a defense to the assessment of damages or termination under your contract where your alleged nonperformance is beyond your control and without your fault or negligence.

Note that under the UCC (and under many commercial contracts), any shortfall due to the unexpected event must be allocated fairly amongst customers. And if a company fails to allocate the shortfall fairly, the company risks losing the entire defense of force majeure or impracticability. In a government contracts context, such a failure may also give rise to potential liability as an overpayment or False Claim. Thus, failing to allocate fairly can result in huge liability.

## II. Look Out for Potential Impacts and Workarounds

At present, the virus has been detected in 6 continents and over 100 countries, including the United States. COVID-19 has been classified by the World Health Organization as a "pandemic." There are over 100,000 confirmed cases and more than 4,000 deaths resulting from COVID-19. You should be planning for and alert to any actual or potential impacts arising from this emergency. Below are a few potential impacts to be thinking about:

# Force Majeure and the Coronavirus (COVID-19)

## A. Impacts due to illness in your workforce

The virus may be transmitted person to person through respiratory droplets even though infected persons do not appear to be ill. Given the apparent ease of transmission and the fact that the CDC does not identify a specific period of time when the infected person will remain contagious, companies should consider prompt and appropriate action to address the situation and avoid further contagion. Companies would be wise to track these events to determine whether and to what extent they will have sufficient workforce to carry on, as well as whether and to what extent they need to take additional steps to address or mitigate the situation. The severity of these types of events and the limits on your ability to overcome or mitigate them may trigger force majeure consideration.

## B. Impacts due to government direction

News reports reveal that governments at the federal, state and local levels are taking actions, inter alia, to try to limit the spread of the virus.

For example, a federal quarantine has gone into effect blocking the transit of persons into the United States – foreign nationals who have visited China or Iran within the past 14 days may not enter the United States; citizens and lawful permanent residents of the United States who have been to China or Iran in the past 14 days are being allowed back in to the United States but are being redirected to one of 11 airports to undergo health screening. Depending on the results of the screening, there will be some restrictions on their movements for a period of time.

States are also being impacted and [declaring states of emergency](#), including California, Colorado, Florida, Illinois, Kentucky, Maryland, New York, Utah, and Washington.

At the state and local levels, at least one state government now has taken action to create a [containment area](#) to prevent further spread of the virus. [Other state and local government actions](#) being considered and/or implemented include school closures for a period of time in a number of [areas](#), as well as restrictions on public events and movement. This type of “social distancing” is consistent with [White House guidance](#), and efforts proposed by the Centers for Disease Control.

Where the government prevents action or directs certain action, this may give rise to an impact to your business that you cannot avoid and which is beyond your fault or control.

## C. Impacts as a result of customer, higher-tier contractor, and supply chain actions

Disruptions in the supply chain may affect the ability of a company to obtain needed raw materials, supplies or services to meet its requirements.

## Force Majeure and the Coronavirus (COVID-19)

For example, quarantines in China to stem the tide of the virus' progression are impairing the delivery of supplies and services and are resulting in [shortages of raw](#) and finished materials and components used throughout the supply chain.

Closures or reduced workforces in lower-tier suppliers or services providers also may affect the availability of needed supplies or services for higher-tier contractors and end-customers. Particularly hard hit at this time is the electronics supply chain, where impacts of the virus are resulting in delays in production and delivery of computer and telecommunications equipment and components.

Within the United States, production and services delays are also being experienced. [Microsoft](#) has asked employees who can to work from home and agreed to pay vendor hourly service providers their regular pay during their period of reduced service needs. Manufacturers are considering options to work around these delays and unavailable parts. Companies are considering alternative places and methods to conduct their manufacturing, such as [trying to use 3D printed parts from local suppliers](#) instead of tooled parts that normally would come from China.

Whether and to what extent these impacts constitute force majeure events or sufficient efforts to mitigate so as to excuse any performance deficiencies will need to be assessed on a case by case basis. However, early identification of potential issues and impacts and timely efforts to consider and seek to address them will be important.

### III. Insurance Considerations

Businesses should carefully review their insurance policies to assess any applicable coverage for losses resulting from the coronavirus, including supply chain disruption, business interruption, property damage, and liability claims. Whether there is coverage for coronavirus-related losses will depend on the particular circumstances and the terms of the insurance policies.

While businesses often maintain business interruption insurance, coverage is generally triggered only where there is "direct physical loss of or damage to" to insured property by a covered cause of loss. Some courts have concluded that contamination events that render property unfit for intended use may constitute a "physical loss" sufficient to trigger business interruption coverage, but this will be a fact-intensive exercise in each case. Some businesses (e.g., in the healthcare industry) may have business interruption coverage for communicable or infectious diseases without a physical damage trigger. However, for the standard policyholder, a cessation of business operations without any "physical loss" to insured property will not trigger coverage.

Contingent business interruption insurance provides coverage for losses arising from supply chain disruption, but generally requires physical damage to the property of a supplier or customer on whom the policyholder relies for business. Policies do vary, however, in their requirements to trigger contingent

## Force Majeure and the Coronavirus (COVID-19)

business interruption insurance, and should be carefully assessed to determine if the circumstances and policy language support coverage. Businesses may also maintain “supply chain risk insurance” that does not require physical damage to property.

Property policies may also contain “civil authority” coverage that insures for business interruption-related losses when the government prohibits or impairs access to the policyholder’s premises. As with the other types of business interruption coverage, this often applies only where there is physical damage – here, where there is physical damage to adjacent or nearby property. However, if civil authorities block access to the business premises, the policy should be reviewed carefully to determine whether there is a “physical loss” trigger and, if so, whether it is met.

Policies may also expressly exclude coverage for infectious diseases or pathogen contamination events. Businesses in service and healthcare industries, on the other hand, may have policy endorsements specifically providing limited coverage for such perils.

### IV. Next Steps

1. Proactively evaluate your contracts to determine your requirements, contract provisions and insurance policies that may be applicable to the current COVID-19 situation.
2. Take steps to promptly identify any actual or potential impacts arising from the situation both within your company and your supply chain.
3. If you do identify any impacts, promptly assess and determine what it will take to respond and whether and to what extent there are actions that you can take to address or mitigate the situation.
4. Where impact events arise, be sure to track these events and your efforts to address them.
5. Determine if you have any notice or reporting requirements as these may be thresholds to your ability to assert defenses or seek relief.
6. If you are encountering impacts that you think may constitute a force majeure event, contact your counsel to make sure you do so in a way that minimizes your potential liability.

This is a rapidly evolving situation. Taking steps to identify and address your potential risk areas is important. We are watching developments in this area closely and will issue further alerts as matters unfold. The Stinson Task Force is planning a webinar to cover this topic on March 24 from 12 - 1 p.m. CDT. If you are interested in this event, please [let us know](#).

### CONTACTS

Christina Arnone

Zane A. Gilmer

Sharon R. Markowitz

**STINSON**

STINSON LLP \ STINSON.COM

# Force Majeure and the Coronavirus (COVID-19)

## RELATED CAPABILITIES

Business Litigation

Corporate Finance

Government Contracts & Investigations

Labor, Employment & Benefits

STINSON

STINSON LLP \ STINSON.COM