



PROGRAM MATERIALS

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Contractual Performance in The Age of Coronavirus: Force Majeure, Impossibility and Other Issues

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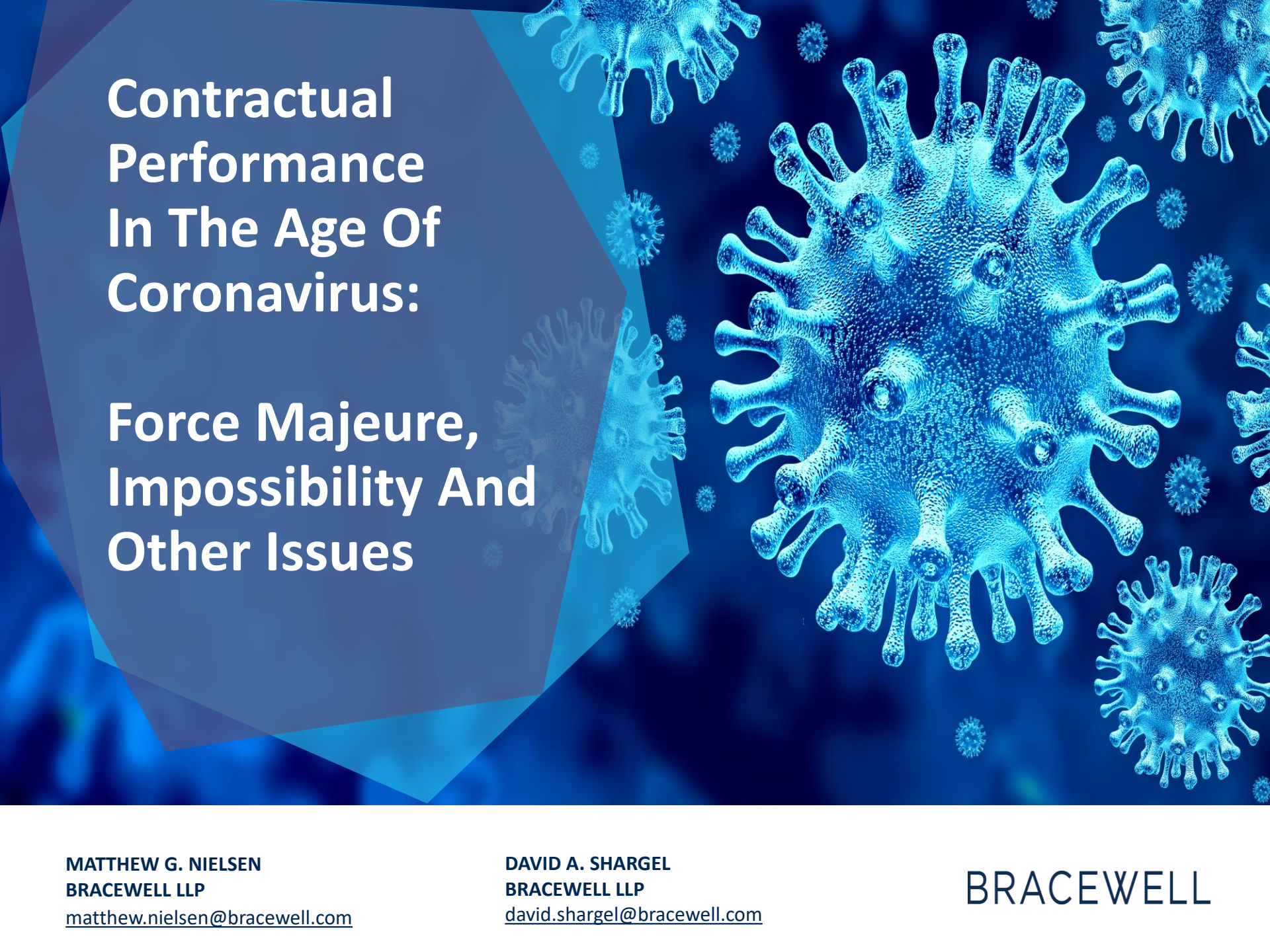
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Contractual Performance In The Age Of Coronavirus:

