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COVID-19 UPDATE

Force Majeure Clauses and the COVID-19 Pandemic: What You Should Know

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In an effort to reduce the spread of the COVID-19 virus, on March 23, 2020, the Governor of the State of Hawaii issued a proclamation that requires all persons in the State to remain at home or at their place of residence starting on March 25 and continuing until April 30, 2020. Earlier proclamations by the Mayors of various counties, including Mayor Kirk Caldwell of the City and County of Honolulu, issued similar work-from-home mandates and closed restaurants, bars, and many other places of business. The resulting shut-down and closure of all but those companies conducting what is defined as Essential Business, is expected to create significant financial hardship for many (if not all) businesses in Hawaii, from retail to manufacturing, restaurants to processing, and industrial to professional services.

As businesses struggle to find a new normal, they are naturally questioning whether they or other parties to their contracts will be able to timely perform their obligations pursuant to leases, loans, and commercial contracts. They are, with good reason, looking to their contracts and agreements to determine if this COVID-19 pandemic may provide an excuse for a delay or non-performance of their obligations. Numerous scholarly articles about the applicability and interpretation of force majeure clauses have been proffered by law professors and practicing attorneys, but most companies are simply looking for a simple explanation and practical advice and direction. If you are a business facing potential performance issues on a lease or other contract, here is what you should know.

1. Force Majeure clauses in general. Force majeure clauses are included in many contracts to allow the parties to identify and allocate risk upon the occurrence of certain unforeseen or unexpected events that are considered out of the control of either party. They generally allow an affected party to delay or avoid performance of contractual obligations until the force majeure event ends, but in some cases may allow a party to terminate the agreement. Although they are treated as "boiler plate" language added to the ending paragraphs of a contract, there is no standard form of force majeure clause. As a result, the specific terms and language of the force majeure clause in your contract is important and is often the primary determining

factor as to whether a force majeure event has occurred and whether a party's performance may be delayed or excused.

2. Force Majeure clauses are rarely applicable. And that is the way it should be. Force majeure events are intended to be the very rare, unexpected exceptions to the general obligation of both parties to timely perform their obligations under a contract or suffer the consequences. Courts interpret force majeure provisions narrowly, typically only excusing performance where an identified force majeure event occurred that event made performance of a contractual obligation impossible or highly impracticable, *and* the affected party had no way of expecting or avoiding the effects of the force majeure event. Some force majeure clauses include catch-all type clauses that would appear to create a broader scope of applicability and protection of an affected party. However, given the time, cost, and uncertainty of seeking a court determination of the applicability of vague, but wide-reaching language in a force majeure clause, as a practical matter such provisions do little more than create an arguably enhanced bargaining position for an affected party.

3. Force Majeure clauses often do not apply to payment obligations. If the affected party is a lessee under a lease or receiver of services under a contract, they may find that the applicable force majeure clause includes a specific exclusion of payment obligations, thus requiring payments to continue being made during the period of the event. The provision may have language similar to the following found in a lease:

   Notwithstanding anything to the contrary in the preceding, it is understood and agreed that this provision shall not operate to excuse Lessee from the prompt payment of rent or any other payments required to be made under the terms of this Lease.

   Specific language like this in a provision of a contract will generally be enforced as it is presumed to be the intent of the parties, whether or not it was actually negotiated or even discussed at the time of contracting. There may be other non-monetary obligations specifically excluded from your force majeure clause as well.

4. The five things to consider about COVID-19 and a Force Majeure clause. So you have a contract, it contains a force majeure clause, and it does not specifically exclude the performance that you are seeking to delay or have excused. Here are five things you should consider before seeking relief under the force majeure provisions of a contract.

   a. *The triggering event*. What is the triggering event that is making performance impossible or impracticable? Is it the COVID-19 pandemic itself? Is it a shortage caused by others unable to provide necessary materials or services? Is it government action that has forced a shutdown of business? Is it an economic situation resulting from all that is happening in the world? Is it a workforce issue for you or others that make your performance impossible?

