

The Wrath of God and its Impact on Contracts - "Force Majeure"? and "MAC"? Clauses

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If you want to make God laugh, tell him your plans, so the joke goes. But acts of God are often are no joking matter. Hurricanes, earthquakes, drought, floods, locusts and other natural disasters can wreak havoc on life and property. They can also wreak havoc on M&A and other commercial agreements.

The recently announced coronavirus pandemic is a classic example. The pandemic has already resulted in the cancelation of hundreds of individual and group events, from my son's honeymoon cruise to numerous concerts, conventions, sporting events and other mass gatherings. The fallout on the airline, hospitality, cruise line, and other related industries likely will be staggering.

Lawyers, being natural doomsayers, have tried to anticipate God's wrath by crafting contractual clauses that excuse a party's obligations upon the occurrence of certain disastrous events. Known as "force majeure" (a French phrase meaning "superior force") and "material adverse change" ("MAC") clauses, these clauses typically kick in upon the occurrence of "acts of God" and certain other enumerated calamities.

Because of the severe consequences of permitting one party to postpone or escape its contractual obligations (such as closing a multi-million dollar acquisition), "force majeure" and "MAC" clauses deserve special attention from drafters. However, many practitioners regularly relegate these clauses to the boilerplate or definitions sections of agreements, where they often receive less scrutiny. (Worse, many agreements contain no provision regarding these events.) As with all other provisions of a contract, boilerplate or not, lack of attention to detail in this area can be disastrous (pun intended).

For example, many clauses simply state that a party's obligations are postponed or excused upon the occurrence of "acts of God or other events beyond the control of" the affected party. However, "acts of God" is a nebulous phrase and does not cover many man-made disasters such as war, embargo, strikes, cyber-attacks, etc. For example, is a quarantine imposed by governmental authorities in response to the coronavirus pandemic, as has occurred in Italy and other countries, an "act of God"? I doubt God would want to be blamed for these man-made disasters.

Moreover, "events beyond the control of" a party also may be insufficient. Courts are loath to undo contractual obligations, and therefore these exculpatory clauses are subject to strict interpretation. Florida courts, for example, have ruled that a "force majeure" has to be a permanent rather than a temporary circumstance. Using the coronavirus pandemic as an example again, is the pandemic permanent or temporary? More likely the later because the coronavirus like earlier influenza epidemics eventually peters out, which means this pandemic may not be a "force majeure" at all.

"MAC" clauses similarly are fraught with language inexactitudes. Often the "MAC" clause is triggered when an event "could (or would, depending on who you represent) have a material adverse effect on" the other party. Rarely is "material adverse effect" quantified, leaving the determination to the vagaries of litigation. Moreover, the clause typically focuses on the particular target company or industry, but what about the impact on the purchaser? Suppose the purchaser can no longer obtain financing, or financing on reasonable terms? Is this a "MAC"?

Conversely, overly broad "force majeure" and "MAC" clauses may create an illusory contract that amounts to an option by the party benefited thereby. The world is full of risks, business, natural and otherwise, and to create an escape clause that permits a party to back out of a deal due to events that could reasonably be anticipated seems unreasonable. That is what insurance is for, for that matter (although many insurance contracts have multitude limitations and escapes for the insurer that makes typical "force majeure" and "MAC" clauses seem like child's play).

Another defect of these clauses is they do not clearly spell out the process for determining whether an "act of God" or other enumerated event has occurred or, once it has occurred, the obligations of the parties. Suppose one party claims the coronavirus pandemic triggers the "force majeure" clause and the other party disagrees? What is the process for resolving the dispute? Often, the only resort is a race to the courthouse. Perhaps a more efficient approach would be to name an expert that is familiar with the industry and can make a swifter and more reasoned determination.

And even if the parties agree to postpone an obligation, when should the postponement end and the obligation be reinstated? Suppose the triggering event potentially could last months or years? Few in business can wait days or weeks much less years for an "act of God" to be resolved. A time limit after which the non-affected party can terminate the postponed agreement would be prudent. Then the question remains - what are the remedies available to the parties upon termination? Tricky questions indeed.

Even in the absence of specific contractual provisions, a contractual obligation may be excused by common law equitable concepts such as "frustration of purpose" or "impossibility of performance". However, courts typically interpret these concepts more stringently than "force majeure" or "MAC" clauses, such as by requiring a literal "impossibility" of performance rather than mere delay. As with other nebulous equitable rights and remedies, there is no substitute for a well drafted and specifically tailored provision covering the subject.

The coronavirus pandemic has had clients and their attorneys alike anxiously scrambling to review these often obscure provisions. While little can be done with existing language, practitioners should take this opportunity to review their standard "force majeure" and "MAC" clauses. Because if history is any guide, there will be many more "acts of God" and other calamities in our future.

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