PROGRAM MATERIALS
Program #30100
April 6, 2020

Business in the Age of Covid-19: Contracts Under Economic Distress and Uncertainty

Celesq® AttorneysEd Center
www.celesq.com

5301 North Federal Highway, Suite 180, Boca Raton, FL 33487
Phone 561-241-1919 Fax 561-241-1969

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

CELESQ ATTORNEYSEDCENTER
WEBINAR

Live Webinar
April 6, 2020
12:00 pm

BUSINESS IN THE AGE OF COVID-19: CONTRACTS UNDER ECONOMIC DISTRESS AND UNCERTAINTY

Disclaimer

The views expressed by the participants in this program are not those of the participants' employers, their clients, or any other organization. The opinions expressed do not constitute legal advice, or risk management advice. The views discussed are for educational purposes only, and provided only for use during this session.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

SPEAKER:

Jeremy E. Deutsch is a shareholder in Anderson Kill's New York office and is Chair of the firm's Corporate and Securities group. Jeremy has over 20 years' experience in business law, including transactional and day to day legal counseling as well as complex corporate and commercial litigation and arbitration.

In 2018, Jeremy was selected as a member of Law360's Banking editorial advisory board.

Jeremy's corporate practice embraces all areas of corporate transactional and advisory roles. In transactional work, he has represented clients in mergers/acquisitions, sales/leases, employment agreements/terminations, and all manner of commercial transactions, including private investment deals, technology transactions, and private equity. In advisory work, he acts as general counsel to a number of different businesses and provides counsel and advice to established businesses and startups on corporate relationship creation and architecture; corporate governance, including disputes between partners and advising Boards of Directors; and day to day business issues.

In litigation, Jeremy has represented clients and tried cases to verdict and arbitrated matters to final award in matters involving large frauds, breaches of fiduciary duty, breaches of contract and joint venture agreements, complex financial instrument and securities litigation, real estate lending, shareholder derivative suits, stock option litigation, construction disputes, employment disputes, and violations of restrictive covenant agreements by employees. He has experience in cross-border litigation in the United States, Canada and in England, including matters involving securities fraud, trade secret theft, copyright and trademark infringement, commodities fraud, investment fraud, various types of financial fraud, employee theft of high-tech products, officer liability/mandatory indemnification issues, RICO claims, employment contracts and management buyout litigation. He has been lead trial counsel in United States Federal Courts, New York State courts, the state courts of other states, and private dispute resolution in the American Arbitration Association, FINRA, JAMS, and the International Chamber of Commerce International Court of Arbitration. Jeremy also has extensive federal and state court injunction experience.

Jeremy's training as a trial lawyer gives him an unusual perspective on corporate matters, as he has seen and litigated the results of failed deals and ventures. He views corporate work as a form of centralized risk management, insofar as well-designed contracts on other corporate documents foster productive partnerships and can help prevent disputes and litigation.

Jeremy E. Deutsch, Esq.
Shareholder
Anderson Kill
(212) 278-1172
jdeutsch@andersonkill.com

SPEAKER:

Rhonda D. Orin is the managing partner of the firm's Washington, D.C. office. Rhonda has recovered more than $1 billion for policyholders nationwide, including first-party property damage and business interruption claims, cyber liability, third-party liability claims and directors & officers liability. She has been lead counsel in multiple jury and bench trials, argued before the highest courts of several states, and appeared in cases before U.S. Supreme Court.

Rhonda is a Fellow of the American Bar Foundation, an honor given to less than 1% of attorneys. Her skills are recognized by Chambers, the Legal 500, the D.C. Women's Bar Association, Best Lawyers, Super Lawyers and others. She also is the author of "Making Them Pay: How to Get the Most from Health Insurance and Managed Care" (St. Martin's Press 2000).

COVID-19 VIRUS – CHANGING EVERYTHING

Oil & Gas industry + Add to myFT

Global petrol demand to plunge as US stops driving

Refineries set to shut as consumption falls to levels from 1970s Nixon era

FGE, an energy consultancy, said petrol demand in the US alone would fall almost 5m barrels a day next month, equivalent to a 5 per cent drop in global oil demand. World oil demand is forecast to fall by an unprecedented 20m-25m barrels a day, a quarter of normal daily consumption.

“It’s like the entirety of Europe, Africa and the Middle East combined stopped driving,” said Cuneyt Kazokoglu, FGE’s head of oil demand, about the drop in petrol usage in the US.

Insurance ✓ Added

Life insurers braced for hit as bond market buckles

Rising death toll is not biggest issue facing sector as coronavirus outbreak worsens

FTfm M&G Investments PLC + Add to myFT

M&G under pressure as investors flee flagship bond fund

Richard Woolnough's Optimal Income fund has shrunk about a fifth in coronavirus sell-off

The highest-rated triple A tranches of US CMBS have blown out to a yield of 3.6 percentage points above benchmark swap rates, from below 1 percentage point at the start of the year, according to data from Trepp. Lower-rated, triple B tranches have risen from less than 4 percentage points above swaps, to over 11 percentage points.