Conditions being attributed to COVID-19 generally may actually be caused by the government or other's response to the pandemic. This is important because the actual cause of the impediment to your performance must be the event enumerated in the force majeure clause. A "catch-all" provision may be helpful, but will not necessarily guaranty relief (see Item #2 above).

b. *The effect on performance*. Did the identified force majeure event actually prevent performance, or did it just make performance more expensive or difficult? Generally, to be enforceable, force majeure events need to actually make a party's performance of the contractual obligation impossible, or at least so expensive or difficult that it is virtually impossible. That is a tough standard to meet. If performance is possible but will just cost you more, expect that a court will just treat this event as a risk allocated to you under the contract and not give you a "get out of jail free card" by enforcing a force majeure clause. Of course, a judge or arbitrator might see things differently, and there are plenty of examples of cases from different jurisdictions going either way, but the time and cost of this gamble may be significant.

c. *The remedies under the contract*. Assuming it applies, what does the force majeure provision permit you to do? Are you excused from performance completely until the event ends? When does the COVID-19 related force majeure event end? Are you expected to catch up later, or is the missed performance of one or more periodic obligations fully excused? Are you entitled to seek other relief up to terminating the contract? Often the answers to these questions are not clear from the language of the force majeure clause itself and will require discussion and negotiation with the other party to the contract.

d. *The relationship with the other party*. Is this a long-term relationship and long-term contract? How has performance proceeded to date? As may be expected, the analysis of one-time performance contracts with a new relationship will be different from those where you have had a long, mutually-beneficial relationship with the contracting party and have an agreement expected to last many years into the future. If you or the other party have defaulted on your agreement repeatedly in the past, or have had a contentious relationship, you (and they) may look at how COVID-19 is affecting your situation differently.

e. *Procedural Requirements*. Expect that if you wish to claim the right to delay or excuse your performance under a lease or contract, you will likely need to comply with the specific requirements of the force majeure clause and other provisions of the document. Those may include detailed notice requirements and documentation. Simply calling the property manager or your standard contact at the local office of the other party may not be sufficient to exercise your contractual rights.

f. *Consider what you need versus what you want*. I know I said five things to consider, but I am adding one more. You should also consider what you *really need*. The COVID-19 pandemic and all that has followed has been, unquestionably, an unexpected and devastating event for everyone. Negotiated, mutually-agreed resolutions to address the performance issues created by COVID-19 are preferable to any party defaulting and subsequent litigation over excused performance under a force majeure provision of the contract. Having a clear understanding and appreciation for what the other party is facing, as well as what you *need* (not just what you want), will help you arrive at a solution that works for everyone. It will not be ideal, but right now, an ideal solution may be rare to impossible.

5. Force Majeure drafting in a COVID-19 world. If you are entering into a contract now, you are negotiating (among other things) a force majeure clause in the middle of a force majeure event. The challenge is that no one knows what will happen next. No one knows how long this will last. No one knows what the government in Hawaii, the Federal government, or the government in other states will do, or for how long they may do it. How do we plan for this unknown? The answer is simpler than it seems. It is time to stop treating force majeure clauses as "boiler plate" language, and spend the time and effort necessary to consider the COVID-19 related possibilities, including how you wish to apportion and allocate the risk and cost of different events. Hiring qualified legal counsel can help you do that and will help shape the discussion as a fair and equitable division of risk and reward. In some cases, you may just agree that if the COVID-19 pandemic continues to include government shutdowns or other identifiable action beyond a specified date, the parties will cancel their agreement, return deposits and walk away with no further obligation or liability with respect to each other.

As might expect, your particular situation and the language of your contract will be extremely important in determining the legal rights and remedies available to you. Advice and assistance from an experienced attorney who understands commercial contracts or leases, and the intricacies of delay and nonperformance claims is recommended as the above are just some of the issues that may be important in your particular situation.

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Bays Lung Rose Holma is a civil litigation and commercial transactions law firm located in Honolulu, Hawaii and specializing in real estate, construction, business law, commercial financing, and employment law. As an identified Essential Business, BLRH attorneys are available to advise and assist clients, including property owners and their property managers, at any time during and throughout the COVID-19 crisis. BLRH can be reached at (808) 523-9000 with calls directed to someone who can assist you, or via e-mail at mail@legalhawaii.com. In addition, a listing of our attorneys along with their telephone numbers and email addresses is available at www.legalhawaii.com.