

Force Majeure in the Age of COVID-19: A Force to be Reckoned With

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As the COVID-19 pandemic continues to wreak havoc on our social, legal, financial, real estate, and healthcare systems, the widespread disruptions caused by the COVID-19 outbreak have in certain instances made it impossible or impractical for many parties to meet their contractual or other legal obligations. Parties seeking relief from their legal obligations because of these circumstances may raise “force majeure” or “act of God” defenses to their contractual obligations, claiming that events related to the pandemic make it impossible or impractical for those parties to meet their obligations.

Facing COVID-19 related circumstances, businesses, corporations, limited liability companies, and individuals may well find themselves on one side or the other of force majeure defenses as they seek to enforce or obtain relief from contractual or other legal obligations. This Alert considers a variety of circumstances in which force majeure and impossibility and impracticality of performance defenses may arise, and how to both utilize and oppose such defenses depending upon your position or perspective.

What Does the Contract Say?

Whether you are seeking to enforce or obtain relief from contractual obligations, the first order of business is to carefully review the contract to determine whether it contains a force majeure or act of God provision, as this is not always the case. Typically, when such a provision exists “force majeure” is a defined term, such as an act of God that prevents or impairs performance in a fundamental way. Most contracts will not use the word “pandemic” but will instead define force majeure in more general terms. Scrutinize that definition or description closely to determine if the contract provides a basis to assert a force majeure defense.

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Often, contracts may require appropriate notice of a claim that a party cannot perform its obligations and seeks to be relieved of those obligations by virtue of the force majeure provision. Such notice should be given by mail, email, and/or any means specified by the contract. Even if not contractually required, notice will likely serve as a necessary prerequisite to asserting a force majeure defense. Conversely, the absence of notice may prevent the use of the force majeure provision. The failure to provide good notice has precluded the use of force majeure defenses in past pandemics and catastrophic events.

In order to establish a case for force majeure, a litigant must demonstrate that the scope and extent of the force was uniquely pervasive and impossible to overcome. Generally, a force majeure must be beyond the reasonable control of the affected party, rendering that party's ability to perform its contractual obligations impossible, or interfering with the contract terms so starkly and completely that in effect, the contract terms can no longer be met.

COVID-19: Impossibility, Impracticality, or Hardship?

During the ongoing COVID-19 crisis, despite some dislocation and inefficiency, many businesses and individuals can work remotely, and although their profitability may be impacted negatively, they are still able to operate at reduced capacity. As a consequence, determining whether performance of a party's contractual obligations can be enforced or excused will rely on a determination as to whether business operations have been disrupted to the point where it is impossible or impractical to meet certain contractual obligations, or whether meeting those obligations simply represents a hardship which can be overcome.

In New Jersey, professional service providers such as accountants, financial advisors, architects, engineers, physicians, attorneys, and other non-retail business entities have not been mandated by Executive Order to cease operations and may continue to function, if at a reduced level. It may be a hardship to pay rent or meet other contractual obligations under these circumstances, but it is not impossible. Depending on the degree of hardship and impracticality, such businesses may or may not be successful in asserting the force majeure defense. A party advancing the force majeure defense in this context will have to demonstrate that it actively sought, without success, to mitigate or overcome the hardship.

It may be possible to legitimately claim that given its breadth and depth the COVID-19 pandemic represents an unforeseen event that prevented a party from performing its contractual obligations. Impossibility or impracticality of performance are key indicia as to what constitutes a force majeure; an event of such great magnitude and impact that it could not have been anticipated. However, it is the degree to which COVID-19 has disrupted business operations and impaired the ability to meet contractual obligations that will determine the outcome of a case. For this reason, the facts and circumstances of each case must be carefully evaluated.

The failure to take reasonable steps to overcome the disruption of the COVID-19 crisis may preclude a force majeure defense. Therefore, for parties who may consider asserting a force majeure defense, it is critical to keep precise records of what actions were taken in an attempt to meet contractual obligations.

These records should be kept contemporaneously with the events, and should include the specific dates of those actions, the names of personnel who were involved, the location of those actions, and the consequences of those actions.

Conversely, an absence of records or evidence that substantiate the business' attempts to meet contractual obligations may be used to overcome a force majeure defense. It is also important to assess whether a prospective force majeure claimant could have secured a Paycheck Protection Program (PPP) loan, or perhaps reduced or furloughed staff or personnel in an attempt to honor its contractual or other obligations. The ability of a business to demonstrate its inability to honor contract terms is crucial.

It is important to keep in mind that any party making a force majeure claim likely has the burden to prove that its obligations were rendered impossible by COVID-19. Depending on the nature of the business and obligations, this may not be an easy task and in any event, it will be both fact sensitive and industry specific. An understanding of recent federal and state laws, regulations, and Executive Orders is critical to assessing whether a force majeure claim has viability.

Force Majeure: A Brief Review of the Law

Existing force majeure and related case law may provide some basic guidance, but the COVID-19 pandemic is historically unique and will undoubtedly generate new law given the extent of its impact. In general, force majeure clauses are viewed within the context of contracts, but they likely will be applied in other areas of the law such as matrimonial, estate, real estate, landlord and tenant, condominium, and several other areas of the law. Harnessing the facts of each case is therefore critical, as every case will be individually considered.

