COVID-19 Impact on Renewable Energy Asset Development

March 27, 2020

PRACTICES Energy, Power and Natural Resources, Construction Litigation, Energy Finance, Energy Litigation, Project Finance and Development, Renewable Energy

The COVID-19 pandemic and the sweeping government action to curtail its effects across the globe has disrupted global supply chains and may continue to do so for quite some time. These constraints will strain project development timelines across the renewable energy industry.

Delays in receiving critical project components and labor shortages will inject performance uncertainty into nearly every critical phase of renewable energy asset development, including:

- project construction;
- permitting; and
- interconnection.[1]

In facing these uncertainties, parties involved in renewable energy project development should pay close attention to contractual excuses for delay and construction timeline risk, both in existing contracts and any contracts that are signed before the effects of the pandemic are fully understood. As detailed below, it is critical to note that whether the pandemic and associated government action constitute force majeure events will turn on each respective contract and the specific facts and circumstances of each case.

Contractual Excuses for Delay

Generally, a deadline or performance obligation in a project contract will only be excused to the extent the contract includes a specific excuse for delay. The most likely excuse for delay would be found in a contract's force majeure provisions.[2]

In analyzing force majeure clauses, U.S. courts focus on whether:

(1) the event qualifies as a force majeure event under the contract[3];

(2) the risk of nonperformance was foreseeable and subject to mitigation[4]; and

(3) performance is truly impossible.[5]

U.S. courts interpret force majeure clauses narrowly.[6] The burden of proof rests with the party relying on the clause.[7]

Force Majeure Clauses in Existing Contracts

Force majeure provisions are typically either "open" or "closed."

- An "open" provision typically defines force majeure as any event outside of a party's reasonable control that prevents performance. The clause may include a list of events that specifically qualify as force majeure, but the list is not exclusive.

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- A “closed” provision lists only specific events that will qualify as force majeure, though there may be a catch-all for similar events.[8]

In the wake of COVID-19, parties should carefully review their existing force majeure definitions for specific events such as “government action,” “labor shortages,” “disease outbreaks,” “quarantines,” “epidemics,” or “pandemics” because these may fall within the ambit of the currently known COVID-19 impacts.

Force Majeure Clauses in New Contracts

For contracts currently under negotiation, the parties should carefully consider whether to specifically address COVID-19 delays in the force majeure provisions. In making these considerations, it is very important to bear in mind that force majeure provisions often specifically exclude events that were known at the time the contract is signed. Even in the absence of such a specific exclusion, such a restriction may very well be inferred by a court. Therefore, a party that suspects its performance may be impacted by COVID-19 should not remain silent. Nor should the party simply add “COVID-19” or “pandemic” to the list of included events. Instead, a party wishing to retain an excuse based on COVID-19 issues should include very specific language that includes COVID-19 or pandemics generally as a listed force majeure event, but with additional language recognizing that, while it is a currently known event, the full impact is not currently known. Without such specific language, there is a risk a court would later view COVID-19 delays as foreseeable for any new contracts. In addition, the parties should consider whether any contractual deadlines should be extended up front in the face of these uncertainties.

Construction, Development, and Financing Risks for Developers, Lenders, Tax Equity Investors, and Offtakers

The primary COVID-19 issue facing developers, lenders, tax equity investors, and offtakers is the risk associated with construction delays caused by interruptions in the supply chain or labor shortages. These delays will impact each party in different ways depending on the phase of the project.

Development Stage Projects

At the development stage, before construction financing is secured, COVID-19’s impacts may limit the availability of capital or the willingness of investors, lenders, and offtakers to provide project financing.

Financing

- Solar projects at risk of not being operational before the end of 2021 may not receive intended investment tax credits, and wind projects must be operational before the end of 2020 to receive the full 2016 value of the production tax credits.[9]
- It may be difficult for developers to raise capital, as tax equity investors and construction lenders will likely pull back some until COVID-19’s impacts on construction deadlines and the economy overall are clearer

PPAs and Hedges

- PPAs and hedges signed at the development stage (before construction financing is committed) may include a deadline for obtaining such financing, beyond which the counterparty may terminate. While the language in such a contract should be reviewed

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carefully, this deadline does not typically get extended for force majeure or other excused delays.

Construction Stage Projects

Assuming construction financing has been secured, a force majeure event or delays during construction would impact not only developers, but also tax equity investors, construction lenders, offtakers, suppliers, and contractors.

Developers

- A developer with a PPA in place may become liable for delay damages, usually in the form of liquidated damages, for certain delays impacting the project schedule if the project cannot achieve commercial operation by a target commercial operation date. To the extent such delay is caused by a contractor and not excused, the developer may have a corresponding claim for delay against a contractor. These delay damages may even apply following a force majeure event if the PPA places a limit on the aggregate number of days for which a developer's performance may be excused by a force majeure event. If these delays extend too long, the counterparty may have the right to terminate the PPA.
- If the PPA is terminated because construction is delayed, tax equity likely will not fund, and developers may not be able to satisfy obligations to suppliers and contractors and may face damage claims accordingly.

