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Does Force Majeure Force Business Interruption?

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DOES FORCE MAJEURE FORCE BUSINESS INTERRUPTION?

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WHAT IS FORCE MAJEURE?

OVERVIEW OF “SUPERIOR FORCE” CLAUSES

- Contract provision that relieves contracting parties from liability for failing to perform contractual obligations due to circumstances beyond the parties’ control
- Non-performance must be caused by a valid triggering event
- Enumerated events in force majeure clause and standard of contract performance analyzed to determine excused performance and relief from liability
- Historically, narrowly construed



WHAT IS IN A FORCE MAJEURE CLAUSE?

4 ESSENTIAL ELEMENTS

A WELL-DRAFTED FORCE MAJEURE CLAUSE CONTAINS 4 ELEMENTS WITHIN THE LANGUAGE OF THE CLAUSE ITSELF

- Triggering events
- Necessary effect of the triggering event on contract performance
 - Causation
- Effect on contractual obligations
 - Standard of Performance
- Notice requirements



VALID TRIGGERING EVENTS

ANALYZING FORCE MAJEURE CLAUSES

**IDENTIFYING THE TRIGGERING EVENT AS
WELL AS THE TYPE OF EVENT IS AN IMPORTANT
FACTOR IN DETERMINING NON-
PERFORMANCE AND RELIEF FROM LIABILITY**

- Enumerated Events
- Broadly Covered Events
- “Acts of God”
- Catchall Provisions



CAUSATION
ANALYZING FORCE
MAJEURE CLAUSES

A DIRECT RELATIONSHIP BETWEEN THE TRIGGERING EVENT AND CONTRACT PERFORMANCE MUST BE ESTABLISHED

- The historic “but for” test remains at the forefront in determining causation
- Facts of case and specific language in force majeure clause analyzed to determine standard of contract performance:
 - Is performance impossible
 - Is performance inadvisable or commercially impractical
 - What was the intent of the parties at the time of contracting



NOTICE AND FORM OF NOTICE

ANALYZING FORCE MAJEURE CLAUSES

INVOKING FORCE MAJEURE

- Timely notice of invocation must be provided in accordance with the notice provisions of the force majeure clause
- Contract may contain specific provisions for method and form of notice
 - Specific individuals to notify
 - Specific language requirements
 - Specific methods of delivery



**DETERMINING RELIEF
FROM LIABILITY**
ANALYZING FORCE
MAJEURE CLAUSES

**DOES THE CONTRACT CONTEMPLATE THE
REQUESTED RELIEF?**

- Upon the establishment of causation, the party invoking relief has burden of demonstrating that the requested relief is expressly contemplated by the contract
- Foreseeability and negligence are often analyzed with contract language to determine whether invoking party may be excused from liability
- Facts and circumstances such as mitigation and alternative measures determine whether relief comes in the form of delayed performance or complete contract termination



COVID-19 AND FORCE MAJEURE

PRE-COVID-19 APPLICABILITY

TRADITIONAL PRINCIPLES GOVERNING FORCE MAJEURE CLAUSES

- Language strictly interpreted and narrowly enforced
- Clauses extremely limited in scope
- Contractual defense often analyzed within the context of common law defenses
- Performance excused only upon occurrence of a specific event beyond party's control
- Parties excused only if specific event justifying non-performance identified in contract



COVID-19 AND
FORCE MAJEURE
POST COVID-19
INTERPRETATION

**COURTS VARY IN CONSTRUCTION OF
FORCE MAJEURE PROVISIONS
IN CONTEXT OF COVID-19**

- Majority of courts identify Covid-19 as a force majeure event
 - Disputes over *the effect of triggering force majeure provisions* is common trend in litigation
- “Catch-all” language analyzed more broadly to include Covid-19
- Absent strict impossibility, force majeure clauses that permit a more lenient standard have allow courts more flexibility in providing relief
- Contract language, intent of contracting parties and the establishment of causation between the triggering event and non-performance remain narrow and at the forefront of court analysis for relief



WHAT GUIDANCE EXISTS: AT LEAST 14 JURISDICTIONS HAVE ADDRESSED FORCE MAJEURE WITHIN CONTEXT OF COVID-19

CASES ADDRESSING CAUSATION

- Difficulties making contractual payments and minimum purchases does not excuse performance without establishing that COVID-19 was the **precipitating cause** *Future St. Ltd. v. Big Belly Solar, LLC*, 2020 WL 4431764 (D. Mass. July 31, 2020)
- Defendant must demonstrate that county regulations restricting non-essential business operations “**directly affect[ed]** [its] ability to pay rent.” *Palm Springs Mile Assocs., Ltd v. Kirkland’s Stores, Inc.*, 2020 WL 5411353 (S.D. Fla. Sept. 9, 2020)
- Although force majeure clause unambiguously triggered by an executive order, the triggering of the force majeure clause only “**partially excused**” rental obligation because restaurant could have used at least 25% of space for pick-up and delivery services. *In re Hitz Rest. Grp.*, 616 B.R. 374 (Bankr. N.D. Ill. 2020)

