Breach of Contract vs. Force Majeure – Economic Impact Analysis

Executives should evaluate non-contract economic impacts related to a force majeure, including customers, the supply chain, and potential financing agreements and debt covenants.

The current global business environment is unique. Businesses around the world are evaluating whether and when to intentionally underperform—or not perform at all—on a contract and are then seeking protection under a force majeure defense. Authorities have issued or are considering issuing force majeure "certificates" to provide a company a potential shelter from litigation. However, such a hall pass is just the starting point. Regardless of whether a company receives a pass, there are many economic considerations for a force majeure event.

ECONOMIC RIPPLE EFFECT – BEYOND THE CONTRACT AT ISSUE

No one can determine precisely the exact economic implication of such a decision. However, executive management and their legal counsel can make reasonable estimates and informed and calculated decisions. This is true whether a company is evaluating proceeding with a self-initiated force majeure event or reacting to supplier- or customer-initiated force majeure events.

The following are some economic implications executive management should likely consider whether initiating or reacting to a force majeure event:

- Potential economic damages if litigation or dispute proceedings are initiated
- Cost of offsetting supply chain for the short and medium terms
- Cost of storing and maintaining the value of inventory until sales channels return
- Loss and replacement of customers
- Loss of exclusivity arrangements for suppliers or customers
- Financing costs related to debt agreement clauses, and related impact to cross-collateral arrangements
- Cost of alternative actions to force majeure, including negotiating a contract amendment.

Many businesses do not have the financial and economic resources to perform these analyses, and the companies that do have in-house resources are being pulled in many directions and may not have the bandwidth to address these economic evaluations. Failure to perform reasonable economic analyses upfront may put businesses and their executives in a precarious position when stakeholders look back at these events and corresponding decisions in the coming months and years.

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