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The Unfortunate Reality: The Court’s Narrow Application of Common Law Defenses to Contractual Breaches in the Wake of COVID-19 Restrictions

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The Unfortunate Reality: The Court’s Narrow Application of Common Law Defenses to Contractual Breaches in the Wake of COVID-19 Restrictions

By: Michael Hallagan, Staff Editor, Vol. 110

COVID-19 spiraled into not only a healthcare crisis, but a financial one for both individuals and businesses across the nation. Parties that entered into contracts before COVID-19 were confronted by these hardships. Parties with contractual obligations that were suddenly challenged by lockdowns and a global tragedy steered us into an ideal problem; whether COVID-19 regulations excused performance.[1] Before discussing the common law defenses to contractual obligations, it is important to note that many parties have provided force majeure clauses in their contracts.[2] A force majeure clause is a provision detailing a party’s obligation in the occurrence of an event or effect that can be neither anticipated nor controlled.[3] Reliance on such provisions can be successful, as demonstrated by a recent Second Circuit decision on March 23, 2022, finding that a force majeure clause for an art auction is to be conducted in May.[4] The crucial provision, “[i]n the event that the auction is postponed for circumstances beyond our or your control, including, without limitation, as a result of natural disaster . . . we may terminate this Agreement with immediate effect,” was effective in terminating the auctioneer’s contractual obligation to perform.[5] The court concluded that the “COVID-19 pandemic and the restrictions on nonessential businesses issued by Governor Cuomo constituted “circumstances beyond the party’s reasonable control.”[6] This Second Circuit decision appears to be a rarity in many other jurisdictions; not only by the court’s usual strict interpretation of a force majeure clause, but also because the provision is often poorly written.[7]

Even as the restrictions leave daily life for those in many states[8], courts are still dealing with parties with poorly written force majeure clauses or the total absence of a provision detailing party obligations under certain circumstances. A plausible result for these parties is to rely on the common law-based defenses to contractual obligations.[9] Applicable common law defenses include; impossibility of performance, often considered interchangeably by the courts with that of commercial impracticability of performance, and frustration of purpose.[10] Yet, these defenses frankly have a very limited success rate and even with COVID-19, the result for many parties that attempt to shield their liability through these common law defenses are often a disappointment.

Impossibility & Commercial Impracticability Defense

Impossibility of performance is readily defined as an excuse for nonperformance when an unforeseen event occurs after the contract is made which makes performance impossible or commercially implausible.[11] A party utilizing this defense usually must prove the following; (1) after entering into the contract, an unexpected intervening event occurs, (2) the non-occurrence of the intervening event was a basic assumption underlying the contract, and (3) the

intervening event made performance wholly impossible or objectively economically impracticable.[12] While the test in determining impossibility may appear easily applicable to any rule-hungry law student, it ironically can be said that it is nearly impossible to achieve an impossibility defense.[13] Why? Courts narrowly apply the impossibility defense in instances where one party necessary to the contract is deceased, property central of your contract is not destroyed, or the law prevents performance of a party's obligation; a breaching party should seek other avenues to defend their breach.[14] For the two former points, possibilities can come from infirmity or death to central parties resulting from COVID-19.[15] As for the latter point, realistic illustrations of parties that may succeed in these claims are for parties engaged in manufacturing that had been forced to cease all production due to COVID-19 restrictions or the performance outlined in a lease agreement is commercially impracticable due to governmental orders to close their commercial business entirely. In such occasions, these parties may have an impossibility defense to temporarily extend their contractual obligation dependent on jurisdiction.[16] Even more, if such a contract had a specific time provision or the contract revolved around specific deadlines, the contract may be deemed wholly impossible due to the specific provisions.[17] If you are not in this small group of parties, you will most likely have to find another way to defend your nonperformance because such a strict application indicates that if there is any objectively possible means to complete your contractual duty, then say farewell to the impossibility defense.

Frustration of Purpose Defense

Frustration of purpose appears facially promising to parties that had a reason to contract that was then thwarted by COVID-19 and governmental restrictions. A simplified definition is that performance of one's contractual duties is worthless when a later and unforeseen event occurs.[18] Worthless is taken quite literally by the courts; it does not mean practically worthless, more expensive, or new unfavorable market changes, but literally worthless. Market changes due to COVID-19 restrictions plausibly have many industries finding themselves in an inherently worse situation, but if the court can find some reason why contractual performance is not worthless, courts often reject such a defense.[19] Yet, there are circumstances that this defense believably may be successful, such as purchasing a hotel room for the sole purpose of attending a 2021 March Madness game.[20] Even more, a court may have found partial frustration of purpose when COVID-19 restrictions were in effect and one party does not pay rent for commercial property specifically tailored to a specific business owing to the inability to provide services. Still, parties not situated in a parallel situation to these illustrations may need to find alternative options to defend their breach.

