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Commercial Contracts in the Time of Coronavirus: Am I still required to perform?

by Meghan E. Tepas

A FREEBORN & PETERS LLP CLIENT ALERT

ABOUT THIS CLIENT ALERT

The outbreak of COVID-19 has disrupted commercial transactions across the state and the world and will continue to do so. The response to the outbreak and resulting market consequences will undoubtedly make it more difficult for some companies to comply with their contractual obligations. This Alert discusses the possibility that force majeure clauses and the impossibility doctrine may excuse performance under certain circumstances.

In a matter of days, COVID-19 has upended the regular operation of business for many companies across Illinois and the world. As more and more people are staying inside their homes, businesses are losing customers and in some cases, are being forced by government mandates to close their doors to the public all together. Inevitably, this new environment is going to make it difficult for some businesses to continue to meet their obligations under contracts they entered into prior to the outbreak of the virus.

Take for example the scenario in which a bar or restaurant had, prior to the outbreak, contracted to purchase so many units of beer from a distributor but following a government mandate closing all bars and restaurants, the bar/restaurant no longer has a need for the product. Or the situation in which an organization contracted with a catering company to cater its annual conference, but it can no longer hold the conference due to restrictions against large gatherings. Whether the current crisis will excuse performance and relieve businesses of legal liability for failing for perform in situations like these and others will depend on the specific language of the contract at issue and the effect the outbreak has on the obligation to be performed.

What does the contract provide?

Often commercial contracts will contain a "force majeure clause" that is intended to allocate risk in the face of unanticipated events. Typically these clauses contain boilerplate language providing that performance is excused during the occurrence of an act of God, war, action or inaction of a government authority, terrorist acts, civil commotion, riots, strikes, picketing, or extreme adverse weather which greatly impacts a party's ability to perform. Some contracts articulate even more specific categories of events that would constitute a force majeure event, including "public health emergency" or "pandemics," for example.

In addition to defining what constitutes a force majeure event, a force majeure clause will likely also identify the effect such an event must have before a party can invoke its protection. For example, the contract may provide that the unforeseen event must make performance "impossible," or it may require that the event merely "hinder or delay performance" before a party may be excused from performance. Thus, in order to cancel a contract containing a force majeure clause on the basis of unforeseen circumstances resulting from the Coronavirus outbreak, a party must establish both a force majeure event occurred as that term is defined in the agreement and that the event had the required effect on performance.

Courts across the United States have historically interpreted force majeure provisions narrowly, and are often reluctant to relieve parties from their contractual obligations. However, in these unprecedented times, force majeure clauses in contracts may provide an avenue of relief to businesses who find that the Coronavirus has made compliance simply unworkable. Businesses worried about their ability to perform and the ability of their customers or partners to perform under prior contractual agreements should carefully review their contracts to assess the applicability of their force majeure clauses to the current situation.

What if my contract does not have a force majeure clause?

If your contract does not contain a force majeure clause or if the force majeure clause is not broad enough to cover public health emergencies, a party may still be relieved from its obligations under the "impossibility doctrine." In Illinois, this doctrine operates to excuse performance of a contract when performance is rendered objectively impossible either because the subject matter of the contract has been destroyed or by operation of law. The bar to establish impossibility is high, and is not available when performance is made simply more difficult or more expensive.

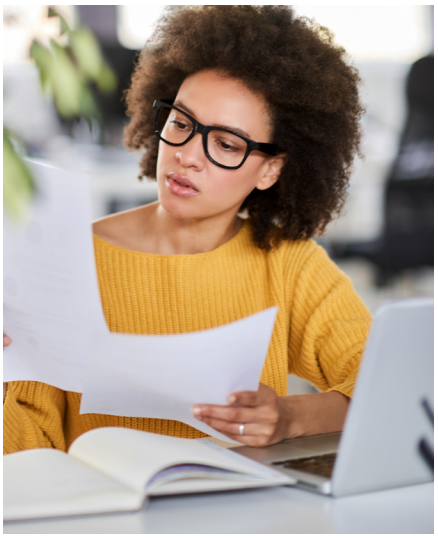
Take the examples noted above. In the first, the government shut down of all bars and restaurants will likely make it more difficult for the bar/restaurant to pay for the ordered product because it no longer has the means to conduct business in order to generate revenue. While this unfortunate situation was prompted by a change in the law, the bar/restaurant will not be able to avoid its obligation to pay for the product. That is so because while paying for the product was undoubtedly made more difficult by the change in the law and the resulting decrease in revenue, it is not objectively impossible. Stated differently, the fact that the bar/restaurant may not be able to sell the product during the shut down does not actually preclude it from purchasing the product and thus, the impossibility doctrine is not applicable.

In the second example, the party that engaged the catering company has a better chance of avoiding operation of the contract and any payment obligation on the basis of impossibility. Unlike the situation in the first example, the conference and thus the contract would have been scheduled to occur on a specific day. When the law changed to prohibit large gatherings, the conference legally could not proceed and thus the contract could not be performed. While the law changed in both examples, only in the second example did the change render performance impossible.