Capital markets + Add to myFT

CMBS investors seek relief from the Federal Reserve

Yields on private-label deals have moved higher in recent weeks, sparking anxiety

Insurance industry could be ‘in jeopardy’ over virus claims, warns Lloyd’s chair

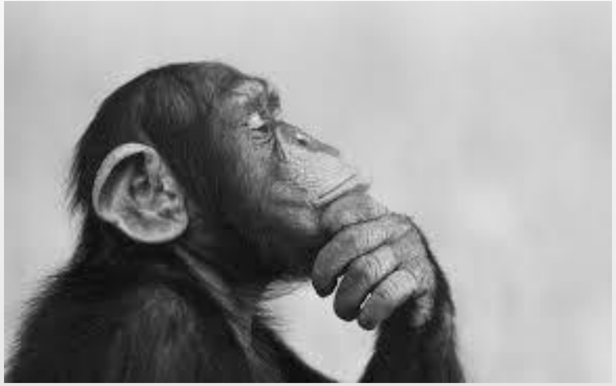
US and UK urge groups to pay out even though many policies do not cover outbreak

One B-rated tranche of a CMBS deal backed by a Hilton hotel in Honolulu has fallen from over 100 cents on the dollar at the start of the month to about 43 cents on the dollar on Thursday. “Clearly no one is going to a hotel at this point unless they have to,” said John Sim, an analyst at JPMorgan.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

SOME CHANGES TO THINK ABOUT

- Projected economic impact
- Global supply chain impact
- Ripple effects
- Travel bans and shipment
- Links between lock downs and defaults



WHAT CAN YOU DO FOR YOUR CLIENTS?

- Courts really don’t like it when you fail to perform a contract.

- Courts really don’t like to excuse performance and leave a party without a remedy other than in the most extraordinary circumstances

- New York Court of Appeals said it very well: contracts allocate risk.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

"Generally, once a party to a contract has made a promise, that party must perform or respond in damages for its failure, even when unforeseen circumstances make performance burdensome; until the late nineteenth century even impossibility of performance ordinarily did not provide a defense (Calamari and Perillo, Contracts § 13–1, at 477 [2d ed. 1977]). While such defenses have been recognized in the common law, they have been applied narrowly, due in part to judicial recognition that the purpose of contract law is to allocate the risks that might affect performance and that performance should be excused only in extreme circumstances (*see,* Wallach, *The Excuse Defense in the Law of Contracts: Judicial Frustration of the U.C.C. Attempt to Liberalize the Law of Commercial Impracticability,* 55 Notre Dame Law 203, 207 [1979])."

Kel Kim Corp. v. Cent. Markets, Inc., 70 NY2d 900, 902 [1987]

Puts everyone in a difficult position given the pandemic, no?

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

HELP THEM UNDERSTAND THEIR CONTRACTS

- Go over the terms that permit contracts to be modified in an emergency
- Consider auditing most important contracts to get out in front
- Read all of your insurance policies carefully

CONCEPTS TO DISCUSS

- Doctrine of Adequate Assurances and Anticipatory Repudiation
- Force Majeure
- Common law impossibility
- Temporary Impracticability
- Common law frustration
- Beware Good Faith and Fair Dealing
- Insurance coverage for business interruption
- Remedies

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

BEYOND THE SCOPE OF TODAY

- Updating public company disclosures;
- Updating private placement memoranda;
- Existing investor disclosures; for instance, do you have to tell the world if a key person has contracted the virus?
- What happens if you have to do mass furloughs or layoffs and even what is the difference between a furlough and a layoff?
- What happens if you have to meet milestones for venture cap funding commitments to be triggered and you can't?
- Material Adverse Change clauses – they are all too specific but if you are in a deal that you don't want to complete, you should examine that clause carefully.
- Are your reps and warranties or covenants now changed or implicated?
- Do you have notice requirements under a contract that may be tripped?
- If you assert any of these defenses to any contracts or contract claims then likely you have to give notice within a certain period of time.
- Do you have to give notice to a lender? Do you have a factor agreement?
- Is there a guaranty somewhere? Are agreements linked such that you face cross default obligations?

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

DOCTRINE OF ADEQUATE ASSURANCES

- Arises out of UCC for sale of goods and anticipatory repudiation concepts
- UCC concepts extended by NY Court of Appeals in *Norcon* and progeny
  - **Key case**: *Norcon Power Partners, L.P. v. Niagara Mohawk Power Corp.*, 92 N.Y.2d 458, 462–68, 705 N.E.2d 656, 659–62 (1998)

Ask, before going down this road:

- What exactly is the performance that you think you are entitled to get assurances on? Be exact in your analysis.
- Are you able to show you are ready and willing to perform your obligations?
- Not applied in numerous situations – loan agreements where delay was matter of months or borrower was merely insolvent.

