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Contractual Rights, Performance Obligations and COVID-19: A Primer on Gap-Filler Doctrines and Force Majeure

By Christopher R. Agostino on March 16, 2020

The spread of COVID-19 has triggered economic turmoil and unprecedented government intervention into private industry. Business owners, lenders, landlords, employers and their respective counter-parties are reviewing the key terms of innumerable business arrangements and relationships impacted by current events. One common contract term that ordinarily draws little attention and is often relegated to the miscellaneous section of many agreements is Force Majeure. Generally, Force Majeure clauses serve to excuse performance and liability where a party cannot carry out its contractual obligations as a result of an event that is beyond that party's control. Many Force Majeure clauses include a laundry list of events that might trigger relief. The events listed traditionally include "Acts of God" such as earthquake, flood, war, and the like. Ideally, for a party that seeks to avoid performance, Force Majeure will include a catch-all that references, "or any event beyond the parties' control." A catch-all clause under Force Majeure can be important to avoid application of, "*expressio unius est exclusio alterius*", which is a contract law principle that means, "to express one thing is to exclude the other." For example, if a Force Majeure clause only lists, "earthquake, flood, and war," does that mean that the parties intended to exclude all other events that were not listed, e.g. pandemic or alien invasion? Many Force Majeure clauses specifically provide that no event – Act of God or otherwise – would serve to excuse the mere payment of money, but what if Force Majeure makes it impossible to generate revenue? Some Force Majeure clauses include complex notice requirements and time limitations that if not strictly followed may limit the applicability of Force Majeure protection. In some cases, failure to follow strict Force Majeure notice requirements might even serve to compromise the benefit of contract Gap-Filler Doctrines described below. The application of any particular Force Majeure clause is contract, fact and jurisdiction specific, but where some Force Majeure clauses require time-sensitive notice prior to enforcement, readers are well advised to review the terms of their specific contracts if performance has been called into question as a result of COVID-19.

As described above, Force Majeure clauses vary and generally no two are alike, which is also why Force Majeure is not always the first place a party might look when it seeks relief from performance. While Force Majeure will likely generate attention in the weeks and months ahead, there are other contract terms that are less well known, but that are arguably more important and more uniformly applicable than Force Majeure in times of crisis. Every contract has certain implied contract terms that protect both parties. Known as "Gap-Filler Doctrines," both Common Law and the Uniform Commercial Code recognize these critical contract terms, whether or not they are expressly stated in an agreement. Two gap-filler contract terms that may apply to this pandemic are: 1) impossibility of performance, or more recently mere impracticability, and 2) frustration of purpose. Impossibility of performance has deep roots in common law and continues to evolve to this day. Historically, literal "impossibility" was required in order to trigger this doctrine. For example, death of a party to the contract or destruction of the subject matter upon which performance was based, were both acceptable prerequisites to excuse performance.

If you contract to rent out a restaurant for a celebration, but the government ordered the restaurant closed through no fault of the restaurant owner, the restaurant owner would be excused from performance (i.e. providing the space) and would not have any liability based on impossibility of performance. This theory has since evolved. Impossibility is no longer a pre-requisite under the Uniform Commercial Code in Massachusetts. Rather, a party may show that performance has become commercially impracticable (i.e. excessively burdensome) in order to be excused. See Mishara Constr. Co. v. Transit–Mixed Concrete Corp., 365 Mass. 122 (1974). As described inMishara and Massachusetts cases that have followed, the degree of impracticability would require evaluation, but generally, parties are not absolutely responsible for contract performance when faced with circumstances that could not have been reasonably anticipated.

Frustration of purpose serves as a gap filler to address the scenario where performance is still possible, but some intervening event has rendered performance worthless. The relevant Massachusetts case involves a contractor that agreed to purchase concrete barriers for a municipal project. See Chase Precast Corp. v. John J. Paonessa Co., 409 Mass. 371 (1991). After the contract was signed, the public objected to use of the barriers so the government forced a contract change that prohibited their installation. Stuck with a contract to purchase these now worthless concrete barriers, the contractor argued that frustration of purpose should excuse the contractor's obligation to purchase the barriers. The Court in Chase Precast agreed and held that where the parties had not expressly allocated the risk, frustration of purpose would excuse performance and insulate the contractor from liability for failure to make the purchase. This conclusion was fact specific, as most requirements and supply contracts allocate the risk of unforeseen circumstances; however, frustration of purpose served this buyer well in the absence of risk allocation.

Gap-Filler Doctrines can serve as critical lifelines to parties faced with mounting contractual obligations in uncertain times. A careful analysis of risk allocation is critical to any contract. Ideally, parties to a contract will expressly identify known and foreseeable risks and address them in a Force Majeure clause or elsewhere. However, as current events reveal, it can be impossible to predict the future and plan for every eventuality in every contract in today's fast-paced business environment. Some businesses might think that they can simply rely on business interruption insurance. However, although it may seem counter-intuitive, business interruption insurance often excludes "Acts of God," including pandemics and war, absent special endorsements that can be expensive. This is why Gap-Filler Doctrines serve an important role in risk management. If COVID-19 has jeopardized your ability to comply with your contractual obligations, a careful analysis of any Force Majeure clause, or Gap-Filler Doctrines such as impossibility of performance, frustration of purpose, as well as "constructive conditions of cooperation" and "mitigation of damages," is critical and may be time-sensitive.

RIW remains available to assist its clients. We will continue to monitor COVID-19 and will send client alerts as further information becomes available. Should you have any questions about this or any issues related to COVID-19 please reach out to your RIW attorney contact.

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