Force Majeure, Impossibility And Other Issues

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Introduction

- ▶ COVID-19 related issues are giving rise to a variety of commercial disputes
 - ▶ Business disruption caused by COVID-19 and accompanying government orders
- ▶ Today's presentation will focus on the following:
 - ▶ Force majeure
 - ▶ Alternative doctrines beyond force majeure
 - ▶ Issues in establishing/defending/litigating force majeure

Force Majeure - Generally

- ▶ Defined
 - ▶ Force majeure is an affirmative defense to excuse a party's failure to perform under a contract when the non-performance is not caused by circumstances within the party's reasonable control
 - ▶ It is difficult to find a universal definition because the contours of force majeure to a particular contract will generally be governed by the express language of the contract
- ▶ Legal sources
 - ▶ Contract clauses
 - ▶ Uniform Commercial Code
 - ▶ Contracts for the International Sale of Goods (CISG)

Force Majeure - Generally

- ▶ Typical contractual language that may be implicated by COVID-19
 - ▶ “Acts of God”
 - ▶ “Pandemic,” “disease,” “state of emergency”
 - ▶ Labor shortages
 - ▶ “Acts of government”
 - ▶ Not caused by fault or negligence of party
 - ▶ Catch-all language
- ▶ Other contract provisions
 - ▶ Expressly or impliedly unilateral language
 - ▶ Delays, limitations of remedies, non-refundable payments
 - ▶ Termination for (alleged) cause

Force Majeure - Generally

- ▶ UCC
 - ▶ Excuses seller's performance where: performance as agreed has been made **impracticable** by the occurrence of a contingency the non-occurrence of which was a **basic assumption** on which the contract was made or by compliance in good faith with any **applicable foreign or domestic governmental regulation or order** whether or not it later proves to be invalid
 - ▶ Requires allocation of performance among customers "in any manner which is fair and reasonable"
- ▶ Contracts for the International Sale of Goods (CISG) Art 79 provides for excuse of performance
 - ▶ Excuses performance for "impediment beyond [the party's] **control**" if the party "could not reasonably be expected to have taken the impediment into **account**" or "to have **avoided** or **overcome** it or its consequences"
 - ▶ Exceptions are made for third party performance

Force Majeure - Generally

- ▶ **Common principles used in enforcing force majeure provisions**
 - ▶ Identifying triggering event -- contractual force majeure provisions will be construed narrowly by courts
 - ▶ Even if there is a triggering event, courts generally require that performance has become impossible, not merely more difficult or expensive
- ▶ **Causation**
 - ▶ The triggering event must direct cause the inability to perform
- ▶ **“Catch-all” language**
 - ▶ Ejusdem Generis
 - ▶ Unforeseeability requirement

Force Majeure - Generally

▶ Notice

- ▶ Most contracts have notice provisions, both from timing and substance
 - ▶ Many contracts will contemplate notice of the “force majeure event” whether or not the impacts on performance have yet occurred
- ▶ Codified force majeure provisions also typically contain notice provisions
- ▶ Courts will interpret a lack of notice as a condition precedent to the affirmative defense of a force majeure

Force Majeure - COVID-19

▶ Triggering Event

- ▶ Does the contractual provision include specific triggering event?
 - ▶ Many older contracts do not include language such as “pandemic,” “disease,” “epidemic,” etc.
- ▶ **Is COVID-19 an “act of God”?**
 - ▶ Traditionally, the phrase contemplates force of nature, like earthquakes, tornados, floods
 - ▶ Black’s Law Dictionary -- “[a]n overwhelming, unpreventable event caused exclusively by forces of nature, such as an earthquake, flood, or tornado.”
 - ▶ “If there be any co-operation of man, or any admixture of human means, the injury is not, in a legal sense, the act of God.” *Michaels v. New York Cent. R. Co.*, 30 N.Y. 564, 571 (1864).

Force Majeure - COVID-19

- ▶ **“Act of Government” or “Illegal”**

- ▶ Stay-at-home orders

- ▶ Essential versus non-essential businesses

- ▶ What is coming as orders are modified, loosened?

