

## Legal Considerations in Excusing Contractual Performance Due to Coronavirus

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*By Richard A. Walawender*

Many commentators have assumed that a party to a contract will be excused from performance if the coronavirus outbreak causes its inability to perform. But in order to be sure this would apply in a particular supply contract for the sale of goods, several factors need to be considered, depending on the nature of the supply contract involved.[1]

### *Scenario 1: Contract has no force majeure provision*

If the supply contract does not contain a force majeure provision, and nothing in the contract states that one party assumes the risk of not being able to perform (as may be the case in a "take-or-pay" contract), then § 2-615 of the Uniform Commercial Code (UCC) is available as a defense against a claim of breach for failure to supply goods. Pursuant to UCC § 2-615, a party may be excused for non-performance where "performance as agreed 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." In other words, performance is excused when it becomes "commercially impracticable because of unforeseen supervening circumstances." Note, however, that where a supplier's ability to supply is only partially impacted, or if it the supplier still has quantities of inventory of the goods available, the supplier will generally be required to provide those goods and, if applicable, allocate the available inventory among its customers in a fair and reasonable manner.

Another issue that courts examine is whether or not the contingency was foreseeable. If the contingency was foreseeable, the reasoning goes, the parties might have entered into the contract aware that such a contingency might occur. For supply contracts entered into prior to 2020, it is unlikely that parties could have foreseen the likelihood of a major supply chain disruption caused by the coronavirus outbreak. Accordingly, under the UCC and based on the above principles, if a supplier cannot continue to provide or produce goods due to the effects of coronavirus, this would most likely excuse performance for so long as such performance remains commercially impracticable.

### *Scenario 2: Contract has a broad force majeure clause*

If the supply contract has a force majeure clause expressly covering contingencies such as acts of God, epidemics, quarantines, or governmental actions, then the force majeure clause will determine how, and to what extent, the parties have allocated the risk of the contingency as between them. Typically, a force majeure clause not only defines the contingency, but also sets forth the procedures and effects of the occurrence. So, the clause might provide that, upon the occurrence of a force majeure event, the supplier is required to notify the customer within a certain period of time, and to provide other details as to the expected length of the disruption, possible alternative sources of supply, etc. Force majeure clauses also often entitle the customer to terminate the supply contract in the event of a force majeure occurrence, and impose additional obligations on the supplier to assist in resourcing the supply, moving tooling, delivering inventory and work in process, etc.

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Importantly, the supplier's failure to provide timely notice or to comply with its obligations under a force majeure clause may subject the supplier to claims of damages relating to the customer's attempts to resource the supply, even if the force majeure event excuses the supplier from having to continue to produce and deliver the goods. Accordingly, it is important for the supplier to pay close attention to the terms of the force majeure clause.

### *Scenario 3: Contract has a narrow force majeure clause that might not cover the contingency*

A more complicated scenario involves the situation where the supply contract contains a narrower force majeure clause that does not expressly include contingencies such as acts of God, epidemics, quarantines, or governmental actions, and/or further provides that the supplier's performance will not be excused under theories of force majeure or commercial impracticability beyond the contingencies expressly stated. In such cases, does the fact that the supply contract contains a force majeure clause necessarily mean that the commercial impracticability defense of UCC § 2-615 is no longer available, and that the parties must look only to the language of the force majeure clause?

First, it is important to carefully interpret the language of the force majeure clause. Many times, force majeure clauses will contain a "catch-all" term (e.g., "an event beyond the reasonable control of a party"), followed by a non-exhaustive list of examples of contingencies. In such cases, a supply chain disruption caused by the coronavirus outbreak should still be considered to be a force majeure event.

However, some force majeure clauses are more narrowly written and do not contain a "catch-all" term or a broader term such as "act of God", but are limited to a list of specific contingencies that are to be considered force majeure events. In such instances, to determine whether the commercially impracticable defense of UCC § 2-615 could still apply depends on a variety of factors that need to be analyzed in the context of the nature of the contract involved.

For instance, in take-or-pay contracts, narrowly written force majeure provisions are common, because the parties often intend to allocate the risk of unforeseen events on certain parties. Thus, with take-or-pay contracts, because the customer is required to pay for a certain minimum quantity of goods, whether or not actually purchased, the supplier may not be excused from its supply obligations even in the event of a coronavirus epidemic, especially if the goods can be obtained from alternate sources, albeit for much higher prices.

In the context of ordinary supply contracts, the question of whether a narrow force majeure clause precludes a party from invoking commercial impracticability under UCC § 2-615 requires a deeper legal analysis. First, there is the language of the clause itself. Some force majeure clauses expressly provide that the supplier's performance will not be excused under any other theories of force majeure or commercial impracticability, but many times the language is not so clear. Second, the intention of the parties is important to consider. Sometimes, the parties simply intend to mirror the commercial impracticability standards of UCC § 2-615 in their force majeure clauses, and, especially when the clause is ambiguous, the parties' prior practice and industry customs and standards may be relevant. Third, where there are conflicting terms and conditions, invoking a "battle of the forms" between the supplier and the customer, UCC § 2-615 may end up filling the gap in any case.

### *Conclusion*

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In many cases, the force majeure clause in a supply agreement will contemplate an event such as supply chain or production disruptions due to the coronavirus. In the absence of a force majeure clause, the commercial impracticability standard of UCC § 2-615 will likely apply to excuse performance, provided the disruption is attributable to the coronavirus outbreak. However, not all cases are so clear, and a more in-depth legal analysis is warranted before presuming, one way or the other, that a party is excused from performance due to the coronavirus. Please contact the authors or your Miller Canfield attorney with further questions.

*This information is based on the facts and guidance available at the time of publication, and may be subject to change.*

[1] This article pertains to contracts for the sale of goods governed by the Uniform Commercial Code under Michigan law. For service contracts or contracts not under the Uniform Commercial Code, including those governed by the Convention on Contracts for the International Sale of Goods, other principles may apply.