CASES ADDRESSING REMEDIES

- Plaintiff could not obtain temporary restraining order to delay defendant’s termination of service agreement based on force majeure because “nothing in the Service Agreement” allowed “forestall termination” as a remedy of force majeure. *Ms v. Cbw Bank*, No. 20-04049-JWB, 2020 U.S. Dist. LEXIS 174257 (D. Kan. Sep. 23, 2020)
- Refusing to refund a deposit after contract termination based upon the contract’s force majeure provision is not a breach of contract when no language in the contract obligated the defendant to refund deposits based on a triggering of the force majeure clause. *NetOne, Inc. v. Panache Destination Mgmt.*, No. 20-cv-00150-DKW-WRP, 2020 U.S. Dist. LEXIS 99089 (D. Haw. June 5, 2020)
- Summary judgment and refund of full deposit in favor of Plaintiff when “governmental authority” made it “illegal or impossible” for defendant to hold event, this triggering the force majeure clause. *Sanders v. Edison Ballroom LLC*, 2021 NY Slip Op 30900(U) (Sup. Ct.)



FORCE MAJEURE TRIGGERED



CONTRACT PERFORMANCE EXCUSED



BUSINESS INTERRUPTION



WHAT IS BUSINESS INTERRUPTION INSURANCE?

OVERVIEW OF BUSINESS INTERRUPTION INSURANCE (BI INSURANCE)

- BI Insurance is a policy of Insurance that can help cover operating expenses and lost income if a covered loss forces your business to shut down.
- Exact coverage varies from policy to policy. Businesses must read their entire policy carefully to determine coverage.
- Potential coverage includes:
 - Lost revenue
 - Fixed costs, e.g. mortgage, rent, and lease payments
 - Loan payments
 - Employee payroll
- Subject to exclusions



HOW IS A BUSINESS INTERRUPTION CLAIM TRIGGERED?

GENERAL REQUIREMENTS TO ASSERT A BUSINESS INTERRUPTION CLAIM

- Necessary Business Closure
 - Business Suspension
 - Business Disruption
- Caused by “Direct Physical Loss or Direct Physical Damage”
- Resulting in actual loss of business income
- Caused by a “Covered Cause of Loss”



CIVIL AUTHORITY COVERAGE

IMPACT OF GOVERNMENT SHUTDOWN

CIVIL AUTHORITY CLOSURES

- Civil Authority coverage pays for business losses when a government bars access to an insured's property after damage to a property *other than the insured's*.
- Coverage is determined by language of the policy itself.
- Commonly requires that actual loss of business income be caused by “action of civil authority” that prohibits access to your premises due to “direct physical loss or damage to property other than the covered premises.”
- Requires complete prohibition from entering; therefore, essential businesses allowed to operate under limited capacity excluded.



HOW ARE BI POLICIES INTERPRETED?

WHAT ARE THE RULES OF THE ROAD?

INSURANCE CONTRACT INTERPRETATION

- Governed by general contract principles.
- Terms are given ordinary meaning.
- Policy provisions considered with policy as a whole.
- Ambiguous terms are construed against the insurance company and in favor of the policyholder.
- In the absence of misrepresentation, if policy language is clear, the clear meaning will be enforced.
- In the face of uncertainty, interpretation weighs in favor of coverage.
- Where coverage is denied based on exclusionary clause, that exclusion should be read narrowly.



COVID-19 AND BUSINESS INTERRUPTION

WHAT IS A DIRECT PHYSICAL LOSS?

INSURANCE COMPANY PERSPECTIVE

- Argue against coverage.
- Contend that “direct physical loss” requires physical alteration or structural damage is required to trigger coverage.
- COVID-19 cannot cause such damage, and economic damages caused by the virus cannot trigger coverage.

INSURED BUSINESS PERSPECTIVE

- Argue in favor of coverage.
- Contend “physical loss” under a BI Policy can occur when a property is impaired, becomes unusable, or unsuitable for a particular purpose.
- COVID-19 caused properties to become unusable and therefore the “physical loss” requirement is satisfied.



COVID-19 AND BUSINESS INTERRUPTION

CAN COVID-19 CAUSE DIRECT PHYSICAL LOSS?

