

## ALERTS

## Litigation Alert — Force Majeure Under New York and Delaware Law

**March 19, 2020**

In a matter of weeks, the COVID-19 outbreak has brought much of the world to a standstill. With the sudden economic decline and government-mandated restrictions now in place, some businesses will find themselves unable to comply with their contractual obligations. Any business anticipating its own — or a counterparty's — inability to comply with contract responsibilities due to COVID-19 should be familiar with how force majeure and other aspects of contract law may apply to them during this global pandemic.[1] Insurance policies covering business interruptions should also be assessed.

### Force Majeure Provisions

A force majeure is an unanticipated event (for simplicity, this *Alert* will refer to it as the “event”) beyond the control of the contracting parties that makes it impracticable or impossible for a party to fulfill its responsibilities and obligations, and may excuse a party from performing under a contract.[2]

Businesses should look for the presence of — and any limitations on — force majeure provisions in any contracts they anticipate that they or their counterparty will struggle to fulfill as a result of the outfall from COVID-19. Those provisions typically require the disabling event to be unforeseeable to both parties, and sometimes specify certain types of events that are per se unforeseeable, such as, for example, earthquakes, acts of terrorism and sometimes epidemics or pandemics.

Since the World Health Organization declared COVID-19 a “pandemic” on March 11, 2020, force majeure clauses that expressly include “pandemics” will likely be triggered.[3] Other contractual language regarding viral outbreaks, epidemics, or governmental prohibitions may also trigger the clause.[4]

Even if COVID-19 falls within the scope of a force majeure provision, the event must *objectively* affect the parties’ ability to perform.[5]

Accordingly, a party seeking to invoke a force majeure clause to excuse its nonperformance must show that the event directly caused performance to be impossible or unreasonably expensive in spite of its skill, diligence, and good faith.[6] Again, the language of the contract will dictate the application, effect and scope of a force majeure clause.[7]

Force majeure provisions may have specific application in particular types of contracts. For more information on some of these specific applications please see the following *SRZ Alerts*: Real Estate Deals and Leases — COVID-19 Considerations (March 17, 2020) (discussing “go-dark” and material adverse effect provisions in leases and other real estate agreements), Trading Agreements — Buy-Side Considerations (COVID-19) (March 17, 2020) (discussing force majeure and related provisions in trading agreements, including ISDA master agreements, prime brokerage agreements, master repurchase agreements, futures agreements and FX master agreements), *SRZ Alert* on Business Interruption and Related Insurance for Losses from COVID-19 (March 17, 2020) (outlining business interruption insurance and other insurance related to loss).

## **What If There Is No Force Majeure Clause?**

Even without a force majeure clause, performance may still be excused if a party cannot meet its obligations due to COVID-19. Generally, a party has no duty to perform under a contract if performance becomes impossible or in some jurisdictions impracticable.[8] “Impossible” and “impractical” are legal standards. Courts may conclude that performance is impracticable when it can only be accomplished at an excessive, unreasonable, and unbargained-for cost,[9] or impossible when a party cannot perform due to circumstances beyond that party’s control.[10] Similarly, the legal doctrine of frustration of purpose excuses nonperformance in certain situations where the objectives of the contract have been utterly defeated by circumstances arising after the formation of the agreement.[11] Finally, contracts sometimes require the parties to

comply with the laws, orders, rules, regulations and requirements of governmental authorities, which also may excuse performance in the face of the many directives being issued for purposes of public health, as well as economic and financial stability.[12]

In the face of the substantial business disruptions that have occurred in the wake of COVID-19, counterparties may seek to renegotiate contracts or reach accommodations in light of longer-term business interests or to avoid the uncertainty of the application of the aforementioned legal doctrines.

