

## CAN PERFORMANCE OF CONTRACTS BE EXCUSED DUE TO THE COVID-19 CRISIS?

Due to the COVID-19 pandemic, Stay at Home Orders, and resulting financial turmoil, many contracting parties find themselves either unable to perform their obligations, or faced with increased difficulty in doing so. Several contract defenses exist which may excuse performance, depending on the specific facts of each case.



**Force Majeure:** Contract provisions, called "*Force Majeure*" clauses, may extend times for performance under contracts for delays that result from unforeseeable events which are beyond the control of the parties, and are extraordinary or outside the usual risks assumed when contracting. Whether any circumstance will be a valid event of *force majeure* depends on the particular language of the contract and the factual situation. Such clauses typically define events that will give rise to an excuse or permit delay in performance. These events routinely include fire or other casualty, labor strikes, government orders or actions, and acts of terrorism, but may include other events such as disease or pandemic. If a contract includes pandemic and/or government orders as *force majeure* events, there may be an excuse of performance. These clauses are most often seen in construction contracts and loans, and are also often included in leases that require either landlord or tenant to make improvements to the property. Typically, the financial hardship of a party is not considered a *force majeure* event, and the obligation to pay money cannot be excused or delayed. There may also be express language requiring the payment of money (such as rent) even during the occurrence of a *force majeure* event.

**Frustration of Purpose and Impossibility:** Other doctrines exist which may excuse contract performance, such as frustration of purpose and impossibility. Unlike a *force majeure* excuse, these doctrines do not require a clause to be present in the contract. Instead, "frustration of purpose" excuses performance when an unforeseen event that is not the fault of the party asserting the defense occurs, and that event is so destructive of the purpose of the contract that even if the contract were performed, that party would not receive the benefit it is owed under the contract. Similarly, "impossibility" excuses performance when an unforeseen event that is not the fault of the party asserting the defense occurs, and that event renders the performance of the contract either literally impossible, or extremely impracticable due to unreasonable hardship or expense. Like the *force majeure* excuse, frustration of purpose and impossibility typically do not apply when the unforeseen event is the financial inability of one party to perform, because such hardship, even if so extreme as to force a party out of business, is a foreseeable risk of entering into a contract. However, due to the unprecedented nature of the COVID-19 crisis, novel theories of excuse are likely to be asserted. Commercial tenants, who unlike residential tenants are not covered by certain Federal and State eviction moratoriums, are especially likely to attempt to expand these defenses to seek rent deferment or abatement, although it is unclear how courts may rule on these theories.

**Business Interruption Insurance and Loss of Rent Insurance:** Commercial landlords and tenants may look to their loss of rent or business interruption policies respectively, in order to mitigate the negative effects of a loss of rental income due to the COVID-19 pandemic. Business interruption insurance is designed to cover a loss of business income that accompanies a slowdown or cessation of business operations. Tenants are sometimes required to carry this coverage under a commercial lease, and the coverage is typically triggered by physical loss or damage to the subject property, although suspension of operations due to a civil authority or order may also be a covered loss. Unfortunately for many businesses affected by COVID-19, these policies often contain exclusions for losses arising from viral or bacterial outbreaks. An analysis of the specific policy language will be important, as will the characterization of the reason for shutting down the business. Whether the closure of a retail outlet, for instance, is the result of a "viral outbreak" or the result of a "civil order" is debatable when many nonessential Michigan businesses have been required to close due to the Governor's Executive Orders. Landlords may also have rent loss policies to cover the loss of rental income arising from a covered loss. Again, whether such policies will cover COVID-19 related losses depends on the policy language, so landlords holding such policies should examine them carefully for potential claims.



This Memo provides only a general overview of the contract issues businesses are experiencing as a result of the COVID-19 pandemic. If you have questions or require legal advice regarding these or other issues arising from the pandemic or any other real estate matter, please contact [Gregg Nathanson](#), [Phil Neuman](#), [Ronn Nadis](#) or [Alexis Havenstein](#).