SUCCESSFUL ARGUMENTS AGAINST COVERAGE

- BI Policies are designed to indemnify for physical loss, e.g. fire or storm; COVID-19 hurts people, not property.
 - Judge Caproni succinctly explained the coronavirus “damages lungs. It doesn’t damage printing presses.” *Social Life Magazine Inc. v. Sentinel Ins. Co. Ltd.*, Trans. at 5:3-4, No. 20 Civ. 3311 (VEC) (S.D.N.Y. May 14, 2020).
- Allegations of deprivation of use are insufficient because “direct physical” modifies “loss” and “damage”; therefore, the damage must be “actual.” *Torgerson Properties, Inc. v. Cont’l Cas. Co.*, 520 F. Supp. 3d 1155 (D. Minn. 2021).
- Policy language referencing a “period of restoration” bolsters argument that “physical loss” requires actual structural damage. *Equity Planning Corp. v. Westfield Ins. Co.*, 522 F. Supp. 3d 308 (N.D. Ohio 2021).



COVID-19 AND BUSINESS INTERRUPTION

CAN COVID-19 CAUSE DIRECT PHYSICAL LOSS?

SUCCESSFUL ARGUMENTS IN FAVOR OF COVERAGE

- The plain meaning of BI policy requiring “direct physical loss or direct physical damage” reasonably requires “physical loss” and “physical damage” to connote different conditions. E.g. *North State Deli, LLC et al. v. The Cincinnati Ins. Co. No. 20-CVS-02569, 2020* (N.C. Gen. Ct. Justice, Durham Cnty. Oct. 7, 2020).
- “Direct Physical Loss” includes circumstances making the covered property uninhabitable, inaccessible, and dangerous. *Elegant Massage, LLC v. State Farm Mut. Auto. Ins. Co.*, 506 F. Supp. 3d 360 (E.D.Va. 2020).
- Physical Loss requirement satisfied where COVID-19 particles attach to and damaged covered property, making it “unsafe and unusable.” *Studio 417, Inc. v. Cincinnati Ins. Co.*, 20-CV-03127-SRB, 2020 WL 4692385 (W.D. Mo. Aug. 12, 2020)



POLICY EXCLUSIONS

IMPACT OF SARS SHAPING COVID-19 COVERAGE

VIRUS EXCLUSIONS

- Even if insured can establish a covered cause of loss, many BI Policies contain virus exclusions which may preclude coverage.
- Following 2003 SARS outbreak, many insurers introduced exclusion clauses related to communicable diseases and epidemics/pandemics.
- Virus exclusion language varies by policy, but can exclude loss or damage caused directly or indirectly by a “virus or bacteria” or “communicable disease.”
- In the future, insureds may look to communicable disease riders to cover costs associated with government-mandated shutdowns and cleaning contaminated property as a result of a pandemic.



POLICY EXCLUSIONS

ATTEMPTS TO AVOID VIRUS EXCLUSION

ARGUMENTS ATTEMPTING TO AVOID VIRUS EXCLUSIONS

- Anti-concurrent causation clauses are invalid.
 - Refusing to dismiss an insurance coverage lawsuit arising out of COVID-19 related concert cancellations and postponements determining that the complaint adequately alleged that COVID-19 was *not* the proximate cause of the cancellations. The virus exclusion included losses “directly or indirectly arising out of ... any communicable disease.” *Frantic, Inc. v. Certain Underwriters at Lloyd’s, London Subscribing to Policy No. B1333ECB190291, et al.*, Case No. 21STCV21403 (Cal. Sup. Ct.).
- Plain language of Virus Exclusion requires that the virus be the immediate cause of the loss.
 - Denying motion to dismiss and finding virus exclusion inapplicable where plaintiff did not allege presence of virus on covered property and alleged that shutdown order was sole cause of loss. *Elegant Massage, LLC v. State Farm Mut. Auto. Ins. Co.*, 506 F. Supp. 3d 360 (E.D.Va. 2020).



BI INSURANCE LEGISLATION

CAN LEGISLATURES SOLVE THE BI INSURANCE DILEMMA?

LEGISLATURES ARE ADDRESSING BI INSURANCE POLICIES

- Pandemic Risk Insurance Act was reintroduced November 2, 2021.
- Multiple state legislatures are considering bills that would require insurers to provide business interruption coverage for COVID-19-related claims, irrespective of virus-related policy exclusions or policy provisions that would otherwise preclude coverage.
- Some bills would explicitly become retroactive to March 2020 upon ratification.
- Many bills establish funds from which insurers that pay BI claims can seek reimbursement.





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