## **Insurance Considerations**

The same circumstances that have made performance of contractual obligations impossible have created massive disruptions in businesses' normal operations, but certain types of insurance may help. Business interruption, use and occupancy, and other similar policies may cover losses caused by the insured's inability to continue normal business operations after losing the ability to use specified property or premises.[13] For more information about insurance for losses relating to COVID-19, please see SRZ's *Alert*, Business Interruption and Related Insurance for Losses from COVID-19 (March 17, 2020).

The full impact of COVID-19 on economies and businesses around the world is still uncertain. However, clients should familiarize themselves with the aforementioned contract and insurance doctrines. We will continue to closely monitor this public health crisis and the potential effects it could have on our client's businesses. Should you have any questions about the concepts explored in this *Alert* or other questions about your business in light of COVID-19 please contact your attorneys at Schulte Roth & Zabel or one of the authors.

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[1] COVID-19 effects may also trigger material adverse change provisions in M&A contracts and in other contexts. See, e.g., "Deal Terms — Assessing Material Adverse Change Clauses and Other Deal Certainty

Considerations Under and After COVID-19,” *SRZ Alert*, March 16, 2020, available here.

[2] GLEN BANKS, 28A NEW YORK PRACTICE SERIES-NEW YORK CONTRACT LAW § 20:13 Force majeure (2d ed. 2019).

[3] Betsy McKay, Jennifer Calfas and Talal Ansari, *Coronavirus Declared Pandemic by World Health Organization*, Wall Street J. (Mar. 11, 2020, 11:59pm), <https://www.wsj.com/articles/u-s-coronavirus-cases-top-1-000-11583917794>; see also *Akorn, Inc. v. Fresenius Kabi AG*, No. CV 2018-0300-JTL, 2018 WL 4719347, at \*51 (Del. Ch. Oct. 1, 2018), *aff’d*, 198 A.3d 724 (Del. 2018) (Clause listed “pandemics, earthquakes, floods, hurricanes, tornados or other natural disasters, weather-related events, force majeure events or other comparable events. . .”).

[4] *Duane Reade v. Stoneybrook Realty, LLC*, 63 A.D.3d 433, 434 (1st Dep’t 2009).

[5] Glen Banks, 28A New York Practice Series-New York Contract Law § 20:13 Force majeure (2d ed. 2019).

[6] Richard A. Lord, 30 Williston on Contracts § 77:31. Force Majeure clauses, (4th ed. 2019).

[7] *Constellation Energy Servs. of New York, Inc. v. New Water St. Corp.*, 146 A.D.3d 557, 558 (1st Dep’t 2017).

[8] Richard A. Lord, 30 Williston on Contracts § 77:31. Force Majeure clauses, (4th ed. 2019).

[9] *Id.*

[10] *Freedman v. Hason*, 155 A.D.3d 831, 833 (2d Dep’t 2017) (“[T]he impossibility must be produced by an unanticipated event that could not have been foreseen or guarded against in the contract”) (quoting *Kel Kim Corp. v. Central Mkts.*, 70 N.Y.2d 900, 902 (1987)).

[11] Richard A. Lord, 30 Williston on Contracts § 77:31. Force Majeure clauses, (4th ed. 2019); Restatement (Second) of Contracts ch. 11, § 266 Existing Impracticability or Frustration (Am. Law Inst. 1981) (October 2019 update).

[12] Tracy Batemen et al., 77A Corpus Juris Secundum, Sales § 370 (2020) (“Force majeure provisions generally have the effect of excusing

nonperformance arising out of certain causes, as, for instance, acts of God, acts of a public enemy, acts of the United States government.”); see also, *Castor Petroleum v. Petroterminal De Panama*, 107 A.D.3d 497, 498 (1st Dep’t 2013) (Government’s restrictive court order fell into the agreement’s broad force majeure provision which included, among other things, a ‘government embargo or interventions or other similar or dissimilar event or circumstances’.)

[13] Steven Pitt et al., 11A Couch on Insurance § 167:11. Generally; need for “loss”, (3rd ed. 2019).

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