Before we can discuss adequate assurances, we need to understand *anticipatory repudiation of a contract.*

- "Anticipatory repudiation occurs when,
- before the time for performance has arisen,
- A party to a contract declares his intention not to fulfill a contractual duty." *Lucente* v. *Int'l Bus. Machines Corp.*, 310 F.3d 243, 258 (2d Cir. 2002).
- Anticipatory repudiation "can be **either a statement** by the obligor to the obligee indicating that the obligor will commit a breach.
- That would of itself give the obligee a claim for damages for total breach.
- **Or a voluntary affirmative act** which renders the obligor unable or apparently unable to perform without such a breach." *Princes Point LLC* v. *Muss Dev. L.L.C.*, 30 N.Y.3d 127, 133 (2017) (quoting *Norcon Power Partners* v. *Niagara Mohawk Power Corp.*, 92 N.Y.2d 458, 463 (1998)).
- "For an anticipatory repudiation to be deemed to have occurred, the expression of intent not to perform by the repudiator must be '**positive and unequivocal**.' " *Princes Point LLC*, 30 N.Y.3d at 133 (quoting *Tenavision, Inc. v. Neuman*, 45 N.Y.2d 145, 150 (1978)).
- When confronted with an anticipatory repudiation, the non-repudiating party has **two mutually exclusive options**. It may either (i) "elect to treat the repudiation as an anticipatory breach and seek damages for breach of contract, thereby terminating the contractual relation between the parties," or (ii) "continue to treat the contract as valid and await the designated time for performance before bringing suit." *Lucente*, 310 F.3d at 258.

<u>Ricatto v. M3 Innovations Unlimited, Inc.</u>, No. 18 CIV. 8404 (KPF), 2019 WL 6681558, at *7 (S.D.N.Y. Dec. 6, 2019) (*Princes* and *Norcon* are key NY cases).

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

- But you're not sure you have a statement or a voluntary act. What do you do?
- You may be in breach of contract, and liable later, if a court disagrees.
- The *Ricatto* case cited above found a failure to plead anticipatory repudiation on a loan where the borrower was insolvent – no unequivocal statement that the borrower couldn't pay.
- But you continue to perform – that's a risk, too.
- **RISK**: "If, on the other hand, the promisee continues to perform after perceiving an apparent repudiation, and it is subsequently determined that an anticipatory repudiation took place, the promisee may be denied recovery for post-repudiation expenditures because of his or her failure to avoid those expenses as part of a reasonable effort to mitigate damages after the repudiation." *Norcon*
- "The Uniform Commercial Code settled on a mechanism for relieving some of this uncertainty. It allows a party to a contract for the sale of goods to demand assurance of future performance from the other party when reasonable grounds for insecurity exist (*see,* UCC 2–609; II Farnsworth, Contracts § 8.23). When adequate assurance is not forthcoming, repudiation is deemed confirmed, and the nonbreaching party is allowed to take reasonable actions as though a repudiation had occurred (*see,* 4 Anderson, Uniform Commercial Code § 2–609:3 [3d ed. 1997 rev.])." *Norcon*
- The Court of Appeals held that a modest extension, at a snail's pace, as is appropriate with an extension, was warranted.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

THE RULE FROM *NORCON*

Considering the UCC demand for assurances mechanism, the Court held that:

- “It should apply to:

  (1) the type of long-term commercial contract between corporate entities entered into by Norcon and Niagara Mohawk here,

  (2) which is complex and not reasonably susceptible of all security features being anticipated, bargained for and incorporated in the original contract.

  (3) Norcon's performance, in terms of reimbursing Niagara Mohawk for credits, is still years away.

  (4) In the meantime, potential quantifiable damages are accumulating and Niagara Mohawk must weigh the hard choices and serious consequences that the doctrine of demand for adequate assurance is designed to mitigate.

- This Court needs to go no further in its promulgation of the legal standard as this suffices to declare a dispositive and proportioned answer to the certified question.”

Recognized in New Hampshire: <u>McNeal v. Lebel</u>, 157 NH 458, 463, 953 A2d 396, 401 [2008] (grounded it on extension of good faith and fair dealing concepts).

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

RESTATEMENT (SECOND) OF CONTRACTS § 251 (1981)

How the restatement incorporated the UCC concept:

1) Where reasonable grounds arise to believe that the obligor will commit a breach by non-performance that would of itself give the obligee a claim for damages for total breach under § 243, the obligee may demand adequate assurance of due performance and may, if reasonable, suspend any performance for which he has not already received the agreed exchange until he receives such assurance.

