EXCUSED PERFORMANCE

MURPHY'S LAW IN OUTSOURCING

Murphy's Law – the principle that what can go wrong, will go wrong – applies to outsourcing. By and large, suppliers of outsourced services deliver good service to customers. Occasionally, something goes wrong. Lawyers earn their keep by providing for remote contingencies.

Suppose there is a serious failure. Customers have their remedies, including termination and recovery of large sums as damages. What protection can suppliers find in usual contract terms? Depending upon the situation, circumstances and contract language, suppliers may find protection in contract clauses that excuse nonperformance caused by *force majeure* conditions or customer acts or omissions that prevent, hinder or disrupt performance.

Force Majeure

Definitions of *force majeure* commonly list familiar examples – not only fire, flood, earthquakes and inclement weather, but war, riots, quarantines and a host of other dire conditions beyond the parties' control. Often, there is a catch-all reference to other circumstances beyond the parties' control; or the clause itself may define *force majeure* as all circumstances beyond the parties' control.

However, governing law varies. In some states, notably New York, protection may be limited to listed causes so that general exclusions have little or no value. California, by contrast, generally excuses nonperformance when 'prevented or delayed by an irresistible, superhuman cause, or by the act of public enemies' of the state or the U.S. [1]

Where the lists govern, they should be comprehensive and risks of particular concern – such as Florida hurricanes or California earthquakes – should be called out. Specificity is good practice even in California and other states where the law may afford broader protection. References should be phrased as broadly as possible. For example, 'storms and inclement weather or all kinds' should cover Atlantic hurricanes, Pacific typhoons and Midwestern tornadoes, among other things.

Over time, customary lists of *force majeure* conditions have grown longer. Oil shocks in the 1970s brought references to embargoes and commodity shortages. September 11, 2001 added terrorism to many forms.

But what of novel risks – such as surveillance, data thefts by criminal gangs, insurgencies and other irregular warfare, cyber-attacks by obscure proxies of intelligence agencies or what diplomats call 'non-state actors'? The answer is a definite 'maybe,' depending upon applicable law and the interpretation of contract language that may have been written before these risks took on their present form.

To reduce uncertainty and enlarge protection, one may succinctly stretch customary language to embrace contemporary risks. Earthquakes cause tsunamis, which may be even more destructive but are not always listed. Declared wars have gone out of style, so one might refer instead to 'war, revolution, insurgencies and other hostilities.' As for hostilities, might those include not only acts of war but 'hostile acts of governments, their security and intelligence agencies and other agents' such as espionage and surveillance? With protectionism in the air, conventional references to embargoes might refer also to sanctions and other trade restrictions. Litanies deserve scrutiny, in order to be sure that they cover emerging risks.

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1 California Civil Code § 1511(2).

COMMENTARY | EXCUSED PERFORMANCE

This publication is a summary of legal principles. Nothing in this document constitutes legal advice, which can only be obtained as a result of a personal consultation with an attorney. The information published here is believed accurate at the time of publication, but is subject to change and does not purport to be a complete statement of all relevant issues.

'Savings' Clauses and Excused Nonperformance

Many usual forms for outsourcing contracts contain so-called 'savings' clauses that excuse failures to perform caused by various acts or omissions of the customer, in somewhat the same way that *force majeure* clauses excuse nonperformance caused by calamities. These are helpful and desirable, but many customer forms are narrowly focused, or laden with restrictive qualifications.

Many, for example, limit their protection to breach of the customer's (comparatively few) express obligations, actionable torts or violations of law. In reality, there is much more that a customer might do or fail to do that could delay, disrupt, hinder or prevent performance – such as shutting down systems or closing facilities, as a customer might for any number of reasons that violate no law, breach no contract term and do not constitute actionable torts. Suppliers are therefore right to insist that delays or nonperformance be excused to the extent attributable to any act or omission of the customer or its agents that obstructs performance.

Without this broader protection, the supplier may not be excused unless it can prove commercial frustration, impracticability or impossibility. These defenses may require showings of extreme hardship, inability to perform or failure of basic assumptions on which performance depends – much more than actual customer delays, interference or mismanagement. If uneconomic or heroic efforts might have saved the day, a supplier may have no defense.

Rarely is one party entirely at fault when complex business relationships go wrong. In such situations, narrowly-focused, restrictive 'savings' clauses may effectively preclude suppliers' defense and counter-claims, increasing exposure and making settlements more difficult and expensive.

Suppliers should watch for and object to any of the following:

- Clauses limited to acts of the corporate customer, as opposed to those of its employees, affiliates and other contractors.
- Clauses limited to acts (rather than acts and omissions) or narrow classes of acts, such as violations of law, actionable torts or breach of express obligations. (Customers often have few express obligations, apart from payment for services.)
- Provisions to the effect that excused nonperformance is the supplier's sole remedy.
- Provisions to the effect that since the supplier has, typically, no right to terminate (so long as bills are paid) there is no breach (thus no liability for damages). When customers breach obligations (including express or implied obligations to cooperate) they should be accountable like anyone else and liable, even if the supplier has relinquished termination rights.

Many contract forms call for suppliers to give notice of any acts or omissions that adversely affect the supplier's performance. Suppliers should do this as a matter of course, just as they should act reasonably to mitigate delays, disruption and costs; although, technically, notice need not be a condition of any relief. If mitigation requires additional cost or performance, suppliers should be compensated, but customers often require (understandably from their standpoint) approval rights.

These are not, of course, the only issues that arise related to these provisions, and we do not here address termination rights, the interplay between *force majeure* clauses and recovery services, among other important, negotiable issues. But in both kinds of provisions, breadth of protection is crucial.