

## Recent events highlight value of *force majeure* clauses

In the wake of Hurricanes Katrina and Rita, businesses in a wide variety of industries publicly claimed *force majeure* — a legal principle (from the French for “greater force”) that releases a party from a contract after uncontrollable events such as natural disasters or war.

Leaders of many small and midsize businesses are also wondering whether they too should invoke this “act of God” clause. Recent catastrophic events have taught businesses of every size a lesson: A *force majeure* clause should be carefully crafted and incorporated into contracts or standard terms and conditions well before a major catastrophe occurs. That will help insulate businesses from unexpected liability after unforeseeable events.

Will the mere declaration of *force majeure* by a party to a contract relieve it from liability for failure to perform its obligations? The general answer is no. A party to a contract generally is required to perform its end of the contract, unless the contract specifies the circumstances under which performance is excused. This is what is typically called a *force majeure* clause.

In a famous federal case, a shipping company contended it was not liable for failure to deliver goods because the Suez Canal closed as a result of 1967’s Six Day War in the Middle East. The 2nd Circuit U.S. Court of Appeals ruled that without a specific clause in the contract, the shipper was liable.

The shipper was aware, the court held, of

tensions in the Middle East and could have made contingency plans to ship the goods around the Cape of Good Hope, or it could have obtained insurance to cover any increased costs necessitated by a longer shipping route. Merely that it will cost a business more to live up to its agreement does not excuse it from what has become a losing contract.

On the other hand, if a natural disaster renders a contract impossible to perform or frustrates its intended purpose, a contracting party may be legally excused from performance without being held liable for damages. This is true if, despite the natural disaster, no human force can perform the contract and no foresight or prudence could have anticipated the “act of God.”

With today’s weather forecasting and reporting, meeting this standard in the case of a hurricane may be difficult. Acts of terrorism do not ordinarily excuse performance unless the contract specifies terrorism as a condition of *force majeure*.

In commercial contracts governed by the Uniform Commercial Code, a party may (under appropriate circumstances) be relieved from performance of a contract when fulfilling it is impracticable following an event the parties assumed would not happen, and when the non-occurrence of that event was a basic assumption of the contract.

The best way to protect a business is to have a *force majeure* clause in the contract that specifies the circumstances under

which the company will be excused from performance. Consider adding causes beyond “acts of God,” such as strikes, shortages, terrorism, embargoes or boycotts.

Well-drafted *force majeure* clauses will include a notice provision in which the party claiming *force majeure* must promptly notify the other party of the claim. In commercial settings where parties have extensive and regular dealings, these disputes and issues are often re-

solved around some cost-sharing or price adjustments if the parties will be dependent on each other well after the extraordinary event.

On the other hand, litigation is much more likely in circumstances where the cost of performance is sharply increased, margins are tight, the agreement involves a single transaction, or the failure of a party to perform will result in a significant loss to the other side. Litigation is made all the more likely without a properly crafted *force majeure* clause.

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