2) The obligee may treat as a repudiation the obligor's failure to provide within a reasonable time such assurance of due performance as is adequate in the circumstances of the particular case.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

THE RULE FROM *NORCON*

Elucidated some time later by an important SDNY bankruptcy decision:

An obligor's statement or voluntary act may be equivocal, and not provide clear grounds to declare an immediate breach. In that situation, the obligee declares a repudiation at his peril. Or the obligor may say or do nothing that suggests his unwillingness or inability to perform, but **the circumstances may nonetheless indicate that performance is not likely**. In these situations, the obligee is entitled—but not required—to seek assurances from the obligor that he will perform when the time for performance arrives. Restatement (Second) of Contracts § 251(1). If the demand is proper and reasonable assurance is not forthcoming, the obligee may treat the failure as a repudiation. *Id.,* at § 251(2).

In re Asia Glob. Crossing, Ltd., 326 B.R. 240, 250 (Bankr. S.D.N.Y.), adhered to in part on reargument, 332 B.R. 520 (Bankr. S.D.N.Y. 2005)

What's the lesson? You may have to ask and you probably shouldn't assume. *Princes Point* held that the filing of a lawsuit against vendors did not constitute anticipatory repudiation. Even if you're not entitled to ask, you're probably better off doing so.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

FORCE MAJEURE

“Generally, a force majeure event is an event beyond the control of the parties that prevents performance under a contract and may excuse nonperformance (*see Kel Kim Corp. v. Central Mkts.,* 70 N.Y.2d 900, 902, 524 N.Y.S.2d 384, 519 N.E.2d 295 [1987])” *Beardslee v. Inflection Energy, LLC*, 25 N.Y.3d 150, 154, 31 N.E.3d 80, 81–82 (2015)

- Will your performance be excused? Depends. Courts don’t like to excuse performance.

- Start with the contract language. Did the parties provide a definition in a contract? Who has an excuse for non-performance? Is the excuse limited?

- (If the contract is silent, you turn to other doctrines like impossibility or frustration of purpose).

- Contracts for sale of goods under UCC 2-615(a): unforeseen circumstances not within contemplation of parties at time of contracting/
  - For instance, Coronavirus: government action / inability to perform directly due to the virus
- All may be deeply fact intensive -- so how are you going to demonstrate this?
  - Keeping good records, among other things
- Do you have alternatives open to you or is this the only choice?
  - Let’s not fall into the “efficient breach” trap

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

RULE: NARROW DEFENSE LIMITED TO THE CONTRACT LANGUAGE

[C]ontractual *force majeure* clauses—or clauses excusing nonperformance due to circumstances beyond the control of the parties—under the common law provide a similarly narrow defense. Ordinarily, only if the *force majeure* clause specifically includes the event that actually prevents a party's performance will that party be excused. (*See, e.g., United Equities Co. v. First Natl. City Bank,* 41 N.Y.2d 1032, 395 N.Y.S.2d 640, 363 N.E.2d 1385; Squillante & Congalton, *Force Majeure,* 80 Com.L.J. 4 [1975].) Here, of course, the contractual provision does not specifically include plaintiff's inability to procure and maintain insurance. Nor does this inability fall within the catchall "or other similar causes beyond the control of such party." The principle of interpretation applicable to such clauses is that the general words are not to be given expansive meaning; they are confined to things of the same kind or nature as the particular matters mentioned (*see,* 18 Williston, Contracts § 1968, at 209 [3d ed. 1978]).

The clause reads: "If either party to this Lease shall be delayed or prevented from the **performance** of any obligation through no fault of their own by reason of labor disputes, inability to procure materials, failure of utility service, restrictive governmental laws or regulations, riots, insurrection, war, adverse weather, Acts of God, or other similar causes beyond the control of such party, the **performance** of such obligation shall be excused for the period of the delay."

Kel Kim Corp. v. Cent. Markets, Inc., 70 NY2d 900, 902-03 [1987]

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

GOLDSTEIN V. ORENSANZ EVENTS LLC, 146 A.D.3D 492, 44 N.Y.S.3D 437 (1ST. DEPT. 2017)

- The bride booked a wedding venue that was condemned by the Dept. of Buildings in NYC shortly before the wedding. She sued for the consequential damages suffered by having to find a last-minute replacement. The owner asserted the defense of *force majeure*.
- The clause in the contract provided: "if the event must be canceled because of 'an order of the Federal, State, or City government or for any reason beyond Owner's control," the client's sole remedy is either another date for the event or a refund'.
- The Court denied summary judgment to the Owner and the reason will be instructive:

  (1) The purpose of force majeure clauses is "to limit damages ... where the reasonable expectation of the parties and the performance of the contract have been frustrated by circumstances beyond the control of the parties" (string cite omitted).