- ▶ **Labor shortage**

- ▶ May not include shortage of own employees

- ▶ Recent meat processing plant closures have cause supply shortages

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Force Majeure - COVID-19

▶ **Reduced demand as a triggering event**

- ▶ Market forces are typically not a force majeure triggering event
- ▶ In the context of a demand drop triggered by COVID-19, they may be

▶ **Catch-all provisions**

- ▶ If in jurisdiction that requires event within catch-all to be unforeseeable
 - ▶ Some argue that pandemics inevitable based on history (i.e., 1918 Spanish Flu)
 - ▶ Contracts entered into after more recent outbreaks (i.e., 2005 SARS or 2009 H1N1)

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Force Majeure - COVID-19

▶ Foreseeability

- ▶ Courts may engage in a foreseeability analysis, depending on the circumstances.
 - ▶ E.g. *Goldstein v. Orensanz Events, LLC*, 146 A.D.3d 492 (1st Dep't 2017)
 - ▶ Wedding venue shut down by order of NYC DOB.
 - ▶ Defendants (owner of building) invoked force majeure clause, which included government orders as a triggering event.
 - ▶ But the court denied summary judgment, finding that a factual issue remained as to whether the DOB order was foreseeable, given Defendants' prior failure to maintain building.
 - ▶ “While, as the motion court found, the clause as written applies to any cancellation pursuant to a government order regardless of whether the order was unforeseeable or outside defendants' control, ***it must be interpreted in light of the purpose of force majeure clauses, '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.'***”

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Force Majeure - COVID-19

▶ Causation

▶ Direct versus indirect

- ▶ Direct – stay-at-home order effectively shuts down a party's manufacturing operation such that it cannot provide supplies to counterparty
- ▶ Indirect – quarantine rules in China disrupts normal supply of component used in manufacturing products

▶ Event cannot be result of party's own negligence or fault

- ▶ Prior to widespread stay-at-home orders, some companies chose to take proactive measures that, while perhaps socially responsible, were not required
 - ▶ Example – cancellation of international travel to secure component manufacturer
- ▶ As preventative measures become more known, will claims of "fault" increase?

Force Majeure - COVID-19

▶ **Defining affected time period**

- ▶ Performance may be excused only during time in which event causes performance impossibility
 - ▶ Differing stay-at-home orders among varying jurisdictions with differing effects on a party's operations

▶ **Opportunistic use of force majeure**

- ▶ COVID-19 is causing large-scale economic hardship for many companies
- ▶ Companies are increasingly looking to use force majeure to excuse performance under contracts that are no longer economically beneficial

Alternative/Novel Theories– COVID-19

▶ **Impossibility and impracticability**

- ▶ Common law doctrine(s) permitting narrowly-defined excuse from performance
- ▶ Excuse for impossibility or impracticability is a strict standard
- ▶ Not available when one party to the contract assumed the risk
- ▶ Some cases of ***impossibility*** are easy; supervening circumstances make performance objectively impossible
 - ▶ Providing a service on a date certain that is illegal under state or local stay-at-home order
- ▶ In other cases, ***impracticability*** exists where “*extreme, unreasonable, and unforeseeable hardship due to an unavoidable event or occurrence*”
 - ▶ More than mere change in degree of difficulty or expense
 - ▶ May not be available where the contract already addresses force majeure

Alternative/Novel Theories– COVID-19

▶ Frustration of purpose

▶ Requires the following:

- ▶ A change in circumstances that;
- ▶ Makes one party's performance virtually worthless to the other;
- ▶ Thereby frustrating that party's purpose in making the contract.
- ▶ The event must be unforeseen, and must neither be caused by nor within the avoidance or control of the party.
- ▶ **The doctrine may be a better fit than impossibility or force majeure where performance or payment is not "impossible," but circumstances still warrant relief from performance.**

Alternative/Novel Theories— COVID-19

- ▶ Some tenants have already tried...

Case 1:20-cv-03838-NRB Document 4 Filed 05/18/20 Page 1 of 8

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

VENUS OVER MANHATTAN ART LLC.,

-against-

980 MADISON OWNER LLC

Plaintiff
Defendant.

