

COVID-19 and Force Majeure Clauses

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FIRM OVERVIEW

- Provide value-added legal services to innovative enterprises worldwide, particularly in highly-regulated industries
- Serve the principal challenges faced by management and board of directors of business enterprises
- Act as a strategic business partner to a diversified client base
- Provide an exceptional understanding of the financial, regulatory, and industry environments important to our clients
- Wilson Sonsini's **COVID-19 Client Advisory Resource** is a collection of alerts, advisories, and programs to help our clients maintain operations and business functions throughout the COVID-19 outbreak

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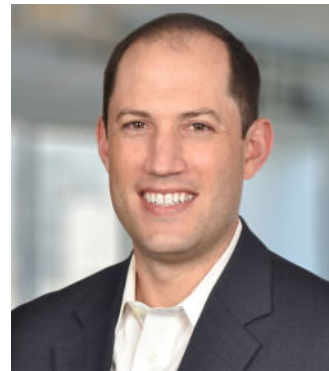
Professional Summaries



Victor Jih is a partner in the Los Angeles office who focuses his practice on internet strategy and litigation matters. He has extensive experience as a commercial litigator in a wide range of complex business disputes at both the trial and appellate levels.

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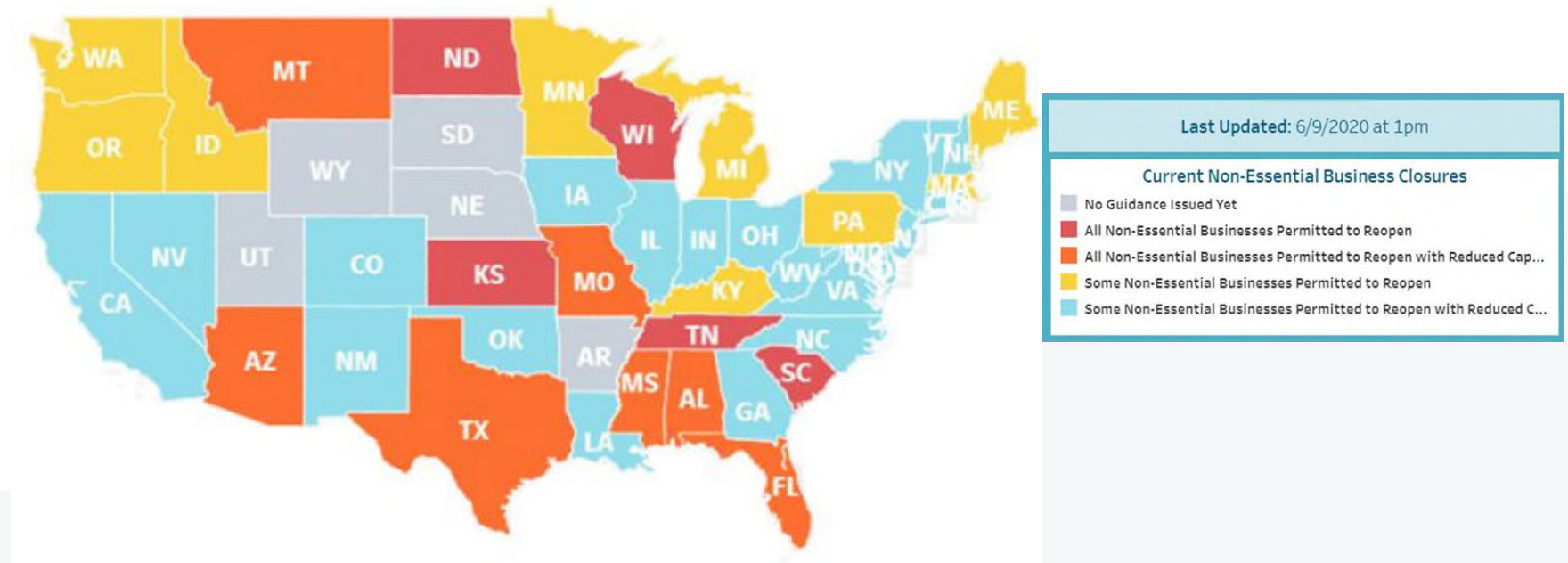
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Impact of COVID-19

Impact of COVID-19

Status of Shelter-in-place Orders



Source: COVID-19 and Alcohol Beverage Regulation, National Alcohol Beverage Control Association, <https://www.nabca.org/covid-19-resources>

Status of Shelter-in-place Orders



Impact of COVID-19

Global Alcoholic Beverages Market

Notable Headlines

- Distilled Spirits Council Member Companies Donate More Than \$8.1 Million to U.S. Bartenders Guild Foundation Emergency Relief Fund and Other Charitable Organizations
- Pandemic Brews Battle Between Liquor Wholesalers, Distillers, and Online Retailers
- Distilled Spirits Council Working With Congress to Ease Tax Hurdles Hampering Efforts to Produce Hand Sanitizer to Combat COVID-19

Source: <https://www.distilledspirits.org/news/discus-monitoring-covid-19-industry-news/#IndustryNews>

Impact of COVID-19

Global Alcoholic Beverages Market



What is Force Majeure?