  (2) "Thus, the clause must be interpreted as if it included an express requirement of unforeseeability or lack of control. The vacate order's citation to defendants' failure to maintain the building and the engineer's letter citing overcrowding as a possible cause for the structural failure present issues of fact whether the failure was foreseeable or within defendants' control and therefore whether the force majeure clause applies in this case."
- Summary judgment denied. Case sent back for discovery into the cause of the structural failure.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

IMPOSSIBILITY

- "Impossibility excuses a party's performance only when the destruction of the subject matter of the contract or the means of performance makes performance objectively impossible. Moreover, the impossibility must be produced by an unanticipated event that could not have been foreseen or guarded against in the contract (*see, 407 E. 61st Garage v. Savoy Fifth Ave. Corp.,* 23 N.Y.2d 275, 296 N.Y.S.2d 338, 244 N.E.2d 37; *Ogdensburg Urban Renewal Agency v. Moroney,* 42 A.D.2d 639, 345 N.Y.S.2d 169)."

  Kel Kim Corp. v. Cent. Markets, Inc., 70 NY2d 900, 902 [1987]

- The excuse of impossibility is generally "limited to the destruction of the means of performance by an act of God, *vis major,* or by law" (*407 E. 61st Garage v. Savoy Fifth Ave. Corp.,* 23 N.Y.2d 275, 281, 296 N.Y.S.2d 338, 244 N.E.2d 37 [1968]).

  Kolodin v. Valenti, 115 AD3d 197, 200 [1st Dept 2014] Sounds like force majeure, no? Act of God. Here a stipulation precluded all contact between the parties and rendered future contractual performance thereby impossible.

- Defendants further argue that the contract was "impossible" to perform due to an eviction proceeding. However, the contract anticipated an eviction proceeding (*see Kel Kim Corp. v. Central Mkts.,* 70 N.Y.2d 900, 524 N.Y.S.2d 384, 519 N.E.2d 295 [1987]). Moreover, performance of a contract is not excused where impossibility is occasioned by financial difficulty or economic hardship (*407 E. 61st Garage v. Savoy Fifth Ave. Corp.,* 23 N.Y.2d 275, 281, 296 N.Y.S.2d 338, 244 N.E.2d 37 [1968])

  Valenti v. Going Grain, Inc., 159 AD3d 645, 645 [1st Dept 2018] So impossibility of performance under a lease was not impossible simply because the commercial enterprise was evicted and now claimed that it couldn't pay rent.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

IMPOSSIBILITY (CONT'D)

- Paragraph 15.2 of the contract conclusively disproves the theory's applicability here. Plaintiffs rely on a case in which the very subject matter of the contract was destroyed, making performance impossible (*see Stewart v. Stone,* 127 N.Y. 500, 28 N.E. 595 [1891]). However, where performance is possible, albeit unprofitable, the legal excuse of impossibility is not available (*see* ***6** *407 E. 61st Garage v. Savoy Fifth Ave. Corp.,* 23 N.Y.2d 275, 282, 296 N.Y.S.2d 338, 244 N.E.2d 37 [1968]).

  Warner v. Kaplan, 71 AD3d 1, 5-6 [1st Dept 2009] – death won't cut it

- The Supreme Court properly determined that RW failed to show that it was entitled to rescission of the subject contract based on the doctrine of impossibility of performance. " '[T]he law of impossibility provides that performance of a contract will be excused if such performance is rendered impossible by intervening governmental activities, but only if those activities are unforeseeable' " (*Pleasant Hill Developers, Inc. v. Foxwood Enters., LLC,* 65 A.D.3d 1203, 1206, 885 N.Y.S.2d 531, quoting *Matter of A & S Transp. Co. v. County of Nassau,* 154 A.D.2d 456, 459, 546 N.Y.S.2d 109; *see Kel Kim Corp. v. Central Mkts.,* 70 N.Y.2d 900, 902, 524 N.Y.S.2d 384, 519 N.E.2d 295). Contrary to RW's contention, a party seeking to rescind a contract must show that the intervening act was unforeseeable, even if the intervening act consisted of the actions of a governmental entity or the passage of new legislation (*see Pleasant Hill Developers, Inc. v. Foxwood Enters., LLC,* 65 A.D.3d at 1206, 885 N.Y.S.2d 531; *Matter of A & S Transp. Co. v. County of Nassau,* 154 A.D.2d at 459, 546 N.Y.S.2d 109; *see also Four Asteria Realty, LLC v. BCP Bank of N.Am.,* 71 A.D.3d 822, 822–823, 897 N.Y.S.2d 487; *Inter–Power of N.Y. v. Niagara Mohawk Power Corp.,* 208 A.D.2d 1073, 1074, 617 N.Y.S.2d 562). Here, RW did not show that it was unforeseeable that a change in the Town's Zoning Code would render it impossible to subdivide the property as initially planned,

  RW Holdings, LLC v. Mayer, 131 AD3d 1228, 1230 [2d Dept 2015] government action changing the zoning should have been foreseeable and thus accounted for in the contract.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