Venus Over Manhattan Art LLC (“Plaintiff”), by and through its attorneys, Margolin & Pierce, Attorneys at Law, as and for its Complaint against 980 Madison Owner, LLC (“Defendant”), alleges as follows:

SUMMARY OF CLAIM

1. This is a suit for a **declaratory judgment** against Defendant Madison Owner LLC seeking a declaration that as a result of the COVID-19 pandemic and Governor Andrew Cuomo’s Executive Orders resulting in the **mandatory closure** of Plaintiff’s business, **the purpose of the lease was frustrated** and plaintiff lawfully terminated its lease with Defendant effective April 1, 2020. Alternatively, Plaintiff seeks rescission of the lease based on impossibility of performance. In addition, Plaintiff seeks monetary damages against Defendant as a result of Defendant’s declaring a default under the terms and conditions of the “Lease” and wrongfully seizing Plaintiff’s security deposit in the amount of \$365,000, based upon Plaintiff’s failure to pay Defendant the April fixed monthly rent and additional rent purportedly due under the lease.

Gallery Sues Landlord, Claiming Covid-19 Shutdown Voids Lease

The lawsuit contends that since the Venus Over Manhattan gallery is closed by government orders during the pandemic, the lease should be terminated.

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Making or Defending the Claim

▶ **Pre-suit best practices**

- ▶ Parties seeking to invoke force majeure provision
 - ▶ Provide notice early even if not required
 - ▶ Communicate with counterparty – agreed substituted performance, waiver, etc.
 - ▶ Keep detailed, centralized records related to non-performance, including:
 - ▶ Timeline of events leading to inability to perform
 - ▶ Relevant government orders and pronouncements
 - ▶ Progression of force majeure event
 - ▶ Efforts to avoid event or find alternative means for performance
 - ▶ Negotiations efforts
- ▶ **Be aware, courts will view this as an equitable or quasi-equitable relief**

Making or Defending the Claim

▶ **Pre-suit best practices**

- ▶ Parties seeking to rebut or avoid force majeure
 - ▶ Respond to any notice; keep responses realistic, professional and performance-oriented
 - ▶ Communicate with counterparty – agreed substituted performance, waiver, etc.
 - ▶ Keep detailed, centralized records related to non-performance, including:
 - ▶ Timeline of events that might provide counter-narrative for claimed force majeure
 - ▶ Relevant government orders and pronouncements
 - ▶ Efforts to avoid event or find alternative means for performance
 - ▶ Negotiations efforts
 - ▶ Damages or losses incurred in non-performance
- ▶ **Be aware, courts will view this as an equitable or quasi-equitable relief**

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Making or Defending the Claim

- ▶ **Bringing the Force Majeure Claim to a Head**
 - ▶ Contractual pre-suit negotiation process/period?
 - ▶ Self-help non-performance
 - ▶ Leading to claims of breach
 - ▶ Leading to anticipatory breach
 - ▶ Other contract remedies
 - ▶ Declaratory judgment action
 - ▶ Suing (or being sued) for breach
 - ▶ Force majeure as an affirmative defense
 - ▶ Choice of law, venue and arbitration provisions

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Making or Defending the Claim

- ▶ **Other Issues in litigating force majeure claims**
 - ▶ Will parol evidence be relevant and admissible?
 - ▶ Document retention policies and suspension
 - ▶ Resurrecting the negotiations (if any) of low-priority provisions
 - ▶ The “relevance” of unrelated performance problems
 - ▶ Dut(ies) to mitigate damages on both sides
 - ▶ Availability of courts in the short- and long-term

Examples of COVID-19 Force Majeure Litigation

- ▶ *E2W, LLC v. Kidzania Operations, S.A.R.L.*, No. 20-cv-02866 (SDNY April 4, 2020)
- ▶ Franchisee (E2W) agreed to open several Kidzania amusement parks in the United States
- ▶ E2W claims that COVID-19 prevented it from opening parks and from obtaining additional financing
- ▶ Kidzania claims default and seeks to terminate franchise agreement
- ▶ E2W seeks preliminary injunction