What is Force Majeure?

Overview

- In the U.S., force majeure is a defense arising in contract.
- The purpose of a force majeure clause is to relieve one or both parties from performing certain duties during circumstances outside their control.
- Force majeure is distinct from common law defenses, such as impossibility and frustration of purpose.
- Courts in various states apply force majeure and common law defenses differently to reach non-uniform (and sometimes conflicting) results.

“An event or effect that can be neither anticipated nor controlled; esp., an unexpected event that prevents someone from doing or completing something that he or she had agreed or officially planned to do.”

“Force Majeure,” Black’s Law Dictionary (11th ed. 2019)

What is Force Majeure?

Frequently Asked Questions

- If my supplier is shutdown, am I responsible for production delays?
- Can we minimize commitments for advertising spend if no one will see it now?
- If my corporate event was force canceled, am I obligated to reschedule or can I get a refund?
- What happens to installments on commercial lease if we are deemed a “non-essential” business?

Bottom line: where contractual obligations have or will become more difficult, costly, or even impossible to perform, should parties be excused for non-performance?

Force Majeure in Practice

Force Majeure in Practice

Past Pandemics

Avian Flu

In a dispute arising out of the avian flu epidemic, an Iowa federal court ruled at the summary judgment stage that an egg producer could not cancel an order for machinery.

Rembrandt Enterprises, Inc. v. Dahmes Stainless, Inc., 2017 WL 3929308, at *13 (N.D. Iowa Sept. 7, 2017).

“Neither party shall be liable to the other for failure or delay in performance of the Work caused by war, riots, insurrections, proclamations, floods, fires, explosions, acts of any governmental body, terrorism, or other similar events beyond the reasonable control and without the fault of such party (‘Force Majeure Event’).”

Rembrandt’s Force Majeure clause

Force Majeure in Practice

Past Pandemics

Avian Flu

Court's Reasoning: the force majeure clause was written to apply only to the *equipment supplier's* performance, which was unimpacted by the pandemic, as the supplier was ready and willing to provide.

- Note, however, the farmer's frustration of purpose defense survived summary judgment because the court found that a jury could agree with the farmer that the purpose of the contract—*i.e.*, to increase egg production—was frustrated by the cancellation of orders due to the flu. *Id.* at *8.

“Neither party shall be liable to the other for failure or delay in performance of the Work caused by war, riots, insurrections, proclamations, floods, fires, explosions, acts of any governmental body, terrorism, or other similar events beyond the reasonable control and without the fault of such party (‘Force Majeure Event’).”

Rembrandt's Force Majeure clause

Force Majeure in Practice

Past Pandemics

Spanish Flu

- The closest historical parallel to the COVID-19 pandemic is likely the Spanish flu, which killed tens of millions of people, including approximately 675,000 Americans, between 1918 and 1920.
- Many courts rejected attempts to invoke the Spanish flu as an excuse for non-performance.
 - *See, e.g., Phelps v. Sch. Dist. No. 109, Wayne Cty.*, 134 N.E. 312, 313 (Ill. 1922) (rejecting attempt to avoid paying teacher's salary because school was closed for a two month period due to the pandemic).



Photo: National Archives photo no. 165-WW-269B-25

Force Majeure in Practice

Past Pandemics

Spanish Flu

- Other courts, however, reached a different conclusion on similar facts.
 - *See Gregg Sch. Twp., Morgan Cty. v. Hinshaw*, 132 N.E. 586, 587 (Ind. App. 1921) (excusing school board from paying teaching salaries on the basis of impossibility after school was closed by board of health).
- These divergent approaches reinforce the view that the outcome of COVID-19-related litigation will frequently be hard to predict.