Conclusion

In reality, impossibility and frustration are unsavory defenses in most jurisdictions, as courts are unwilling to substitute contractual obligations due to unforeseeable events unless events create an obligation so inequitable to the parties as to excuse performance through these means.[21] Even so to courts that utilize a stringent application, they are common law defenses, and since courts are occasionally culpable to altering doctrines; chasing the *red owl* may be a promising path.

[1] See Jenny Rough & Andy Markowitz, *List of Coronavirus-Related Restrictions in Every State*, AARP (Updated Apr. 1, 2022), <https://www.aarp.org/politics-society/government-elections/info-2020/coronavirus-state-restrictions.html> (<https://www.aarp.org/politics-society/government-elections/info-2020/coronavirus-state-restrictions.html>).

[2] See Janice M. Ryan, *Interpreting Force Majeure Clauses*, Venable (Mar. 18, 2020), <https://www.venable.com/insights/publications/2020/03/interpreting-force-majeure-clauses> (<https://www.venable.com/insights/publications/2020/03/interpreting-force-majeure-clauses>).

[3] Michael E. Kohagen, *The effects of COVID-19 on our interpersonal and business relationships grow each day*, Ward and Smith, P.A. (Apr. 6, 2020), <https://www.wardandsmith.com/articles/covid-19-and-force-majeure-what-businesses-should-know#:~:text=Black's%20Law%20Dictionary%20further%20defines,not%20within%20a%20party's%20control> (<https://www.wardandsmith.com/articles/covid-19-and-force-majeure-what-businesses-should-know#:~:text=Black's%20Law%20Dictionary%20further%20defines,not%20within%20a%20party's%20control>).

[4] *JN Contemporary Art LLC v. Phillips Auctioneers LLC*, 29 F.4th 118 (2d Cir. 2022).

[5] *Id.*

[6] *Id.*

[7] Scott Casher, *Second Circuit Holds That Covid-19 Excused Defendant From Performance Pursuant to Force Majeure Clause*, DSUPRA (Mar. 31, 2022), <https://www.jdsupra.com/legalnews/second-circuit-holds-that-covid-19-4603455/> (<https://www.jdsupra.com/legalnews/second-circuit-holds-that-covid-19-4603455/>).

[8] Rough, *supra* note 1.

[9] *Id.*

[10] See Kelly J. Bundy, *Impossibility, Impracticability and Frustration of Purpose in the Age of COVID-19*, ABA (Aug. 3, 2020), https://www.americanbar.org/groups/construction_industry/publications/under_construction/2020/summer2020/impossibility-impracticability-frustration-of-purpose-in-the-age-of-covid-19/ (https://www.americanbar.org/groups/construction_industry/publications/under_construction/2020/summer2020/impossibility-impracticability-frustration-of-purpose-in-the-age-of-covid-19/).

[11] *Id.*

[12] *Id.*

[13] *Id.*

[14] *Id.*

[15] See Eric R. Tubbs, *COVID-19 and the Contractual Defenses of Impossibility/Impracticability and Frustration of Purpose*, (Apr. 6, 2020), <https://nyemaster.com/news/covid19-and-the-contractual-defenses-of/> (<https://nyemaster.com/news/covid19-and-the-contractual-defenses-of/>).

[16] *Id.*; *Impossibility of Performance in the Time of COVID-19*, Freiburger Haber (Mar. 26, 2021), <https://fhnylaw.com/impossibility-of-performance-in-the-time-of-covid-19/> (<https://fhnylaw.com/impossibility-of-performance-in-the-time-of-covid-19/>).


[17] See Rough, *supra* note 1.

[18] See Shireen Barday, Beth Maloney, Rahim Moloo, Hannah Kirshner, & Robert Banerjee, *When a Commercial Contract Doesn't Have a Force Majeure Clause: Common Law Defenses to Contract Enforcement*, Gibson Dunn (April 24, 2020), <https://www.gibsondunn.com/when-a-commercial-contract-doesnt-have-a-force-majeure-clause-common-law-defenses-to-contract-enforcement/> (<https://www.gibsondunn.com/when-a-commercial-contract-doesnt-have-a-force-majeure-clause-common-law-defenses-to-contract-enforcement/>).

[19] See Michael A. Delaney, Wilbur A. Glahn III, & Jennifer L Parent, *Does the Coronavirus Excuse Performance of a Contract? Force Majeure and Impossibility or Impracticability of Performance*, McLane Middleton (Apr. 8, 2020) <https://www.mclane.com/does-the-coronavirus-excuse-performance-of-a-contract-force-majeure-and-impossibility-or-impracticability-of-performance/> (<https://www.mclane.com/does-the-coronavirus-excuse-performance-of-a-contract-force-majeure-and-impossibility-or-impracticability-of-performance/>).

[20] See generally, *Krell v. Henry* [1903] 2 K.B. 740.

[21] See Delaney, *supra* note 19.

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