# IN THE WAKE OF COVID-19

# FORCE MAJEURE AND BUSINESS INTERRUPTION WHAT CAN WE EXPECT FROM THE CASE LAW?

**A Joint Practical Guide from 2TG and K&L Gates LLP** **Spring 2020**

## Introduction

In Exodus 7-10, the land of the Pharaoh was visited with plagues that could have been a role call for the extraordinary events that will usually make up the list for force majeure clauses; in summary—hail; floods; infestation; pestilence; even death.

A good number of disputes are already rearing their heads from the Covid-19 and it is essential to make clear from the outset that the losses to business arise from both Covid-19 itself and the intervention by lawful diktat that has shut down economic activity and enterprises.

Unlike in 'normal' times, claims will now arise for economic losses resulting from Covid-19 as well as government-decreed shutdowns, which have resulted in closure or severe curtailment of business activity. Claims for business interruption would usually involve only some physical damage to premises, or even a requirement to close businesses when infectious disease may have been found to have emanated from within the premises. We are seeing an additional scenario today since claims for business interruption are normally consequent upon, for example, some untoward dramatic event (earthquake; terror attack) that impacts upon the running of the business or an individual pivotal to the business being struck down by illness (an actor; a sportsperson; a chef). Today and from hereon, we are also looking at wholesale closures imposed from outside agency regulation.

The burning question on the lips of so many whose livelihoods have been impacted by Covid-19 and the government sanctioned shut-down is whether and, if so, to what extent, there is any recourse for compensation in reliance upon contractual terms.

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**Force Majeure – General**

The expression 'force majeure' is not a separate legal principle in its own right. It is used as a description of a type of clause that excuses or suspends performance of contractual obligations on the occurrence of a specified event. No court will imply a force majeure clause beyond the common law principles discussed above—one has to be specifically provided for as a term of the contract.

If a party wishes to claim loss as a consequence of a force majeure event, such as Covid-19, then it must ensure that the event meets the contractual requirements to qualify as a force majeure event and then show that the clause applies to the event under scrutiny. In the English case of ***Tandrin Aviation Holdings Ltd v Aero Toy Store*** [2010] EWHC 40, it was held that a Purchaser could not rely upon force majeure, as it was well established under English law that market circumstances affecting the profitability of a contract was not force majeure. The Purchaser's reference to the words "any other cause beyond the Seller's reasonable control" within the force majeure clause in the contract could not be relied upon by the Purchaser, as only the Seller could rely upon this. The same result would likely be had in American courts. ***Kel Kim Corp. v. Cent. Mkts.***, 519 N.E.2d 295 (N.Y. 1987)

Courts interpret force majeure clauses narrowly, and it is often advantageous to draft such a clause to include a list of examples (as long as the event relied upon is on the list). The lists will often have the usual; hurricanes; floods; earthquakes (such events often classified as 'acts of God'). Unfortunately, no list ever covers everything, and try as one might to include other obvious events (terrorism; labour disputes; pandemics; disease) a catch-all wording such as "any other similar event" might not always work. Such wording is often constrained to apply in events of the same nature as those specifically listed. It may be less difficult to persuade a court to allow a force majeure catch-all phrase to apply if the event relied upon is similar to one or more in the listed events. If, for example, there is no provision at all for any form of pandemic, it might be more difficult to persuade any arbitrator or court that the Covid-19 pandemic comes within the catch-all phrase. For example, in the New York case of ***Kel Kim Corp. v. Cent. Mkts.***, 519 N.E.2d 295, 296 (N.Y. 1987), it was held that the failure of one party to secure insurance was not covered by a catch-all clause, because it was of a completely different kind of event than those specifically listed.

The International Chamber of Commerce has a model force majeure clause which provides that plagues, epidemics, curfew restrictions and prolonged breakdown of travel are all presumed to be outside both the parties' control and contemplation at the time that the contract was executed. Thus, unless such events are specifically excluded as force majeure events elsewhere in the contract, these will be helpful to use in classifying Covid-19 as a force majeure under standard clauses.

**The Case Law**

Early case law in the English courts found that an epidemic could be described as an example of force majeure ***Lebaupin v Richard Crispin & Co [1920]*** All ER 353 whilst almost a hundred years later, the case of ***Gardner v Clydesdale Bank [2013]*** EWHC 4356 (Ch) described a flu pandemic as an example of force majeure.

Interestingly, in the case of ***Navrom v Callitsis Ship Management SA [1988]*** 2 Lloyds Rep 416, the court found that there could be no justification to limit a force majeure clause to events that did not exist at the time of the contract or could not have been predicted at the time that the contract was made. There seems to be some tension between this dicta and the fundamental principle which generally supposes that to invoke a force majeure clause, the

event could not have been in the contemplation of the parties or reasonably foreseeable.

There is also tension in American case law, where some states do not allow force majeure clauses to provide excuses for foreseeable events, ***Kel Kim Corp. v. Cent. Mkts.***, 519 N.E.2d 295, 296 (N.Y. 1987), and others do, ***InterPertrol Berm. Ltd. v. Kaiser Aluminum Int'l Corp.***, 719 F.2d 992, 999 (9th Cir. 1983).

