COVID-19 Financial Remedies: Force Majeure, Business Interruption Insurance Coverage and Contractual Provisions FAQs

Below are some FAQs based on inquiries that the presenters received during Kelley Drye's April 1, 2020 presentation of *COVID-19 Financial Remedies: Force Majeure, Business Interruption Insurance Coverage and Contractual Provisions*. A recording of the presentation is available here. While some of these questions were addressed during the presentation, other questions were not. Where there is overlap in the questions asked, we have consolidated those questions. Please note that the below FAQs are not legal advice and you should contact an attorney regarding legal questions specific to your circumstances.

1. **Question:** Would it be better to use the word "epidemic" or "pandemic" in a force majeure clause? In the alternative, should both words be included?

Answer: The inclusion of specific force majeure events will depend on the negotiating positions of the parties. As defined by the Centers for Disease Control and Prevention ("CDC"), an epidemic is a rise in the number of cases of a disease beyond what is normally expected in a geographic area. The word "pandemic" is used to describe a disease that has spread across multiple countries and affects a large number of people. Notably, neither the CDC nor the World Health Organization ("WHO") specify how many countries or how many people need to be affected in order for a disease to be declared a pandemic. However, the WHO's declaration of a pandemic will trigger response plans in a number of countries. These response plans may include travel bans, quarantines, and other measures. These measures may also be covered in the force majeure clause's enumerated events, such as "government orders" or "national or local restrictions."

When a contracting party relies on materials or parts from a specific geographic region it may want to include "epidemic" in the force majeure clause. For example, if ImportCo imports automotive parts from the Automotive Industry Cluster in the Wuhan Economic and Technological Zone, the party would want to be excused from its contractual performance obligations under a force majeure clause before the spread COVID-19 was declared a "pandemic." Conversely, if ManufactureCo purchases parts from ImportCo and wants to help ensure that ImportCo performs under the supply contract, it may seek to avoid the inclusion of "epidemic" in order to require ImportCo to source the automotive parts from an area or country not affected by the epidemic. It should also be noted that ManufactureCo may want to include force majeure clauses in its contracts with its customers that are consistent with the force majeure clauses contained in its contracts with ImportCo and other suppliers.

If both "epidemic" and "pandemic" are included in the contract, ImportCo would have broader defenses available to it. It should be noted that if the supply contract is silent as to "epidemic" or "pandemic," the Uniform Commercial Code Com. Code § 2615, as adopted by the applicable State jurisdiction ("UCC"), may apply.

2. **Question:** In states like Illinois, New York and California where the catch-all language may be limited to the specific events enumerated or similar events, is it better to use only "catch-all" language without listing any specific types of force majeure events?

Answer: Parties enter into contracts in order to provide certainty as to how and when obligations are performed. Contracts allocate risk between the parties. There is a danger in using catch-all phrases. Using phrases such as "any emergency beyond the parties' control" or "any unforeseen event not contemplated by the parties" without specify what types of events the force majeure clause covers are likely to cause conflict between the parties if the provisions of the clause are invoked. Remember, courts are most likely to uphold a force majeure defense if the circumstance that occurs matches or is similar to an event enumerated in the clause or contemplated elsewhere in the contract. Depending on the circumstances, a lack of enumerated events may increase the risk for both parties that they receive an adverse judgment from the court.

The party asserting a force majeure defense will bear the burden of proving that the event was unforeseeable and that the event makes performance impossible, impracticable or whatever standard is contained in the clause. Because most courts will apply a force majeure clause narrowly, failing to specify what events are covered will increase the burden of proof on the invoking party. The invoking party will need to show that the event was unforeseeable and that the lack of certainty caused unnecessary conflict between the parties. Moreover, if the party must look to common law contract defenses to avoid performance, this will place the determination of the adequacy of the defense squarely in the hands of the court and add to the risk that the defense(s) will fail.

Therefore, it is advisable that the parties give careful consideration to the force majeure enumerated events and identify with specificity those events that may impact either parties ability to perform under the contract. This includes looking at the subject matter of the contract, the parties' location, and other factors that determine when the force majeure clause will be applied. For example, a South Florida-based company that provides on-site information technology services to retail stores is faced with different possible force majeure events than an Oklahoma-based company that supplies finished steel products to the construction industry.

3. **Question:** In jurisdictions, such as the United States Court of Appeals for the Seventh Circuit, where a court may adopt the view that that common law defenses do not apply where parties have included force majeure language in the contract, is it advisable to include force majeure language?