Force Majeure in Practice

Modern Analogues

9/11 Terrorist Attacks

1. One New York court held that a customer's inability to contact a Manhattan-based travel agency, due to difficulties with telephone lines and closures of the agency's office, could entitle her to a reasonable suspension of her obligation to timely cancel her reservation, if not outright excuse her untimely cancellation. *Bush v. ProTravel Int'l, Inc.*, 746 N.Y.S.2d 790, 797 (N.Y. Civ. Ct. 2002).
2. However, another court ruled that leasees in the World Trade Center, who paid upfront rent credits in exchange for monthly services, could not recover those prepaid sums after the towers were destroyed. The court found the leasees were sophisticated parties, and their ability to recoup losses was expressly foreclosed by the contract. *One World Trade Ctr., LLC v. Cantor FitzgeraldSec.*, 789 N.Y.S.2d 652 (Sup. Ct. N.Y. Co. 2004).

Force Majeure in Practice

Classic Alcohol Cases

Wartime Alcohol Cases

In WWII, the Massachusetts Supreme Court found a buyer's payment obligations in an alcohol shipping contract persisted despite a force majeure event, and the buyer was obligated to pay the full shipment cost for molasses, even though the shipment had been destroyed by a submarine while in transit to the buyer.

Baetjer v. New England Alcohol Co., 319 Mass. 592, 66 N.E.2d 798 (1946).



Force Majeure in Practice

Classic Alcohol Cases

Prohibition

- In at least one Prohibition case, a California court agreed that a saloon lease could be excused entirely where the contract was specifically predicated on the leasee's ability to lawfully sell alcohol.
 - *Indus. Dev. & Land Co. v. Goldschmidt*, 56 Cal. App. 507, 509 (Dist. Ct. App. 1922).
- In other Prohibition cases, courts were unwilling to excuse saloon leases due to their ability to pivot and provide other services.
 - *See, e.g., Grace v. Croninger*, 12 Cal. App. 2d 603, 607 (1936).



Invoking Force Majeure

Invoking Force Majeure

Commonly Enumerated Categories

- Epidemic / pandemic / viral or communicable disease outbreak
- Quarantines
- Lack of or inability to obtain fuel, power, components, or materials
- Disruption of supply chains
- Disruption of transportation systems
- Disruption of labor force
- National emergency
- Act, order, or requirement of any governmental authority
- "Act of God"
- A "catch-all" phrase such as "or other similar causes beyond the control of such party"



Invoking Force Majeure

Overview

Three major considerations:

1. Contractual Language

2. Jurisdiction

3. Factual Analysis

Invoking Force Majeure

1. Contractual Language

Contractual Language

Force majeure clauses must be written and explicit.

- Contractual language may outline clear situation to trigger or even preempt force majeure.

Examples

1. “**Except for any payments due** [plaintiff] in accordance with this Lease, [plaintiff] and/or [defendant] shall be excused for the period of any delay and shall not be deemed in default with respect to the performance of any of the terms. . . .”
2. “If and when drilling or other operations hereunder are delayed or interrupted . . . **the time of such delay or interruption shall not be counted against Lessee**, anything in this lease to the contrary notwithstanding.”
3. “In the event [either party] is prevented, delayed, or stopped from performing any act . . . **then the time for the party's performance shall be extended** . . . by reason of such event of force majeure.”

Invoking Force Majeure

1. Contractual Language

Many clauses require impossibility or other performance impacts prior to being triggered.

Examples

1. “The parties' performance under this Agreement is subject to acts of God . . . or any other emergency beyond the parties' control, **making it inadvisable, illegal, or impossible to perform their obligations** under this Agreement.”
2. In case of strike, lockout, or other labor trouble (whether the parties hereto are directly or indirectly involved) . . . **which shall render it impossible for Seller to deliver, or Buyer to handle or dispose of such milk**, no liability for non-compliance with this agreement caused thereby during the time of continuance thereof shall exist or arise with respect to either party thereto.”

Invoking Force Majeure

2. Jurisdiction

California

Total nonperformance generally excused when:

1. a direct and proximate result of
2. a triggering force majeure event contemplated by the contract
3. that need only be unforeseeable if not specifically contemplated by the parties, and
4. “in spite of skill, diligence and good faith on [the party’s] part, performance became impossible or unreasonably expensive”

Invoking Force Majeure

2. Jurisdiction

California

- Some California statutes are instructive (but not controlling) on establishing the whether a force majeure event has occurred.
 - Cal. Civ. Code § 3526: “No man is responsible for that which no man can control.”
 - Cal. Civ. Code § 1511(2): providing that the performance of an obligation is excused “when it is prevented or delayed by an irresistible, superhuman cause, or by the act of public enemies of this state or of the United States, unless the parties have expressly agreed to the contrary.”
- Force majeure provisions must either be specific or else will be construed to refer to the unforeseeable.
 - *See Free Range Content, Inc. v. Google Inc.*, No. 14-CV-02329-BLF, 2016 WL 2902332, at *6 (N.D. Cal. May 13, 2016) (under California law, “unless a contract explicitly identifies an event as a force majeure, the event must be unforeseeable at the time of contracting”)

