

The Force of Force Majeure in Supply-Chain Agreements

Presented by Taft Law Chicago Lawyers:

John M. Riccione

Brianna M. Skelly

William J. Serritella, Jr.

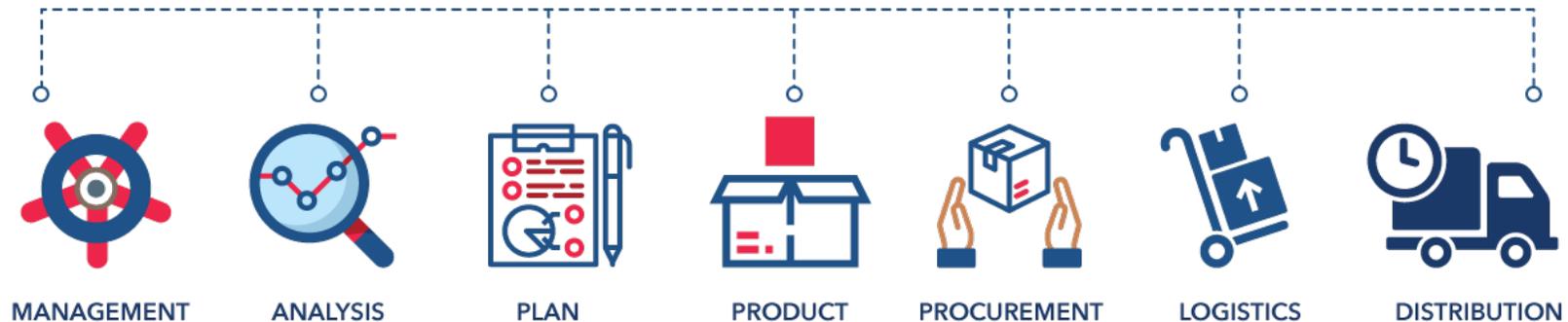
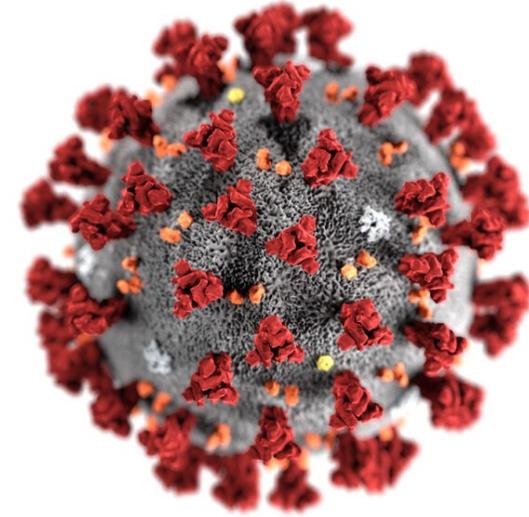
Elizabeth Winkowski

Taft/

ACC Association of
Corporate Counsel
CHICAGO

Covid-19 and Its Impact on the Supply Chain

- Availability of Goods and Materials
- Labor
- Logistics
- Price



Supply Chain Disruption as a Basis for Injunctive Relief in Breach of Contract Actions

Injunctive relief for manufacturers when suppliers demand a price increase or fail to deliver specified quantities of goods



Other Claims Relating to the Supply Chain

Business interruptions due to supply chain issues are not covered by commercial property and general liability insurance policies.



Covid-19, Supply Chain Disruption, and Defenses to Non-Performance

- Force majeure Clauses
- Impracticability (UCC § 2-615)
- Common Law Doctrines
- Impossibility
- Frustration of Purpose
(Commercial Frustration)



Force Majeure

- A “contractual provision allocating the risk of loss if performance becomes impossible or impracticable, especially as a result of an event or effect that the parties could not have anticipated or controlled”
 - Triggering events may include war, natural disasters, or government action
 - A mere increase in cost will not trigger a force majeure provision unless there is extreme and unreasonable difficulty, expense, or injury

Causation Element

- To excuse non-performance, a force majeure event must directly and proximately cause the non-performance.
 - Difficult to show if a defendant had difficulty fulfilling obligations prior to the pandemic or was able to meet obligations during the epidemic
 - *La Simple Co, Ltd. v. SLP Enterprises, LLC*, No. CV 21-10058-LTS, 2021 WL 1648762 (D. Mass. Apr. 27, 2021).

