

>> COVID-19 ALERT

How the COVID-19 Crisis Impacts Contract Obligations

THE BOTTOM LINE

- >> Businesses need to consider if fulfilling their contractual obligations is possible during the COVID-19 crisis. If performance truly is not possible, a party may be excused from performing based on the following legal doctrines:
 - *Force Majeure*
 - Frustration of purpose
- >> Because access to court systems is limited at this time, parties should negotiate contract performance-related issues on their own. This will likely save company resources in the long-term and can help maintain key business relationships.

The COVID-19 pandemic is impacting businesses throughout the U.S. and around the world, causing great uncertainty in numerous ways.

Even with new guidance and regulations being issued by governments daily, many questions remain. One issue likely to arise is whether businesses must fulfill contractual obligations to clients, vendors, and other partners.

If facing such issues, businesses must rely on the particular terms of their contracts. However, certain key principles are broadly applicable and should be considered.

ABILITY TO PERFORM

Given the many restrictions already in place, businesses first need to determine whether they are even able to perform their contract obligations. For example, events and gatherings are currently prohibited and access to public accommodations is restricted in many jurisdictions. Many contracts related to such activities clearly cannot be performed in the present climate. Businesses should keep this consideration in mind, whether the contractual obligation is their own or their counterpart's.

Businesses are already adapting and continuing to provide services, especially when performance may be made remotely. In some instances, the parties may be able to perform but in a manner different from what they originally contemplated. Where performance is possible, it will likely not be excused by the crisis, whereas when a contract truly cannot be performed, a party may be excused pursuant to one of the legal doctrines discussed below. Businesses would be wise to consider creative alternative means of performance, thereby minimizing disruption and disputes, which courts may ultimately view unfavorably given the circumstances.

JUSTIFICATIONS EXCUSING PERFORMANCE

Even in these unprecedented circumstances, the starting place for any analysis of a party's obligations is within the contract's four corners. While specific language could alter application of the below doctrines, parties should consider:

Force Majeure

- >> Many contracts contain a *force majeure* provision. These are intended to address circumstances beyond the parties' control that impede or prevent performance of contractual obligations. *Force majeure* provisions generally allow parties to delay performance or have it excused altogether.
- >> Many *force majeure* provisions list types of unforeseen circumstances that will constitute a covered event. A pandemic is sometimes included; if not, there are

often other events listed of the same type (e.g. “Acts of God”), such that courts might consider a pandemic covered, especially in light of government mandates that limit all non-essential personnel activities.

- >> Generally, courts strictly construe *force majeure* provisions, so if a contract has express exceptions (stating that certain obligations are not relieved), even in this extraordinary situation, a court will likely apply the *force majeure* provision as written.
- >> Mere impracticality or difficulty is typically not enough to excuse performance, nor is economic hardship or changed market conditions generally considered a *force majeure* event.
- >> If the parties did not include a *force majeure* provision in a contract, courts will not read one in.

Frustration of Purpose

- >> Similar to *force majeure*, frustration of purpose may excuse a party from performing.
- >> Frustration of purpose may apply if there is a mutually understood “basis” for the contract, the basis has been completely frustrated, and the transaction makes little sense without it.
- >> Only rarely do courts find a contract’s purpose frustrated and typically not based on

economic hardship or changed market conditions, so there will likely need to be some aspect of the COVID-19 crisis that has impacted the contract’s basis.

- >> For example, if parties had contracted to hold an event coinciding with the 2020 NCAA Final Four, because the tournament was cancelled — as opposed to merely postponed — the contract’s basis would be frustrated and a court may relieve the parties of their obligations.

IMPORTANT TAKEAWAYS

In this time of crisis, everyone should consider the following when assessing contract obligations and how to proceed:

- >> First determine whether performance is possible in light of government restrictions and best practices, focusing on the health and safety of all parties.
- >> If performance is possible — even if made more difficult or costly by the COVID-19 crisis — parties will likely be obligated to perform, though they should consider reasonable accommodations during this difficult time.
- >> If performance is not possible or the crisis has defeated the entire purpose of the contract, the doctrines of *force majeure* and frustration of purpose may excuse performance.

- >> Access to both state and federal courts has been restricted in many jurisdictions. Litigants are being urged to avoid burdening the courts with non-urgent matters. If parties are unable to resolve disputes without judicial intervention, they may not receive prompt relief that courts might provide under ordinary circumstances.
- >> Attempting to negotiate issues relating to contract performance will likely save company resources in the long-term, and can help maintain important business relationships that will be critical after the crisis. In some instances, a contract partner’s continued operation may depend on accommodation from its partners.

FOR MORE INFORMATION

Ina B. Scher
Partner
212.468.4937
ischer@dglaw.com

Daniel A. Dingerson
Associate
212.237.1488
ddingerson@dglaw.com

or the D&G attorney with whom you have regular contact.

Davis & Gilbert LLP
212.468.4800
1740 Broadway, New York, NY 10019
www.dglaw.com

© 2020 Davis & Gilbert LLP