STATE OF CALIFORNIA *FORCE MAJEURE* LAW COMPENDIUM

(during COVID-19 pandemic)

Prepared by

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A. Introduction

This memorandum will seek to provide a California exemplar for the USLAW NETWORK Compendium of Law on relevant considerations with respect to invoking "force majeure" clauses in contracts in light of the ongoing COVID-19 crisis.

B. *Force majeure* in California

1. Introduction

The ongoing global COVID-19 pandemic is upending regular commercial activity across the United States and around the world, and that disruption is expected to escalate. Among the issues confronting our clients is the effect public health orders and other measures to address COVID-19 are threatening, impacting, and in some cases, outright prohibiting the performance of material contractual obligations. In every business transaction, extreme events beyond the control and fault of the obligor may arise and prevent that party from performing the contract. These are commonly referred to in commercial contracts as *force majeure* events. *Force majeure* clauses work to mitigate the negative effects of *force majeure* events, including business interruption and supply chain disruption. However if the contract is silent on *force majeure*, several other contract defenses remain available in California.

2. Requirements to Obtaining Relief Using *Force Majeure*

More than a century ago, the principal contractual impossibility defense to excuse non-performance was that performance was prevented by an "act of God." *Pope v. Farmers' Union & Milling Co*., 130 Cal. 139 (1900). Over time, the "act of God" impossibility defense came to be routinely embodied in commercial contracts as a *force majeure* clause. Generally, a *force majeure* clause is triggered when the occurrence of a *force majeure* event, sometimes generally referred to as an "act of God," ultimately renders performance so impracticable that it is excused. Today, California courts define a *force majeure* clause as one that allocates the risk of loss if performance becomes impossible or impracticable, especially as a result of an event or effect that the parties should not have anticipated or controlled." *Nat. Res. Def. Council v. Norton*, 236 F. Supp. 3d 1198, 1220 n.9 (E.D. Cal. 2017) (quoting Black's Law Dictionary 718 (9th ed. 2009)).

In some instances, performance will be delayed or fail due to voluntary human behavior in response to COVID-19, which may or may not be sufficient to constitute a *force majeure* event. Increasingly, restrictive orders issued by federal, state, and local governments to protect public health are interfering with intended contractual performance. While the language of each *force majeure* clause will merit close examination and analysis, where the COVID-19 pandemic is the reason for delayed performance or non-performance, especially when due to governmental orders or other government action, *force majeure* clauses are likely to be implicated and may excuse the non-performance. The fact that a company will lose money fulfilling its contractual obligations during the pandemic, however, standing alone, likely will be insufficient to trigger a *force majeure* clause.

If the contract is silent on *force majeure*, a court's decision whether to excuse an impacted party's performance during the *force majeure* event depends largely on the foreseeability of the event under applicable statutory or common law.

Under California law, unless a contract explicitly identifies an event as a *force majeure*—and we note that in some cases the *force majeure* clause may mention a global pandemic specifically—the event must be unforeseeable at the time of contracting to qualify. *Free Range Content, Inc. v. Google Inc*., No. 14-cv-02329-BLF, 2016 WL 2902332, at *6 (N.D. Cal., May 13, 2016) (citing *Watson Labs. Inc. v. Rhone-Poulenc Rorer, Inc*., 178 F. Supp. 2d 1099, 1111 (C.D. Cal. 2001). Regardless, for the COVID-19 outbreak to constitute a *force majeure* event, the ongoing pandemic must be the proximate cause of nonperformance. *See Hong Kong Islands Line Am. S.A. v. Distribution Servs. Ltd*., 795 F. Supp. 983, 989 (C.D. Cal. 1991), *aff'd*, 963 F.2d 378 (9th Cir. 1992). Thus, the focus of the inquiry today is the impact of the COVID-19 pandemic on performance.

The "act of God" defense has been codified and expanded upon in the California Civil Code. Section 1511 provides, in relevant part:

> Cal. Civil Code § 1511. Causes excusing performance.
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> The want of performance of an obligation, or of an offer of performance, in whole or in part, or any delay therein, is excused by the following causes, to the extent to which they operate:
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> 1. When such performance or offer is prevented or delayed by the act of the creditor, or by the operation of law, even though there may have been a stipulation that this shall not be an excuse; however, the parties may expressly require in a contract that the party relying on the provisions of this paragraph give written notice to the other party or parties, within a reasonable time after the occurrence of the event excusing performance, of an intention to claim an extension of time or of an intention to bring suit or of any other similar or related intent, provided the requirement of such notice is reasonable and just;
>
> 2. When it is prevented or delayed by an irresistible, superhuman cause, or by the act of public enemies of this state or of the United States, unless the parties have expressly agreed to the contrary; …

Note that section 1511, subsection (1) requires "written notice to the other party or parties, within a reasonable time after the occurrence of the event." While the COVID-19 pandemic is in some ways a slow moving event, a party who determines they will not be able to perform under their contract due to a governmental order must provide written notice to their contractual counterparty within a reasonable time to qualify for relief. What will be a reasonable time will differ depending on the identity of the parties, the nature of the performance, and the reason for the delay. Contracting parties also will need to closely review their agreements to determine if they agreed to waive their rights under section 1511.

Additionally, California law requires that parties invoking *force majeure* demonstrate that they made "sufficient" or "reasonable" efforts to avoid the consequences of the *force majeure* event, such as seeking other suppliers or other methods of performance. *See, e.g.*, *Butler v. Nepple* 54 Cal.2d 589, 599 (1960) (*force majeure* did not excuse a drilling company from its contractual obligations following a supplier strike where there was no showing that the additional expense or other methods to drill were "extremely or unreasonably difficult").)

3. Scope of Relief

Once impossibility is established or *force majeure* is enforced, the next threshold question is whether the circumstances merit only a delay in performance, or a complete termination of all contractual obligations. Generally, the impacted party is excused from performance. (*See San Mateo Community College Dist. v. Half Moon Bay Ltd. Partnership*, 65 Cal. App. 4th 401, 413 (1998)). However, if "time is of the essence" in the contract, a court may order a complete termination of all contractual obligations. (*See, e.g.*, *Autry v. Republic Productions* (1947) 30 Cal.2d 144 (holding that by the time Word War II was over, the economic conditions had changed to such a degree that the famous actor was excused from the performance of a contract he signed prior to the war).)

4. Other Considerations

Closely related to impossibility is the legal concept of frustration of purpose. Unlike *force majeure* clauses and California Civil Code section 1511, each of which is a defense to be raised to excuse non-performance, the doctrine of frustration of purpose is available as a defense where contractual performance remains possible but has become valueless. This defense to contract enforcement applies when performance is not impossible or impracticable, but has become pointless—i.e., the main purpose of a contract has become frustrated. *Dorn v. Goetz*, 85 Cal. App. 2d 407 (1948). A party's inability to pay alone, even if unexpected, will not be sufficient to invoke a frustration defense. Likewise, an increased cost to perform the contract may not be sufficient. To be successful in asserting a frustration defense, the purpose or 'desired object' of both parties must have been frustrated. In other words, the total or near-total destruction of the purpose for which, in the contemplation of both parties, the transaction was entered into must be shown. *Id*. at 411.

It cannot be underemphasized that a party invoking a *force majeure* clause or defense based on impossibility or frustration of purpose must be careful to establish that its inability to perform under the terms of the contract actually prevented the performance or frustrated the purpose of the contract, rather than merely increasing one's financial hardship incurred in performing its contractual obligations.

Finally, a party must take caution to adhere to any specific notice or other relevant requirements specific to the contract at issue.

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