CHANGES TO US ENERGY AND TRADE POLICY COULD TRIGGER CONTRACTUAL RELIEF MECHANISMS

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US Energy, Infrastructure, and Resources Alert

By: Thomas G. Allen, Slade Sevier, Marla Tun Reschly, Eric D. Brill

The Trump Administration has issued several executive orders and made numerous policy pronouncements that could alter the economics of existing contracts and cause parties to explore new risk sharing mechanisms for future contracts. The primary area of uncertainty relates to tariffs due to their direct impact on the price of materials and equipment. Other US policy changes, such as federal funding freezes and the potential repeal of Inflation Reduction Act tax credits, could also impact deals, with outsized effects in the renewable energy industry.

Due to the effects these policy changes may have on the costs and benefits of existing and future contracts, parties should be aware of potential contractual relief clauses in those agreements. From a US law perspective, what follows is a discussion of contract clauses that might serve as a basis for relief under existing contracts, or as a risk sharing tool for future contracts. Energy transactions are used for specific context. However, many different types of transactions might be impacted by US policy changes, particularly for imports. In light of these policy changes, parties should carefully consider whether to include contractual relief clauses in future contracts aimed at excusing performance or altering the price of the bargain. For existing contracts, parties should closely review their rights and determine whether they have additional contractual rights because of changes to laws and policies.

FORCE MAJEURE

Force majeure clauses are provisions that excuse a party from performance, sometimes temporarily, where extraordinary events occur, beyond a party's control, that prevent or delay a party from performing a contractual obligation. The prevention or delay of performance must be without the fault or negligence of the non-performing party. Increased difficulty or increased cost of performance is typically not enough to sustain a force majeure defense. Even where a party's performance becomes unduly expensive, force majeure is not usually implicated. Whether force majeure applies depends heavily on the wording of the particular contract clause. Some US jurisdictions interpret force majeure clauses narrowly and only excuse performance if the specific event preventing or delaying performance is stated in the force majeure clause.

In the current environment, parties may want to explore the applicability of force majeure where government actions operate to terminate contracts, leases, permits, or other rights necessary to the performance of the contract. The repeal or elimination of subsidies and tax credits might also constitute an event of force majeure,

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depending on the specific contract language, although change in law or price adjustment clauses might be a better mechanism to capture situations amounting to changed deal economics.

CHANGE IN LAW

A change in law clause is designed to address any unexpected change in the legal or regulatory landscape that has a substantial impact on the obligations of a party. Such clauses are designed to offset the losses/damage due to changes in the law applicable at the time of contract execution.

Where the change is captured by the change in law clause and hinders a party's performance, that party can claim relief in accordance with the terms of the clause. Foreseeable costs are ordinarily not included in such provisions.

In the energy industry, we have seen change in law clauses related to duties and tariffs on key equipment. The uncertain nature of import duties on solar panels has been a popular area to use this type of risk allocation tool. Changes or adjustments to production and investment tax credits under the Inflation Reduction Act are also areas where parties have liberally utilized change in law provisions to account for this risk.

MATERIAL ADVERSE CHANGE/MATERIAL ADVERSE EFFECT

Material adverse change (MAC) clauses are intended to protect parties from substantial unanticipated events that adversely affect the financial or operational conditions of a business. Usually used in Mergers and Acquisitions agreements, MAC clauses allow the buyer to avoid closing where a significant decline in the target's value occurs or is reasonably anticipated. MAC clauses are often heavily negotiated, with sellers seeking narrow exceptions and buyers seeking wide protection. Like other contractual relief mechanisms discussed herein, whether a MAC clause is enforceable and will provide relief is dependent on the specific contractual language to which the parties have agreed. It is therefore critical to carefully identify and allocate potential risks and to address those risks directly in the contract wording. MAC clauses have infrequently been held to apply. However, there is precedent within the past 10 years of courts enforcing such provisions. *See, e.g., Akorn, Inc. v. Fresenius Kabi AG*, C.A. No. 2018-0300-JTL, 2018 WL 4719347 (Del. Ch. Oct. 1, 2018).

PURCHASE PRICE ADJUSTMENT

A purchase price adjustment clause is a tool intended to alter the contract price in response to one or more triggering events. Triggering events often involve factors that are beyond the parties' control. They can be anything that the parties deem likely to have a substantial or material impact on the value of the asset being purchased or the services being rendered. These clauses are often triggered post-closing. They allow parties to account for changing circumstances over the term of the agreement.

Purchase price adjustments are used frequently in the acquisition of power generation assets. Changes to subsidies, feed-in-tariffs, increased import duties, revision to amounts available for tax credit financing, plant capacity, and other events that alter the value of the project or project company are often the subject of price adjustment clauses.

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There may also be individual commodity or equipment price adjustments for items that are critical to a project. Those are more likely to be seen in a construction or EPC contract. Adjustments based on currency fluctuations are also sometimes utilized.

OTHER THEORIES OF CONTRACTUAL RELIEF

Parties may look to other theories for contractual relief. The concepts of frustration of purpose, commercial impracticability and impossibility of performance are three examples of such theories. Frustration of purpose may lie where an unforeseen event alters a party's main purpose for entering a contract, making the performance of the contract dramatically different from the performance originally anticipated. Importantly, both parties must have known of the principal purpose at the time the contract was made. Impracticability excuses a party from a specific duty outlined in a contract when that duty has become unreasonably difficult or too expensive to perform. Impossibility refers to a case where a specific contractual obligation becomes reasonably impossible to fulfill.

Frustration of purpose, impracticability, and impossibility are not easy theories to prove. The set of circumstances to which these concepts may apply are unusual and increased expense is typically not enough to sustain such a claim in most instances.

CONCLUSION

The changing US policy landscape, particularly with respect to imports and domestic energy regulations, could cause the cost to perform the contract and the expected benefits of the contract to be different than originally contemplated. For future contracts, parties should carefully consider whether to include contractual relief clauses aimed at excusing performance or altering the price of the bargain. For existing contracts, parties should review their rights carefully and determine whether they have additional contractual rights because of changes to laws and policies.

Due to the changing US policy landscape and the effects these changes may have on the costs and benefits of existing and future contracts, parties should be aware of potential contractual relief clauses in those agreements.

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KEY CONTACTS



THOMAS G. ALLEN
PARTNER

WASHINGTON, DC
+1.202.778.9188
THOMAS.ALLEN@KLGATES.COM



SLADE SEVIER
PARTNER

NASHVILLE
+1.615.780.6740
SLADE.SEVIER@KLGATES.COM



MARLA TUN RESCHLY
PARTNER

CHARLOTTE
+1.704.331.7417
MARLA.RESCHLY@KLGATES.COM



ERIC D. BRILL
ASSOCIATE

PITTSBURGH
+1.412.355.6335
ERIC.BRILL@KLGATES.COM

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