“Force Majeure” means an event beyond the reasonable control of the Parties, including, but not be limited to, riots, civil commotion, wars, hostilities between nations, laws, governmental orders or regulations (including delays in governmental approvals despite, in the case of Licensee, its commercially reasonable efforts to overcome such delays as reflected in demonstrable evidence, but in such case subject to Section 18.5), embargoes, actions by government or by political sector(s) of their respective countries, acts of God such as earthquakes, floods or storms, fires, explosions, strikes, acts of terrorism or sabotage. Notwithstanding the foregoing, any government imposed restriction or exchange control that prevents Licensee from maintaining its legal authorization to conduct business, or from paying any sums required by this Franchise Agreement in the time and manner required hereunder shall not be construed as an event of Force Majeure, except as expressly provided in Section 18.5.

FM provision in franchise agreement

Kidzania's opposition

2. The Force Majeure Clause Does Not Excuse E2W's Performance

E2W cannot rely on the Force Majeure clause because (1) its nonperformance (failure to pay) occurred long before and was not caused by the COVID crisis, and (2) the Force Majeure Clause states that Minimum Guaranteed Royalties must be paid, even if a Force Majeure occurs.

May 11, Judge Carter grants TRO/PI

ORDERED that Defendant KidZania and its agents, employees, and affiliated companies under its control are enjoined from terminating the Franchise Agreement and taking any actions that would interfere with the continued operations of Plaintiff, including indicating or disclosing to any third party that the Franchise Agreement has been terminated. The Parties are **ORDERED** to otherwise maintain the status quo of their operating relationship pending a decision in the ICC arbitration regarding the termination of the Franchise Agreement.

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Examples of COVID-19 Force Majeure Litigation

- ▶ *Palm Springs Mile Associates, Ltd. V. Ross Dress for Less, Inc.*, No. 20-cv-21865 (SD Fla. May 4, 2020)
- ▶ Landlord claims breach of commercial leases and accelerated rent.
- ▶ Force majeure clause excludes making of payments.
- ▶ Likely an issue for many tenants.

26.14. Force Majeure.

As used in this Lease, the term “Force Majeure” means delay resulting from causes beyond a party’s reasonable control such as strikes, walkouts or other labor disputes, acts of God, inability to obtain labor, materials or merchandise, governmental restrictions, regulations or controls (hereinafter “governmental matters”) excluding from “governmental matters” planning and building permits, if issued within the average time period for doing so in the issuing jurisdiction for the last twelve (12) months, and governmental approvals and inspections if performed pursuant to the jurisdictions and conditions within the average period of time of requesting the jurisdictions approval or inspection, judicial orders, war, riot or civil commotion, fire or casualty. The party obliged to perform shall give prompt notice to the other as soon as reasonably possible after the onset of such delay stating the cause and an estimate of the duration thereof. If, as a result of an event of Force Majeure, either party shall be delayed or hindered or prevented from the performance of any act required hereunder (other than the making of payments) within the time period set forth herein, the performance of such act shall be excused for the period of delay not to exceed sixty (60) days in any calendar year, and the period of performance of such act shall be extended for a period equivalent to the period of such delay not to exceed sixty (60) days in any calendar year, unless a provision of this Lease expressly states that Force Majeure is not applicable, such as the end dates of Permitted Delivery Periods and the Automatic Termination Date. Financial inability to perform shall not constitute an event of Force Majeure.

Plaintiff’s complaint

28. While the Leases do contain a force majeure provision (Article 26.11 in the 511 Lease; 26.13 in the 1345 and 5296 Leases), the provision does not apply to these circumstances. The provision also excludes from its scope the “making of payments.” Accordingly, since the provision is not applicable, and the Tenant’s failure to pay rent is not excused, there is no contractual basis for the Tenant to avoid its obligation to pay rent.