DEFENSE OF TEMPORARY COMMERCIAL IMPRACTICABILITY

- If the nature and scope of the credit crisis were more limited or a mere economic downturn, John Hancock's argument that the crisis was foreseeable or that Hoosier Energy should have protected itself better might be more persuasive. However, the credit crisis facing the world's economies in recent months is unprecedented and was not foretold by the world's preeminent economic experts. The crisis certainly was not anticipated in 2002, when the deal between Hoosier Energy, Ambac, and John Hancock was being finalized. Retrospect will not assist John Hancock here, nor will an assertion that it was Hoosier Energy's responsibility to prepare for and guard against any imaginable commercial calamity. After all, "foreseeable" is different from "conceivable." *Specialty Tires,* 82 F.Supp.2d at 439, quoting John E. Murray, Jr., Murray on Contracts § 112 at 641 (3d ed. 1990) ("If 'foreseeable' is equated with 'conceivable', nothing is unforeseeable."). Hoosier Energy has come forward with evidence indicating that the obstacles it faced were not specific to Ambac but were the product of the credit crisis that effectively but temporarily froze the market for comparable credit products *at any price.* Those effects were not anticipated and could not have been guarded against.[5]

  Hoosier Energy Rural Elec. Co-op., Inc. v. John Hancock Life Ins. Co., 588 F. Supp. 2d 919, 932 (S.D. Ind. 2008), aff'd but criticized, 582 F.3d 721 (7th Cir. 2009)

DEFENSE OF TEMPORARY COMMERCIAL IMPRACTICABILITY (CONT'D)

- Temporary commercial impracticability excuses performance until circumstances have changed, plus a reasonable time afterwards:
  - Impracticability of performance or frustration of purpose that is only temporary suspends the obligor's duty to perform for the duration of the impracticability or frustration; it does not discharge the ultimate duty or prevent it from arising. Thus, temporary impracticability only relieves the promisor of an obligation to perform for as long as the impracticability lasts plus a reasonable time afterwards.
- 30 Williston on Contracts § 77:103 (4th ed. 2008); see also Restatement (Second) of Contracts § 269 (1981); *Specialty Tires of America,* 82 F.Supp.2d at 442 (applying doctrine to excuse performance temporarily); *Long Signature Homes, Inc. v. Fairfield Woods, Inc.,* 248 Va. 95, 445 S.E.2d 489, 491 (1994). New York law recognizes the doctrine of temporary commercial impracticability. See *Bank of Boston Int'l of Miami v. Arguello Tefel,* 644 F.Supp. 1423, 1427 (E.D.N.Y.1986) (recognizing doctrine but holding it did not apply after the obstacle to performance had been removed); *Bush v. Protravel Int'l, Inc.,* 192 Misc.2d 743, 746 N.Y.S.2d 790, 797–98 (Civ.Ct.2002) (applying doctrine based on interruptions in communication following September 11, 2001 terrorist attacks in New York).[4]

  Hoosier Energy Rural Elec. Co-op., Inc. v. John Hancock Life Ins. Co., 588 F. Supp. 2d 919, 931 (S.D. Ind. 2008), aff'd but criticized, 582 F.3d 721 (7th Cir. 2009)

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

FRUSTRATION

Warning: This is a tough one to use – neither death nor hurricanes have excused performance as *frustrated*

- In any event, this doctrine is a narrow one which does not apply "unless the frustration is substantial" (*Rockland Development Assocs. v. Richlou Auto Body, Inc.,* 173 A.D.2d 690, 691, 570 N.Y.S.2d 343 [1991]). In order to invoke this defense, the frustrated purpose must be so completely the basis of the contract that, as both parties understood, without it, the transaction would have made little sense (*see* Restatement (Second) of Contracts, § 265 [1981]).

  Crown IT Servs., Inc. v. Koval-Olsen, 11 A.D.3d 263, 265, 782 N.Y.S.2d 708, 711 (1st Dept. 2004)

- Similarly, although at first blush the general definition of "frustration of contract purpose" would seem to suit these circumstances, closer examination reveals that the defense cannot be applied here. "In order to invoke the doctrine of frustration of purpose, the frustrated purpose must be so completely the basis of the contract that, as both parties understood, without it, the transaction would have made little sense" (22A N.Y. Jur.2d, Contracts § 375). Since it is agreed that Altman was purchasing the apartment solely ****315** for her own residence, her death would, by this definition, frustrate the purpose of the contract. However, "the doctrine of frustration of purpose ... is not available where the event which prevented performance was foreseeable and provision could have been made for its occurrence" (*Matter of Rebell v. Trask,* 220 A.D.2d 594, 598, 632 N.Y.S.2d 624 [1995], citing *407 E. 61st Garage,* 23 N.Y.2d at 282, 296 N.Y.S.2d 338, 244 N.E.2d 37). Since the contract actually made explicit provision for the event of either party's death, the doctrine is not available here.

  Warner v. Kaplan, 71 AD3d 1, 6 [1st Dept 2009]

- The doctrine applies "when a change in circumstances makes one party's performance virtually worthless to the other, frustrating his purpose in making the contract" (Restatement [Second] of Contracts § 265, Comment *a*).