Facto v. Pantagis, 390 NJ Super 227 (App. Div. 2007) dealt with a typical force majeure provision in a contract. In this case, plaintiff contracted with defendant to provide a wedding hall reception, and 45 minutes into the reception there was a power outage. This event gave rise to defendant invoking the force majeure provision. The Court concluded that given the fact that the outage represented an unforeseeable "act of God" the plaintiff was not obligated to pay the wedding hall except for the 45 minutes of services that were provided. The hall was also not responsible for the failure to perform, as both were governed by a force majeure. Moreover, the Court concluded that in the absence of a force majeure clause there would be a common law defense to a contract based on impossibility or impracticality of performance. Since there was an express contractual force majeure provision, the Court applied the contract, not the common law. The application of the force majeure clause to both parties in this case may prove to be critical in future cases. Just as the wedding hall could not perform, the wedding party would only have to pay the reasonable value of services that were rendered before the power outage. We can foresee many courts possibly splitting the difference if partial performance was possible. Thus, for example, if a restaurant could still perform take-out functions during the COVID-19 pandemic, it may still be responsible for part of the rent. It is fairly clear that fundamental fairness and some equitable consideration will likely play a role in any court review.

In *MJ Paquet v. NJ Department of Transportation*, 171 NJ 378 (2002) the New Jersey Supreme Court dealt with revised government OSHA regulations which made a portion of a highway painting construction project dealing with a bridge highly “impractical.” Because the contractor Paquet would have had to “expend substantial, unanticipated costs to complete its performance of the bridge painting work,” for which it would not receive adequate compensation by virtue of DOT’s lack of consent, and as the additional painting work was inextricably linked to the original work, the Court ruled that the DOT had the right to cancel that portion of the contract work, and that Paquet should be released from its contractual obligations.

It thus appears that in the COVID-19 context, “impracticality” and “impossibility” of performance caused by government regulation may likely play a major role in negating contractual obligations given the Executive Orders issued by Governor Murphy closing “non-essential” retail businesses. However, as these Executive Orders currently permit many retail businesses serving food or liquor to do so on a take-out basis, claiming the full benefit of a force majeure clause for those businesses may not prove possible. Additionally, landlords may claim that because they didn’t receive any rent payment, or received reduced rent payments from tenants, their contractual obligations, in turn, should be reduced or made void by force majeure considerations as well.

The federal courts have taken a similar approach to force majeure issues. In *Norfolk Southern Railway v. New York Terminals*, 2017 WL 4005158 (DNJ 2017) the Court was confronted with a weather impracticality issue in a rail shipping contract governed by a tariff. However, because the defendant failed to provide written notice of the weather delays as required by the tariff, the Court disallowed the claims despite the force majeure and impossibility of performance aspects. This case reinforces that parties should carefully review and abide by the notice provisions of their contracts. Because notice is a critical factor when making a force majeure claim, conversely, a lack of notice and/or sufficient record-keeping may prove to be a viable defense to a force majeure claim.

With respect to contracts dealing with sales transactions involving goods, the doctrine of impracticality of performance is codified in New Jersey’s Uniform Commercial Code (UCC) at NJSA 12A:2-615, which states in pertinent part: **12A:2-615. Excuse by failure of presupposed conditions**

Except so far as a seller may have assumed a greater obligation and subject to the preceding section on substituted performance:

(a) Delay in delivery or non-delivery in whole or in part by a seller who complies with paragraphs (b) and (c) is not a breach of his duty under a contract for sale if 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. . . .

(c) The seller must notify the buyer seasonably that there will be delay or non-delivery and, when allocation is required under paragraph (b), of the estimated quota thus made available for the buyer.

The UCC provision contains complex language as to whether the seller's performance was rendered impractical by a "contingency the non-occurrence of which was a basic assumption" under the contract – in other words, an unforeseen event. We anticipate substantial debate over whether under this provision of the UCC, the COVID-19 pandemic may be considered a "contingency the non-occurrence of which was a basic assumption" of a sales contract.

It is critical to note that the UCC also requires timely and appropriate notice of a delay due to impracticality of performance. Thus, we again emphasize that if contractual performance is going to be impacted by a COVID-19-related force majeure issue, the cancelling party provide timely and appropriate notice to the relevant parties or risk jeopardizing its claim.

Conclusion

Although COVID-19 is uncharted territory, the breadth and depth of the pandemic is such that force majeure defenses will inevitably be advanced. Under these exceptional circumstances all parties should take appropriate steps to best position themselves to either assert or defend against these claims.

As contractual defenses are often narrowly construed by the courts, force majeure and impossibility and impracticality defenses are no exception. Relieving one party of its contractual obligations as a result of a COVID-19-related hardship would then shift the burden of the hardship to the other contracting party. Consequently, we would expect that the courts will attempt to achieve an equitable result in determining whether, and to what extent, they will relieve parties of contractual obligations as a result of force majeure.

Finally, we would again note that the common law impossibility or impracticality defenses can have application in areas of the law other than those involving contracts. Such defenses may well be used in the matrimonial, environmental, mortgage, tax, and insurance law contexts. Many payment obligations during the COVID-19 crisis have been temporarily postponed or set aside by regulatory guidance and Executive Orders, and such pronouncements may be used as persuasive authority in making force majeure claims but may not necessarily be dispositive. As a result, such defenses should generally be employed only when clearly supported by the facts and circumstances of the case.

Please contact the authors of this Alert with questions or to discuss your specific circumstances.

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