



54TH ANNUAL IFA LEGAL SYMPOSIUM



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May the Force Be With You: A Close Examination of the Drafting and Enforcement of Force-Majeure Clauses

Panelists

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Overview

1. Force majeure clauses in franchising
2. Introduction to hypothetical
3. Common law concepts
4. Force majeure clauses



Force Majeure Clauses in Franchising

- Audience Survey

Introduction to Hypothetical

- “Mikey,” the famous athletic footwear brand, subcontracts the manufacture of its iconic footwear to a third-party manufacturer based in Shanghai. Recently, the manufacturer has had to shut down production due to stringent government lockdown requirements to prevent the spread of the Covid virus. Not getting its shipments per the supply agreement with the manufacturer, Mikey is running out of merchandise inventories for its franchised mono-brand stores, e-commerce business and third party retailers.
- Mono-brand “Mikey” stores operate under franchise agreements requiring Mikey to sell franchisees reasonable quantities and assortments of footwear, but franchisees are not receiving new merchandise shipments due to the product shortage; they have banded together complaining to Mikey about the lack of supply.
- You are the GC of Mikey and have decided to consult with the law firm of Andrews, Dance, Richardson & Wulff about the franchisee complaints.



First Scenario

The franchise agreement has *no force majeure* clause.

Excusing Performance Under Common Law

- Under Common Law, a Supervening Event Occurring After Contract Made But Before Performance Can Excuse Duty to Perform if:
 1. Supervening event renders performance impossible or impracticable or it frustrates the purpose of the contract;
 2. Event was unforeseeable and without party's fault, negligence, or misconduct;
 3. Its non-occurrence was a basic assumption of the parties' agreement; and
 4. Risk of the event was not allocated to either party

Examples of Potential Supervening Events

- Natural Disasters
- Epidemic or Pandemic
- Terrorism
- War
- Death or Disability of Key Individual
- Governmental Action

Impossibility

- Performance no longer possible because of an unexpected supervening event beyond party's control
- Narrowly applied
- Generally requires:
 - Objective impossibility, not just financially unappealing or more difficult
 - Unanticipated, unforeseeable event
 - Not brought about by party's own fault

Impracticability

- Performance made impracticable without party's fault by unforeseeable event, the non-occurrence of which was basic assumption of the contract
- More flexibility than impossibility, but still high standard
- Commercially senseless; e.g., performance is not impossible, but unduly burdensome – can only be done at cost that is excessive, prohibitive, or unreasonable

Frustration of Purpose

- Though performance is possible, supervening event destroys the known, principal purpose of performance for one of the parties
- Anticipated value of contract no longer exists for one party due to supervening event, rendering performance pointless
- Party's "principal purpose" of contract must be known to other party; unstated, private purpose is not enough.
- Not sufficient to excuse duty to perform: changes in market conditions; changes to party's financial condition; increased costs; loss of expected profits; increased difficulty

Common Law Doctrines

- Analysis of common law doctrines in context of the hypothetical

Force Majeure Clauses

- Refer to the contract!
 - The force majeure analysis starts (and often ends) with the contract language.
- Key concepts:
 - Has a force majeure event occurred?
 - Does the force majeure event justify nonperformance?
 - What remedies are available?
 - How does a force majeure clause interact with common-law defenses?

Second Scenario

The franchise agreement has the following *force majeure clause*:

Neither Party shall be in breach of this Agreement if it is unable to perform any of its obligations hereunder due to Force Majeure (as defined below), provided (a) the affected Party provides the other Party with prompt notice of the occurrence of the Force Majeure event (no later than 10 days after its onset), which notice shall include a reasonably detailed description of the nature and extent of the event, the efforts the affected Party has made to avoid the impact of the event on that Party's performance, and an estimate of the duration of the event, (b) the affected Party exercises reasonable ongoing commercial efforts to mitigate the impact of the Force Majeure event and provides the non-affected Party with periodic updates on those efforts, (c) no Force Majeure event shall excuse any failure to pay amounts due and owing hereunder, and (d) if the Force Majeure event continues to materially impact the affected Party for more than 180 days after its onset, the non-affected Party shall have the right to terminate this Agreement, effective on notice thereof.

1. ***“Force Majeure”*** shall mean “any acts of God, war, riot, civil commotion, fire, flood, earthquake, labor disputes or embargo.”

Has a force majeure event occurred?

- Refer to the contract!
- Specified force majeure events
 - Dictionary definitions
 - Case law definitions

Has a force majeure event occurred?

- Catch-all provisions
 - What is the scope of the catch-all provision?
 - Was the event within the party's reasonable control?
- Foreseeability
 - Force majeure events generally may be foreseeable
 - Exceptions:
 - Contract may require force majeure events to be unforeseeable
 - Courts often require that events under the catch-all be unforeseeable

Alternative Scenarios

1. **“Force Majeure”** shall mean “any acts of God, war, riot, civil commotion, fire, flood, earthquake, labor disputes or embargo and any **similar** event beyond a Party’s reasonable control.”
2. **“Force Majeure”** shall mean “any acts of God, war, riot, civil commotion, fire, flood, earthquake, labor disputes or embargo and any other **unexpected** event beyond a Party’s reasonable control.”
3. **“Force Majeure”** shall mean “any acts of God, war, riot, civil commotion, fire, flood, earthquake, labor disputes or embargo **and any other event** beyond a Party’s reasonable control.”