  PPF Safeguard, LLC v. BCR Safeguard Holding, LLC, 85 A.D.3d 506, 508, 924 N.Y.S.2d 391, 394 (1st Dept. 2011)

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

BEWARE GOOD FAITH AND FAIR DEALING

New York law imparts to every contract an implied covenant of good faith and fair dealing

Under New York law, "[i]mplicit in all contracts is a covenant of good faith and fair dealing in the course of contract performance." *Dalton v. Educ. Testing Svc.*, 663 N.E.2d 289, 291 (N.Y. 1995) (citing *Van Valkenburgh, Nooger & Neville v. Hayden Publ. Co.,* 281 N.E.2d 142, 144 (N.Y. 1972), *cert denied* 409 U.S. 875 (1972)). "This embraces a pledge that 'neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract.' " *Id.* at 291 (quoting *Kirke La Shelle Co. v. Armstrong Co.*, 188 N.E. 163, 167 (N.Y. 1933)). Put another way, "[t]he covenant of good faith and fair dealing, implied in every contract under New York law, 'includes an implied undertaking on the part of each party that he will not <u>intentionally and purposely</u> do anything to prevent the other party from carrying out the agreement on his part.' " *Lykins v. IMPCO Techs., Inc.*, No. 15 Civ. 2102 (PGG), 2018 U.S. Dist. LEXIS 111705, at *20 (S.D.N.Y. Mar. 6, 2018) (quoting *Kader v. Paper Software, Inc.*, 111 F.3d 337, 342 (2d Cir. 1997)) (emphasis in original). And, while the duty "includes a promise not to act arbitrarily or irrationally," *Dalton*, 663 N.E.2d at 291, "[a] plaintiff must show substantially more than evidence that the defendant's actions were negligent or inept." *Sec. Plans, Inc. v. CUNA Mut. Ins. Soc'y*, 769 F.3d 807, 817 (2d Cir. 2014) (citing *Behren v. Warren Gorham & Lamont*, 808 N.Y.S.2d 157, 158 (N.Y. App. Div. 2005)); *see also Thompson v. Advanced Armament Corp.*, 614 F. App'x 523, 525 (2d Cir. 2015) ("Acts done out of 'negligence' or 'ineptitude' are insufficient, as are intentional acts done without the purpose of cheating the plaintiff.") (quoting *Sec. Plans*, 769 F.3d at 817).

"The duty of good faith and fair dealing, however, is not without limits, and no obligation can be implied that 'would be inconsistent with other terms of the contractual relationship.' " *Dalton*, 663 N.E.2d at 291-92 (quoting *Murphy v. Am. Home Prods. Corp.,* 448 N.E.2d 86, 91 (N.Y. 1983)). In addition, "[t]he boundaries of the duty do not ... extend so far as to prevent a party from acting in its own interests even if the result is to incidentally lessen the value the other party expected to receive from the contract." *Gruppo, Levey & Co. v. ICOM Info. & Commc'ns., Inc.*, No. 01 Civ. 8922 (JFK), 2003 U.S. Dist. LEXIS 11213, at *28 (S.D.N.Y. July 12, 2003) (citing *M/A-Com Sec. Corp. v. Galesi*, 904 F.2d 134, 136 (2d Cir. 1990)). For this reason, "[t]he covenant will be breached only in a narrow range of cases." *Sec. Plans*, 769 F.3d at 817. Indeed, "a party who asserts the existence of an implied-in-fact covenant bears a heavy burden, [because] it is not the function of the courts to remake the contract agreed to by the parties, but rather to enforce it as it exists." *Lykins*, 2018 U.S. Dist. LEXIS 111705, at *21.

<u>HUNTINGTON TECHNOLOGY FINANCE, INC. f/k/a MACQUARIE EQUIPMENT FINANCE, INC. f/k/a MACQUARIE EQUIPMENT FINANCE, LLC, Plaintiff, v. GARETT ALAN NEFF, a/k/a GARY NEFF, JOHN MARK SCHMID, & DAVID KARL SCHMID, Defendants.</u>, No. 3:18-CV-01708 (VLB), 2020 WL 1430092, at *13 (D. Conn. Mar. 24, 2020)

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

REMEDIES

- Renegotiate! – best time to try to get new terms
- Forbearance requests
- Rescission or reformation
- Demand letters
- Directed Judgment actions
- Or, let's talk about insurance

INSURANCE POLICIES

- Read all of your insurance policies carefully
  - They are not all the same

- Give prompt notice to your insurers

COMMERCIAL PROPERTY POLICIES

- “All-Risk” versus “Named Peril”
- Property damage: costs to restore infected property
- Business Interruption: lost profits from shutdowns

"PHYSICAL LOSS OR DAMAGE"

- Usually require "physical loss or damage" to trigger coverage
- Insurers will argue physical damage = structural damage
- This will be a key issue that the courts will need to address

CORONAVIRUS AS PHYSICAL DAMAGE

- "Physical damage" = carpet fumes, carbon monoxide leaks, asbestos fibers, etc.