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Examples of COVID-19 Force Majeure Litigation

- ▶ *Pacific Collective, LLC. V. Exxonmobil Oil Corp.*, No. 20-cv-03887 (CD Cal. April 28, 2020)
- ▶ Plaintiff is purchaser of land that it says it intended to develop immediately after closing
- ▶ After stay at home orders were issued, Plaintiff claimed that scheduled closing was impossible
- ▶ Plaintiff provided notice to defendant (buyer) that it was invoking the force majeure provision

38. FORCE MAJEURE.

The deadline for performance of any obligation of a party hereunder shall be automatically extended one day such performance is delayed on account of force majeure, which as used herein means acts of God, strikes, lockouts, sit-downs, material or labor restrictions by any governmental authority, civil riot, floods, wash-outs, explosions, earthquakes, fires, storms, acts of the public enemy, acts of terrorism, wars, insurrections, defaults by the other party and any other cause not reasonably within the control of the party whose performance is delayed by force majeure and which, by the exercise of due diligence, the claiming party is unable, wholly or in part, to prevent or overcome.

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Brian Steelman
Annette Moore
March 30, 2020
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Plaintiff's notice of FM

labor restrictions, earthquakes, fires, storms, acts of the public enemy, acts of terrorism, wars, insurrections, defaults by the other party and any other cause not reasonably within the control of the party whose performance is delayed by force majeure and which, by the exercise of due diligence, the claiming party is unable, wholly or in part, to prevent or overcome."

The ongoing COVID-19 pandemic is a force majeure that prevents Buyer from meeting its obligations under the Agreement by the Closing. As you are aware, the City of Los Angeles, County of Los Angeles, and State of California each issued "Safer at Home" orders on March 19, 2020. The City of Culver City issued its own "Safer at Home" order on March 20, 2020. Among other restrictions, the "Safer at Home" orders (1) require all persons to remain at least 6 feet away from one another, and (2) close all "Non-Essential Retail Businesses."

While our client fully intends to proceed with its purchase of the Property, the aforementioned orders and restrictions inhibit our client's ability to close escrow while the governmental orders and restrictions remain in force. The "Safer at Home" orders will be in effect until at least April 19, 2020, a minimum period of thirty-one days, unless further extended. Unfortunately, the "Safer at Home" orders are expected to remain in effect for an unknown additional period of time.

Defendant's response

While Purchaser's business is not an "Essential Business" under the "Safer at Home" Orders, it is allowed to continue business operations and the services required to close the transaction are "Essential Businesses" and functional at this time. These are the same circumstances in which Seller is operating, and Seller remains willing and prepared to close this transaction. The Title Company has also confirmed that, at this time, it is able to close the transaction. There are no other conditions to closing that exist in the Agreement that cannot be met.

At this time, the "Safer at Home" Orders do not prevent or prohibit Purchaser's performance of its obligations under the Agreement nor do they prevent or prohibit Closing. Therefore, Seller rejects Purchaser's assertion that it is unable to perform due to a force majeure event and demands Purchaser perform its obligations as stated in the Agreement and First Amendment to Sale and Purchase Agreement.

Examples of COVID-19 Force Majeure Litigation

- ▶ *Pacific Collective, LLC. V. Exxonmobil Oil Corp.*, No. 20-cv-03887 (CD Cal. April 28, 2020)
- ▶ Plaintiff sues seeking declaratory judgment that it is not in breach of the agreement

5 SUMMARY OF ACTION

6 1. In March 2020, citizens of the State of California were facing an unprecedented

7 global pandemic known as COVID-19, which brought with it the deaths of thousands of

8 Americans, and prompted City, County, and State officials to execute orders and directives for all

9 persons residing in California to stay at home for an indefinite period. The orders, which were all

10 directed at preserving and protecting the safety of human life, rendered it impossible for Plaintiff

11 to perform the acts of closing under a land purchase agreement entered with Defendant. Said

12 orders and directives also made it impossible for Plaintiff to redevelop the real property upon

13 closing, which redevelopment Defendant acknowledged was Plaintiff's intended use. Despite the

14 global pandemic and the City, County, and State Orders, Defendant, in material breach of the

15 agreement, rejected Plaintiff's rightful invocation of the force majeure clause in their agreement

16 to merely extend the closing date, as expressly provided for in their agreement, while the force

17 majeure persisted. Making matters worse, Defendant also attempted to unilaterally terminate the

18 transaction in further material breach of their agreement, all because Plaintiff was unwilling to

19 violate law and jeopardize human life.

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QUESTIONS?