Answer: It should be noted that most jurisdictions have not adopted a view as to whether the inclusion of a force majeure clause prevents the application of non-contractual defenses, many courts will allow a party to raise both contractual and common law defenses. That said, a party should consider if the jurisdiction's common law defenses and the provisions of the State-adopted UCC, if applicable, provide greater protection than that being contemplated in the contract. It would be prudent to include those protections in the contract's force majeure clause rather than forgo the inclusion of the clause. As a practical matter, it will be difficult for the parties to agree on if a force majeure clause may be invoked if they must turn to the common law and argue if the facts of precedential cases are similar or dissimilar to their circumstances.

4. **Question:** Some force majeure clauses require notice within a specified time after an event, and identification of the actual or anticipated inability to perform. How should companies proceed where there may be multiple events, such as travel bans or shelter-in-place orders in relevant jurisdictions, related to COVID-19? Is a blanket notice sufficient if there is ongoing uncertainty about damage or should a company send multiple force majeure notices as further events hinder or prevent contractual performance?

Answer: A party should carefully read the notice provisions of the force majeure clause and follow the requirements set forth therein. In general, a contracting party should send notice that it will be availing itself of the protections provided by a force majeure clause as soon as it believes that a force majeure event will affect its performance. A blanket notice is likely not sufficient if the contract has multiple deliverables and/or requires performance over an extended period of time. For example, partial performance of contractual obligations may be possible at different points in time as an event evolves.

As a practical matter, communication between the contracting parties is critical. Therefore, multiple notices may be advisable to address an evolving situation, such as COVID-19. Again, communications regarding circumstances that may affect the performance of contractual obligations, particularly among long-term business partners and key customers, can help preserve those relationships during this public health crisis.

5. **Question:** If a party to a contract notifies the other party that it is exercising its rights under a force majeure clause, how should the party receiving the notice respond?

Answer: The party receiving a notification of invocation of a force majeure clause should respond to the notice within a reasonable time. The response should set out the receiving party's position, cite to facts supporting this position and it should reserve all rights. The response should also take into account if the receiving party will be invoking similar force majeure defenses in other contracts in order to avoid inconsistent positions with regard to the force majeure event.

The response should be provided quickly if the receiving party is continuing to provide services or goods under the contract. Because parties have a general duty to mitigate their damages it is important for the receiving party to consider the affect that the cited force majeure event may have on the parties' post-notification contractual obligations. The parties may discuss if partial or delayed performance is possible. In short, consistent, timely and clear communications are key to helping the parties reach a resolution or preserving the parties' rights if litigation results.

6. **Question:** When drafting a force majeure clause in contracts going forward, is a public health crisis, such as COVID-19 now foreseeable?

Answer: Given the effect that COVID-19 is having on the global and national economy, companies should include "pandemic," "epidemic," or similar language in contracts force majeure clauses and consider how the parties' performance obligations will be affected or altered in such an event.

7. **Question:** Is it advisable to make a claim for business interruption even if the current policy has a virus/disease exclusion in order to be on record? Or does one risk future premiums being raised even if claim is denied for making that claim?

Answer: Before giving up on a business interruption claim because the policy contains a "virus/disease" exclusion, a policyholder should carefully review (and/or ask coverage counsel to review) the specific language of the exclusion, as well as the policy's insuring agreement, to confirm that the exclusion does, in fact, apply to the specific circumstances of the policyholder's claim. Even if the policy does contain a virus/disease exclusion that appears to bar coverage for a business interruption claim, the policyholder may want to consider making such a claim anyway, given the potential for legislative action that could require insurers to cover such claims. At this time, it is unclear whether any such legislation would require the policyholder to have made a claim at the time of the loss, or would allow policyholders to come forward with new claims after enactment of the legislation. In balancing whether to make such a claim, the policyholder should consult with its broker, who will likely have an understanding of the insurer's underwriting practices and the degree to which making a claim could impact future premium increases.

8. **Question:** Like flood insurance after a major flooding event, do you anticipate that event cancellation policies will be more difficult to obtain in the future?

Answer: Event cancellation insurance historically has been a profitable niche for insurers and they will undoubtedly continue to write those policies in the future. It is extremely unlikely, however, that insurers will be willing to cover the risk of cancellation losses resulting from COVID-19 or other communicable diseases. Accordingly, policyholders should expect to see policies with strict exclusionary language that bars coverage for cancellations caused by these events. Although such exclusions have always been common in event cancellation policies, insurers in the past were willing to allow policyholders to "buy back" those exclusions, effectively writing them out of the policy. In the future, insurers may not allow buy-backs of communicable disease exclusions, or in the alternative such buy-backs could be prohibitively expensive.

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