Is Non-Performance Justified?

- Did the force majeure event cause nonperformance?
- Have you given notice?
 - Failure to give proper notice can doom a force majeure defense.
 - Scope of the notice can determine the scope of the defense.
 - When do courts forgive a failure to give notice?

Force Majeure and COVID-19

- Forecasts of unpredictable pandemic justice have not panned out.
 - *In re Hitz Restaurant Group*, 616 B.R. 374 (Bankr. N.D. Ill. 2020)
- Courts continue to apply force majeure clauses as written.

Third Scenario

The franchise agreement has the following *force majeure clause*:

Neither Party shall be in breach of this Agreement if it is unable to perform any of its obligations hereunder due to Force Majeure (as defined below), provided (a) **the affected Party provides the other Party with prompt notice of the occurrence of the Force Majeure event (no later than 10 days after its onset)**, which notice shall include a reasonably detailed description of the nature and extent of the event, the efforts the affected Party has made to avoid the impact of the event on that Party's performance, and an estimate of the duration of the event, (b) **the affected Party exercises reasonable ongoing commercial efforts to mitigate the impact of the Force Majeure event and provides the non-affected Party with periodic updates on those efforts**, (c) no Force Majeure event shall excuse any failure to pay amounts due and owing hereunder, and (d) if the Force Majeure event continues to materially impact the affected Party for more than 180 days after its onset, the non-affected Party shall have the right to terminate this Agreement, effective on notice thereof.

“Force Majeure” shall mean “any acts of God, war, riot, civil commotion, fire, flood, earthquake, labor disputes, pandemic, epidemic or embargo.” **Note: Pandemic and epidemic are included.**

Third Scenario - Hypotheticals

1. Due to pandemic-related shutdown orders, the third-party manufacturer used by Mikey as its sole supplier of footwear products can only produce half of the products it typically produces. Mikey allocates this reduced inventory so that its e-commerce business remains fully stocked with products, leaving its franchised mono-brand stores to suffer the brunt of the manufacturing shortfall.
2. Two weeks after its manufacturer shuts down production, Mikey gives notice to its franchisees of the shutdown as a force majeure event.
3. Five days after its manufacturer shuts down production, Mikey gives notice to its franchisees that a force majeure event has occurred and will last for 30 days. The shutdown actually lasts for 60 days.

What remedies are available?

- Refer to the contract!
 - Courts generally enforce force majeure clauses as written.
- Force majeure carve outs and “hell or high water” provisions
- Terminate?
- Delay?

Third Scenario

The franchise agreement has the following *force majeure clause*:

Neither Party shall be in breach of this Agreement if it is unable to perform any of its obligations hereunder due to Force Majeure (as defined below), provided (a) the affected Party provides the other Party with prompt notice of the occurrence of the Force Majeure event (no later than 10 days after its onset), which notice shall include a reasonably detailed description of the nature and extent of the event, the efforts the affected Party has made to avoid the impact of the event on that Party's performance, and an estimate of the duration of the event, (b) the affected Party exercises reasonable ongoing commercial efforts to mitigate the impact of the Force Majeure event and provides the non-affected Party with periodic updates on those efforts, (c) **no Force Majeure event shall excuse any failure to pay amounts due and owing hereunder**, and (d) **if the Force Majeure event continues to materially impact the affected Party for more than 180 days after its onset, the non-affected Party shall have the right to terminate this Agreement, effective on notice thereof.**

"Force Majeure" shall mean "any acts of God, war, riot, civil commotion, fire, flood, earthquake, labor disputes, pandemic, epidemic or embargo." **Note: Pandemic and epidemic are included.**

Third Scenario - Additional Hypotheticals

1. A Mikey franchisee is forced to close its store due to pandemic-related shutdown orders. The franchisee gives proper notice and seeks to excuse its obligation to pay franchise fees to Mikey for the duration of the shutdown.
2. After seven months of continued shutdown orders affecting its manufacturer, Mikey seeks to terminate the franchise agreements with some (but not all) of its franchisees.
3. After seven months of continued shutdown orders affecting Mikey's manufacturer, a franchisee seeks to terminate its franchise agreement with Mikey.
4. After two months of continued shutdown orders, Mikey's manufacturer is able to reopen and resume production. Mikey's franchisees demand that Mikey deliver the inventory they normally would have received during the manufacturer's shutdown.

Interaction with Common-Law Defenses

- Force majeure clauses may limit recourse to common-law defenses
- Foreseeability issues
 - Courts have held that events specified in the force majeure clause have been foreseen by the parties and therefore are not unforeseeable.
- Frustration of purpose often unaffected

Final Scenarios

Mikey seeks to excuse its failure to supply franchisees with footwear due to a pandemic-related shutdown of its sole third-party manufacturer. **Does Mikey have a common-law defense to performance?**

1. The franchise agreement provides: “*Force Majeure*” shall mean “any acts of God, war, riot, civil commotion, fire, flood, earthquake, labor disputes, pandemic, epidemic or embargo.”
2. The franchise agreement provides: “*Force Majeure*” shall mean “any war, riot, civil commotion, fire, flood, earthquake, labor disputes or embargo.” **Note: Pandemic, epidemic, and acts of God are not included.**