Perhaps all this proves is that there can be no absolute rule as to how such clauses will be interpreted, but the contract terms and the context will need careful scrutiny.

**Business Interruption**

In California, it is instructive to note that business interruption coverage operates to compensate the insured for those losses that stem from the business interruption such as loss of profits; loss of earnings; expenses incurred during the period of repair or restoration of the damaged property that has been destroyed or damaged by the peril covered in the policy contract. Such coverage may extend for a reasonable time required for such repairs to be effected: ***Buxbaum v. Aetna Life & Cas. Co.***, 126 Cal. Rptr. 2d 682 (Cal. Ct. App. 2002). A question in today's climate might be whether a business, having been shut down by government decree, but which is still liable for outgoings (rent; salaries; utilities), would come within the definition of 'expenses incurred.'

Generally the claim for business interruption can arise only when the entire business has suffered from interruption, not the later extra costs of a particular project: ***Pac. Coast Eng'g Co. v. St. Paul Fire & Marine Ins.***, 88 Cal. Rptr. 122 (Cal. Ct. App. 1970). The facts of this case disclose that the claimant's facility was shut down following a fire and explosion on a barge and the business interruption clause was found to cover losses during the period of shut-down, but not for additional expenses brought about by work after the shut-down when the barge was being restored. Once again, we see a tension between the ***Buxbaum*** case and this last cited case as to where to draw the line between business interruption and extra expenses after an interruption is over. All this goes to show is that no hard and fast rules can be gleaned from the cases but each one clearly turns on its own facts and the specific terms of applicable contracts.

Meanwhile, in New York, it has clearly been stated that the court is expected to construe business interruption clauses in insurance contracts in accordance with their plain language.

Where that language is unambiguous, the court can simply give effect to the clause as written: ***K.Bell & Assocs., Inc. v. Lloyds Underwriters***, 97 F.3d 632 (2d Cir. 1996). If an ambiguity exists, the New York courts will examine the "*reasonable expectations of the average insured upon reading the policy and employing common speech*": ***Mostow v. State Farm Ins. Cos.***, 668 N.E. 2d 392 (N.Y. 1996). In the aftermath of the 9/11 attack, the court held that an airline's loss of business due to post 9/11 airline restrictions was **not** covered under business interruption insurance. In that case the contract required that an interruption be caused by physical damage in order to be covered, and the court found that the physical destruction of the airline's ticket counter at the World Trade Center and a collection of ash at the airline's Reagan Airport location was not connected to $1.2 billion in lost ticket revenue and that the government order (restricting flights) was not a direct result of the actual physical damage at either the insured's location or adjacent location, but had been issued entirely due to national security concerns; ***United Airlines, Inc. v. Ins. Co. of State of Pa.***, 385 F. Supp. 2d 343 (S.D.N.Y. 2005). How this decision might play into claims arising from Covid-19 in cases which involve no physical damage but losses all arise from similar public policy considerations will

need to be seen, and will likely turn on individual facts and contract language.

Once again, it must be stated that the exact terms of the policy will need to be considered.

**Conclusion**

This (hoped) once in a lifetime pandemic, that has created such disruption, might allow parties to find sympathy within the courts to give as broad an interpretation as possible to any force majeure clause. Assuming that a pandemic does come within a force majeure clause, it may then be possible to argue that some of the measures imposed, such as the closing of borders and travel restrictions, may fall within a more liberal interpretation of force majeure. As can be seen from the canter through the cases above, some outcomes are fairly easy to predict, others not so. It will be interesting to see how different courts in different jurisdictions care to interpret what claims are allowed and what claims are declined.

Whilst a good deal of sympathy is likely to be engendered for the companies and businesses that have sustained losses entirely outside of their control, on the other hand, the sheer scale of the likely claims may be considered by the courts to be of such magnitude that the courts may exercise caution due to the unprecedented claims likely to be made upon the purses of insurers in particular. The courts may be faced with the unenviable task of having to choose between businesses that have sustained unrecoverable losses and insurers who might even run the risk of being unable to find sufficient funds to meet all the claims made upon their policies.

Only time will tell.

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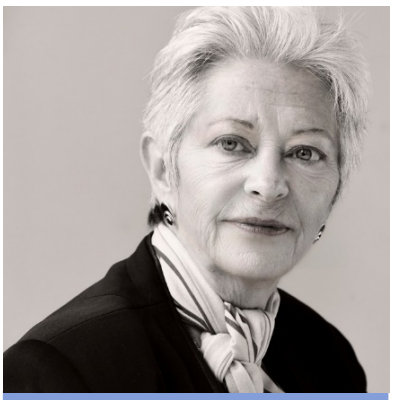

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Jacqueline's areas of work span contract and tort. She handles commercial matters both in the UK and the US as well as personal injury, clinical negligence, insurance and product liability.

Jacqueline has acted for both claimants and defendants in very high-profile, public interest cases. She has acted for local authorities and insurers as well as receiving a significant volume of instructions from trades' unions and Government departments, the Police and the Fire Brigade. She has acted for claimants in cases arising out of major disasters, including the original and recent Thalidomide claims. She is also instructed in major multi-party matters and high profile group actions against multi-national corporations.

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