Interpreting Force Majeure Clauses

Sample Clause:

“The parties’ performance under this Agreement is subject to acts of God, war, government regulation, terrorism, disaster, strikes (except those involving [a party’s] employees or agents), civil disorder, curtailment of transportation facilities, or any other emergency beyond the parties’ control, making it inadvisable, illegal, or impossible to perform their obligations under this Agreement. Either party may cancel this Agreement for any one or more of such reasons upon written notice to the other.”

Interpretation Principles

- Force majeure clauses are usually narrowly construed and must specify the specific circumstances excusing performance.
- Courts may apply the principle of ejusdem generis (“of the same kind”), which determines the meaning of a word in a series based on the words surrounding it.
- Where included, a force majeure clause supersedes the common law doctrine of impossibility.
- A “catch-all” force majeure clause, such as “any other cause not enumerated herein but which is beyond the reasonable control of the parties” will typically not apply if parties could have reasonably foreseen the event at issue at the time of contracting.

Does Covid-19 Constitute a Force Majeure event?

The answer depends on the language of the contract.

- **Pandemic, epidemic, or virus.** Express terms such as these would obviously encompass Covid-19.
- **Government action.** Terms such as government action or government regulations may also apply to Covid-19 related executive orders.

Force Majeure: Government Action

It may be more difficult for certain manufacturers to claim inability to perform due to Covid-19 because many executive orders were broadly worded to include manufacturers as essential businesses.



Force Majeure: Government Action Con't

- In Illinois, “Essential Businesses and Operations” were broadly defined to include certain shipping and logistics services as well as certain manufacturers “producing and supplying essential products and services in and for industries.”
- Current federal guidance includes workers in the logistics and critical manufacturing sectors as part of the “Essential Critical Infrastructure Workforce.”

Force Majeure: Other Terms

- **Natural disaster.** Even if the force majeure clause does not include a pandemic or virus in its express terms, Covid-19 may constitute a “natural disaster.”
- **Act of God.** Defined as “an overwhelming, unpreventable event caused exclusively by forces of nature, such as an earthquake, flood, or tornado,” and includes 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.”
- **Other circumstances beyond the parties’ control.** Whether a “catch-all” provision such as this would cover Covid-19 depends on whether the pandemic was foreseeable, which is an unresolved question.

Impracticability (UCC § 2-615)

- UCC § 2-615 excuses seller's performance where performance "has been made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made or compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid."
- Elements
- Limitations
- Does Covid-19 render performance impracticable? It seems likely.

Impossibility

- Excuses contractual obligations where a party's performance becomes objectively impossible due to:
 - Destruction of the subject matter
 - Operation of law
- Elements
- Limitations
- Can Covid-19 render performance impossible? Possibly, but not likely.

Frustration of Purpose (Commercial Frustration)

- Excuses contractual obligations where a party's performance under the contract is rendered meaningless due to an unforeseen change in circumstances.
- Elements:
 - Event not reasonably foreseeable; and
 - Event totally or almost totally destroys the value of the party's performance.
- Can Covid-19 frustrate a contract's purpose? Probably yes, under some circumstances.

Checklist for Assessing Defenses

- Determine whether the contract contains a force majeure clause
 - If one is included, what events are specified?
 - Is there a catch-all provision?
 - Was the pandemic foreseeable at the time of the contract?
 - Did Covid-19 or related governmental actions cause non-performance?
 - Does the reason for non-performance go beyond economic hardship?

Checklist for Assessing Defenses Con't

- Consider whether other contract defenses are available
 - Impracticability, impossibility, frustration of purpose
- Review insurance policies
- Keep detailed records of events, dates, and evidence

Questions?



John Riccione

jriccione@taftlaw.com

(312) 836-4173



William Serritella, Jr.

wserritella@taftlaw.com

(312) 840-4396



Brianna Skelly

bskelly@taftlaw.com

(312) 836-4195



Elizabeth Winkowski

ewinkowski@taftlaw.com

(312) 840-4307

Thank You!

Taft/

ACC Association of
Corporate Counsel
CHICAGO