- *Gregory Packaging, Inc. v. Travelers Prop. Cas. Co. of Am.*, No. 2:12-04418, 2014 WL 6675934, at *7 (D.N.J. Nov. 25, 2014) (an ammonia discharge in a manufacturing facility constituted "direct physical loss of or damage to" the facility because it "physically rendered the facility unusable for a period of time").

- *Motorists Mut. Ins. Co. v. Hardinger*, 131 F. App'x 823, 825 (3d Cir. 2005) (bacteria contamination of a home's water supply could constitute a direct physical loss where the "functionality" of the property is "nearly eliminated or destroyed," or when it renders the property "useless or uninhabitable").

CORONAVIRUS AS PHYSICAL DAMAGE (CONT'D)

- *Oregon Shakespeare Festival Association v. Great American Insurance Company*, 2016 WL 327247 (D. Ore. June 7, 2016) (business entitled to BI coverage when it had to cancel performances at a theater due to smoke from wildfires that infiltrated the premises).

- *Port Auth. v. Affiliated FM Ins. Co.*, 311 F.3d 226, 236 (3d Cir. 2002) (the presence of large quantities of asbestos in the air of a building may constitute "physical loss or damage").

- *TRAVCO Ins. Co. v. Ward*, 715 F. Supp. 2d 699, 709 (E.D. Va. 2010), aff'd, 504 F. App'x 251 (4th Cir. 2013) (finding "direct physical loss" where "home was rendered uninhabitable by the toxic gases" released by defective drywall).

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

CORONAVIRUS AS PHYSICAL DAMAGE (CONT'D)

- *Mellin v. Northern Sec. Ins. Co.*, 167 N.H. 544, 550-51, 115 A.3d 799, 805 (N.H. 2015) (responding to plaintiffs' argument that "physical loss encompasses pervasive odors," the court concluded that "physical loss may include not only tangible changes to the insured property, but also changes that . . . exist in the absence of structural damage").

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

COUNTERVENING AUTHORITY

- Other cases will be relied upon by insurers to argue that the presence of a virus is <u>not</u> physical damage.

- E.g. *Source Food Tech., Inc. v. U.S. Fidelity & Guar. Co.*, (8th Cir. 2006) (policyholder's inability to transport its beef products across the U.S./Canada border due to concerns over mad cow disease did not trigger coverage resulting from physical damage).

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

ALSO "CONTAMINATION EXCLUSION"

- "**Contamination**, and any cost due to **contamination** including the inability to use or occupy property or any cost of making property safe or suitable for use of occupancy."

- Applies "unless directly resulting from other physical damage not excluded by the Policy."

- Contamination is defined in relevant part as "any condition of property due to the actual or suspected presence of any . . . virus."

"COMMUNICABLE DISEASE" EXTENSION

"If a described location owned, leased or rented by the Insured has the *actual not suspected presence* of communicable disease and access to such described location is limited, restricted or prohibited by:

a) An order of an authorized governmental agency regulating such presence of communicable disease; or

b) A decision of an Officer of the Insured as a result of such presence of communicable disease,

This Policy covers the Business Interruption Coverage loss incurred by the Insured during the Period of Liability *at such described location with such presence* of communicable disease"*

* Emphasis supplied

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

“CIVIL AUTHORITY” EXTENSION

“This Policy covers the Business Interruption Coverage loss incurred by the Insured during the Period of Liability if an order of civil or military authority prohibits access to a location provided such order is the direct result of physical damage of the type insured *at a location or within five (5) statute miles of it.”**

* Emphasis supplied

“INGRESS-EGRESS” EXTENSION

“This Policy covers the Business Interruption Coverage loss incurred by the Insured due to the necessary interruption of the Insured’s business when ingress to or egress from a described location(s) is physically prevented, either partially or totally, as a direct result of physical loss or damage *of the type insured* to property of the type insured *whether or not at a described location.”* *

* Emphasis supplied

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

ARE THERE SUBLIMITS?

- Yes -- all of these extensions usually have sublimits
- Narrowest: “Communicable Disease”
- Middle ground: “Civil Authority”
- Broadest: “Ingress/Egress”
- Policyholders should think carefully about how to frame their claims.

ANDERSON KILL
ATTORNEYS AND COUNSELORS AT LAW

WRAP UP

Any questions?

Feel free to reach out to us directly if you don't have the opportunity now to ask questions.

Thank you

THANK YOU.

Jeremy E. Deutsch, Esq.
Shareholder
Anderson Kill
(212) 278-1172
jdeutsch@andersonkill.com

Rhonda D. Orin, Esq.
Partner
Anderson Kill
(202) 416-6549
rorin@andersonkill.com