Invoking Force Majeure

2. Jurisdiction

New York

Total nonperformance generally excused when:

1. a direct and proximate result of
2. a triggering force majeure event expressly contemplated by the contract
3. that was unforeseeable at the time of contracting
4. beyond the parties' control, and
5. the force majeure event rendered the contractual performance objectively impossible

Invoking Force Majeure

2. Jurisdiction

New York

- Some New York courts have required events be “unforeseeable” even if they were specifically enumerated in the contract.
 - *Goldstein v. Orensanz Events LLC*, 146 AD3d 492, 492 (1st Dept 2017) (finding a wedding venue could not cancel a wedding contract after the city shut down the building, even though the force majeure clause accounted for “any cancellation” due to “government order,” because the shutdown was potentially foreseeable)
- Where the force majeure clause allows for total excuse of obligations, New York courts generally find a force majeure event only if the triggering event renders performance “objectively” impossible due to the destruction of the means of performance by a force majeure event.
 - *Pleasant Hill Developers, Inc. v. Foxwood Enters., LLC*, 65 A.D.3d 1203, 1206, 885 N.Y.S.2d 531 (2009); *Phillips Puerto Rico Core v. Tradax Petroleum Ltd.*, 782 F.2d 314, 319 (2d Cir. 1985).

Invoking Force Majeure

2. Jurisdiction

Other Jurisdictions

- A Seventh Circuit opinion from Judge Posner once suggested, “[A] force majeure clause must always be interpreted in accordance with its language and context, like any other provision in a written contract, rather than with reference to its name.” *Wisconsin Elec. Power Co. v. Union Pac. R. Co.*, 557 F.3d 504, 507 (7th Cir. 2009).
- Similarly, many courts in Texas will treat a force majeure clause like any other clause in the contract.

Invoking Force Majeure

3. Factual Analysis

Factual Analysis

1. The nature of the triggering event giving rise to nonperformance
2. Causation between the event and the specific performance to be excused
3. Type of remedy sought

Invoking Force Majeure

Additional Considerations

Logistical Questions

- If claiming termination, have you acted consistent with termination?
 - Contract will determine the method of invocation.
- There may be additional requirements such as notice periods, cure efforts, or other remedial measures as contemplated by parties.

Invoking Force Majeure

Common Law Comparison

Comparison to Common Law

1. Impossibility: Available in all jurisdictions. Excuses performance where contract has become “objectively” impossible. Some states acknowledge “temporary” impossibility.
2. Impracticability: Available in some jurisdictions. Excuses a party from a specific duty outlined in a contract when:
 1. That duty has become unreasonably difficult or too expensive to perform
 2. Due to an unforeseen circumstance or condition
3. Frustration of Purpose: Available in most jurisdictions. Excuses a party from performance when:
 1. Mutuality: contractual purpose is expressly understood by both parties
 2. Foreseeability: supervening event was not foreseeable
 3. Destruction: contractual purpose is rendered virtually worthless by supervening event to at least one party

Invoking Force Majeure

Current Application

How Courts are Treating Force Majeure Right Now

- At least one court in SDNY has granted a preliminary injunction where force majeure has been invoked: *E2W, LLC v. Kidzania Operations, S.a.r.l* (No. 1:2020-cv-02866, filed Apr. 6, 2020).
- There, an amusement park franchisee was compelled to close the park due to COVID-19 and subsequently failed to pay franchise royalties. The franchisor attempted to terminate the franchise for cause. The amusement park operator countered that force majeure excused its payment obligations because the clause was written to excuse “any of [the parties’] obligations” impacted by force majeure for the duration of the force majeure event.
 - The court enjoined the franchisor from terminating the contract, even though monetary payments are rarely considered force majeure. This may signal that courts are hesitant to embrace force majeure, even if potentially straightforward, to dismiss at the earliest pleading stages.

Strategic Considerations

Strategic Considerations

- Businesses may have interests impacted on either side of force majeure.
- Be careful in how you articulate the force majeure event itself and identify what is preventing performance.
- Have you been acting consistently with force majeure position?

Strategic Considerations

- What if you're wrong?
- Damages
 - Direct & Liquidated Damages
 - Consequential and Incidental
 - Specific Performance
 - Attorney's Fees

Strategic Considerations

- How does the force majeure position impact you? What does worst case look like if right or wrong?
- Timing
- Negotiated resolution?

Questions?

WSGR COVID-19 Task Force

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