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COVID-19 has upended the operations of countless California businesses. As fallout from the pandemic continues, many companies face uncertainty regarding their contractual obligations and whether they or their counterparties have any legal basis to excuse or delay performance in light of the pandemic. Contractual force majeure clauses and the doctrines of commercial frustration and impossibility are defenses that are likely to arise with regularity. Although each contract will have its own unique issues that should be considered in assessing the parties' rights and obligations, below is a basic discussion of these defenses under California law. Please note, however, that as with many situations in the current environment, federal, state, and local legislation or other orders are being implemented almost daily and may otherwise modify the discussion below.

Force Majeure

Many real estate contracts contain a "force majeure," or "act of God," provision that excuses a party's performance of certain obligations if a specified event – such as war, earthquakes, strikes, or governmental shutdown – occurs. California courts may excuse a party's non-performance of a contractual obligation if such an unforeseen event occurs and prevents the party from performing.

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The most important consideration in understanding whether a force majeure provision may apply is to examine its specific terms and determine which events are covered by the provision. For example, force majeure provisions in many leases exclude from its application the continuing obligation to pay rent. Other force majeure provisions only excuse performance for a specified period of time.

A party who is invoking a force majeure provision must show that despite its skill, diligence, and good faith, performance became impossible or unreasonably expensive due to an unforeseen event. It also must prove that the force majeure event is the proximate cause of nonperformance. Thus, with respect to COVID-19, if a party's failure to perform is caused by another event and not the pandemic, that party may not be able to invoke the force majeure clause. Relatedly, if one party's ability to perform rests on a third party's performance, courts will look to whether the third party's inability to perform falls within the scope of the force majeure provision and whether it is in fact impossible or unreasonably expensive for the party to satisfy its obligations despite exercising skill, diligence, and good faith.

Contractual force majeure provisions often contain special notice or timing provisions. Parties should examine their force majeure provisions to ensure that they are providing timely notice in the manner specified by the provision, such as personal service.

Frustration of Purpose

Even if a contract does not contain a force majeure provision, a party may be able to assert, as an alternative argument, that the purpose of the contract was frustrated by an event, which should thereby excuse its performance.

To invoke the doctrine of commercial frustration, a party must show that changed conditions have rendered the performance bargained for from the promisee worthless. Under this doctrine, California courts have required a promisor seeking to excuse itself from performance to prove that the risk of the frustrating event was not reasonably foreseeable and that the value of counter-performance is totally or nearly totally destroyed.

In recent days, certain cities and counties and the State of California have ordered mandatory closures of "non-essential businesses" or imposed other restrictions in operations through shelter-in-place or safer at home ordinances or orders. In determining whether such governmental-mandated restrictions would frustrate the purpose of a contract, courts in California have decided that if the regulation does not entirely prohibit the business to be carried on in the leased premises but only limits or restricts it, thereby making it less profitable and more difficult to continue, the lease may not be terminated or the lessee excused from further performance. However, some of these mandatory closures may provide a party with an avenue to argue frustration of purpose at least during the period of the mandatory restriction. For example, a commercial tenant may argue that because its doors were ordered to be closed, the reason the tenant entered into the lease – to operate its business – is no longer possible. Because of this, the tenant could argue that it receives no value from the lease, and should be relieved of the obligation to pay rent.

Generally, however, the doctrine of frustration of purpose has been applied narrowly, and courts generally find that it does not apply except in very narrow circumstances. Indeed, treatises and several courts recognize that there is no impracticability or illegality in a tenant's payment of rent, because, among other things, the tenant should assume the



risk of casualties as temporary owner of the estate.

Impossibility

Akin to the doctrine of frustration of purpose, the doctrine of impossibility follows much of the same law. The party asserting the defense of impossibility has the burden to prove the following elements: (1) a supervening event made performance impossible or impracticable; (2) the nonoccurrence of the event was a basic assumption upon which the contract was based; (3) the occurrence of the event resulted without the fault of the party seeking to be excused; (4) the party seeking to be excused did not assume the risk of occurrence; and (5) the party has not agreed, either expressly or impliedly, to perform in spite of impossibility or impracticability that would otherwise justify nonperformance.

The doctrine applies where performance is subsequently prevented or prohibited by a judicial, executive or administrative order made with due authority by a judge or other officer of the United States, or of any one of the United States. In order to be an excuse for nonperformance of a contract, the impossibility of performance must attach to the nature of the thing to be done and not to the inability of the obligor to do it.

However, as with the application of the defense of frustration of purpose, even where the impossibility doctrine may apply, but is merely temporary, a party's duty is likely to be suspended only during the time of the impossibility. In other words, the party may be entitled to some relief based on the unforeseen event, but then must perform once that event has passed.

Force majeure, frustration, and impossibility are all defenses that companies are likely to encounter in the wake of COVID-19. California businesses should review their existing contracts, with the assistance of their counsel, to understand whether these doctrines could apply to upcoming contractual obligations.