Assessing your contractual obligations.

The effect COVID-19 will have on commercial transactions and parties' contractual obligations is bound to be varied and unpredictable. As businesses begin to rethink business as usual and attempt to adjust to the current market landscape, they would be well-advised to review their contracts and consult counsel on the operation of any force majeure clause and the applicability of the impossibility doctrine.

If you have questions, please contact Partner Meghan E. Tepas at mtepas@freeborn.com or 312-360-6454 or visit Freeborn's COVID-19 webpage.



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Meghan is passionate about litigation and takes a thoughtful and creative approach to each of her cases. She focuses on general breach of contract disputes and employment disputes including those involving breach of non-compete and non-solicit agreements. She has extensive experience representing clients facing claims of negligent hiring and breach of fiduciary duty relating to allegations of employee sexual harassment and sexual misconduct. Meghan also counsels start-ups and small businesses with respect to vendor, customer, and employee contracts.

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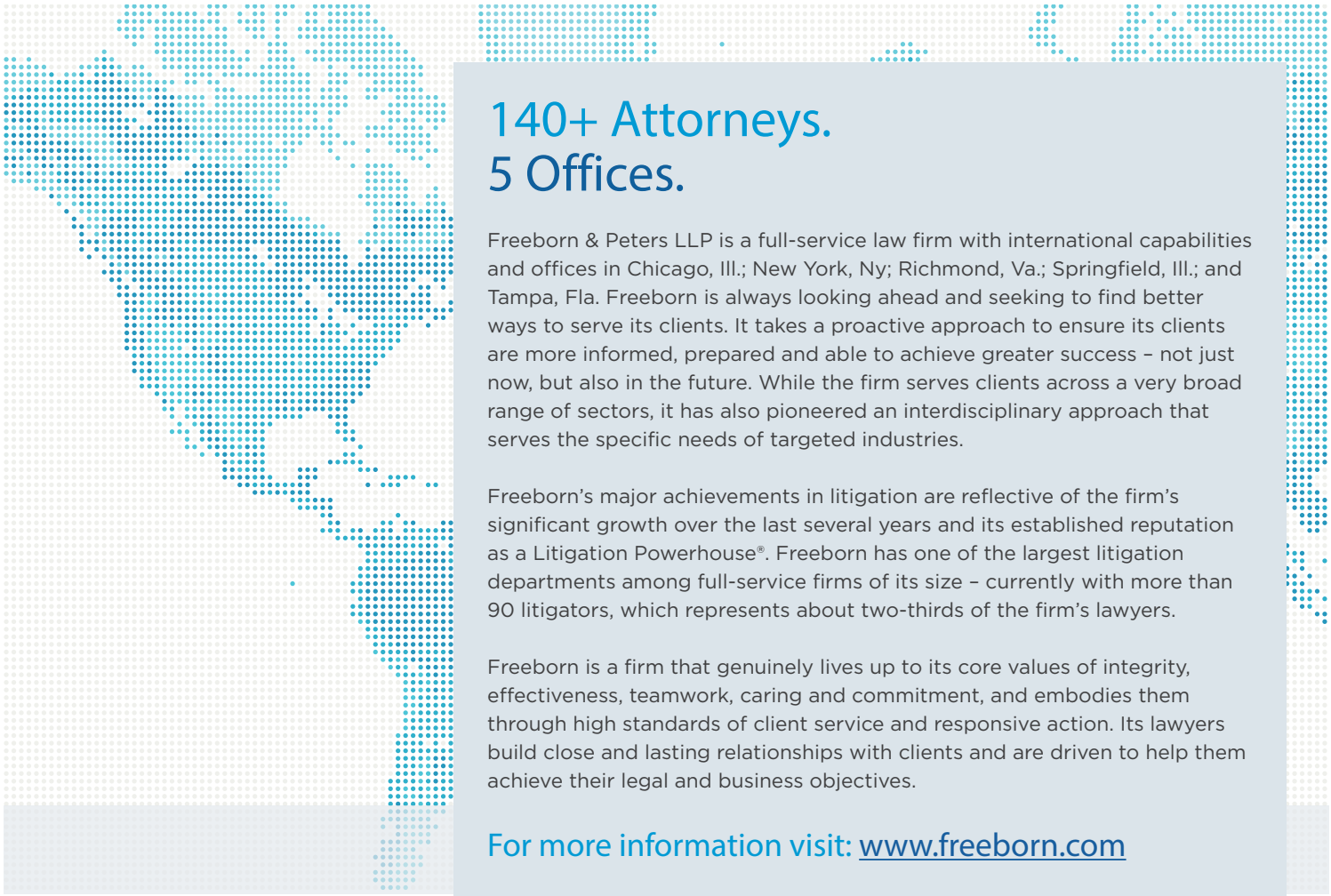

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