Financing

- Under typical tax equity arrangements, the project must be operational by a specified deadline or the tax equity investor may terminate its obligation to fund. This date is not extended for force majeure or other delays.
- If tax equity does not fund such that any construction debt cannot be repaid on time, this will typically lead to a default to construction lenders. The lenders would have the right to accelerate and exercise remedies against the project, including foreclosure. This is a significantly adverse event not just for the project sponsor, but also for the lenders and for any offtakers that are secured by liens on the project and other assets of the project company.

Offtake Agreements

- PPAs and hedges will typically have a deadline for commercial operations, which deadline is typically extended for force majeure, but usually with some outside limit.
- For a project that is selling "as generated" energy, a delay beyond the outside date described above will usually result in delay damages for some period, then a right for the buyer to terminate.
- For a project that is selling a "fixed shape" energy product, a delay in completion will often not excuse the project's performance. The project will need to start settling on a specified date regardless of whether it is operational. Additionally, the counterparty will usually have the right to terminate if project completion is delayed beyond the outside date described above.
- Whether this is an issue for an offtaker will depend on how much construction risk the offtaker has taken and the credit support it is receiving pre-project completion.

Recommendations

COVID-19 has upended economies across the globe. Developers, construction lenders, tax equity investors, offtakers, and hedge providers should carefully review their contracts to analyze (1) the

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applicable force majeure provisions to understand what may or may not trigger a force majeure event and (2) their construction timeline risk.

Contract Review

In reviewing force majeure provisions, parties should review:

- defined force majeure events to see if reference is made to "epidemic," "pandemic," "labor shortages," "government intervention," "outbreak of widespread illness," or similar phrases;
- enumerated exclusions to force majeure; and
- the operative conditions of the force majeure clause, such as notice requirements, which should be strictly complied with, and any related termination rights.

Construction Risk Analysis

In analyzing construction timeline risk, parties should:

- review construction and financing deadlines in relevant operative documents to understand how potential supply chain delays and labor shortages may impact obligations;
- diligence the relevant supply chains to ensure that they account for and to anticipate supply chain risk;
- review the force majeure clauses in other project-related documents to ensure that there are no gaps in force majeure coverage that would prohibit the affected party from passing its damages through to the applicable counterparty or terminate, which would leave the developer, lender, or offtaker without recourse; and
- to the extent delays are expected based on recent developments, start communicating with the other transaction counterparties to see if the parties can agree upon an amended timeline or other mutually agreeable solution to address such delays.

For additional guidance navigating this evolving crisis, please visit our Trending Issues COVID-19 web page.

If you have any questions about the article below or issues with respect to your business or commercial operations, please do not hesitate to contact the partners listed at the end of this article.

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[1] The Edison Electric Institute (EEI) warned in February 2020 that up to 40% of electric company employees could be out sick, quarantined, or unable to remain in the workforce because of COVID-19. *See* EEI, *Electric Companies & Pandemic Planning*, https://www.eei.org/issuesandpolicy/Documents/Electric%20Companies%20and%20Pandemics%20-%20What%20You%20Should%20Know.pdf. *See also*, Darrel Proctor, "Pandemic Creating 'Crisis' for Solar Industry" (March 17, 2020), *https://www.powermag.com/pandemic-creating-crisis-for-solar-industry/*, last visited on March 18, 2020 (noting that "the COVID-19 pandemic is affecting delivery schedules and [the] ability to meet project completion deadlines based partly on new labor shortages.").

[2] Even if force majeure does not apply, other legal doctrines may excuse a party's performance depending on which law governs the contract. These legal doctrines include frustration of purpose and commercial impracticability, but like force majeure provisions, these doctrines are interpreted narrowly.

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[3] *See Kel Kim Corp. v. Central Markets, Inc.*, 70 N.Y. 2d 900, 902-03, N.Y.S.d 384, 385, 519 N.E.2d 295, 296 (1987).

[4] *See United States v. Brooks-Callaway Co.*, 318 U.S. 120, 122-23 (1943) (holding that the force majeure event must be unforeseeable).

[5] *See Phillips Puerto Rico Core, Inc. v. Tradax Petroleum Ltd.*, 1984 WL 677 (S.D.N.Y. Aug. 2, 1984).

[6] English law is more restrictive than U.S. law. To the extent your international projects are subject to English law, please let us know and we can advise you accordingly through our London branch. See our alert on March 11,

[7] *See Phibro Energy, Inc. v. Empresa De Polimeros De Sines Sarl*, 720 F. Supp. 312, 318 (S.D.N.Y. 1989).

[8] Under New York law, when a provision uses a catch-all, it is generally construed in accordance with the doctrine of *ejusdem generis*, which means that only events similar to the events specifically identified will be considered force majeure events.

[9] Democrats are already looking to insert renewable energy tax credit provisions into the COVID-19 stimulus packages currently under negotiation, but as of the date of this article, it is unclear if any extensions are forthcoming. *See* Lisa Martine Jenkins, "House Democrats Push for Renewable Energy Tax Credits in Coronavirus Stimulus" (March 17, 2020), https://morningconsult.com/2020/03/17/house-democrats-push-for-renewable-energy-tax-credits-in-coronavirus-stimulus/?utm_source=newsletter&utm_medium=email&utm_campaign=newsletter_axiosgenerate&stream=top, last visited March 19, 2020.

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