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Events Excusing Performance of a Contract

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Businesses are beginning to slowly emerge from COVID-19 and are focused on efforts to return to normal operations. Amidst these efforts, businesses are still facing difficult financial situations, which often involve making decisions on whether the business can perform under its existing contracts. In some cases, dealing with these contract performance issues are “bet the company” decisions, and factors affecting these decisions are discussed below.

My company cannot perform under a contract. What are my options?

When unexpected events occur such as a global pandemic, parties to a contract may need to evaluate various legal bases to excuse performance under an otherwise binding written contract. The application of these legal arguments involves a fact specific inquiry, and it normally results in notice being provided to the other party to the agreement explaining the basis for non-performance. Each of the arguments are discussed below.

Impossibility of Performance and Impracticability of Performance.

Impossibility of performance arises when an event outside the parties' control renders the performance of contractual duties literally impossible. Relatedly, impracticability of performance occurs when an event outside the parties' control renders performance of a contract possible, but highly impractical. High impracticability arises in situations where the performance itself becomes unreasonably difficult or expensive, or performance may result in injury or loss to one of the parties.

Frustration of Purpose. Commercial frustration of purpose is applicable when an event outside the parties' control destroys the non-performing party's expected value of the contract. Like impracticability, the performance is still possible, but the expected value received from the performance is significantly diminished or destroyed.

How Do Courts Apply These Doctrines? In reviewing the defenses of impossibility, impracticability, and frustration of purpose, courts review whether the event was outside of the parties' control and whether the event's non-occurrence was a basic assumption underlying the purpose of the contract. When the event was caused by a party, other contractual remedies may be available to the other party. Similarly, where an event occurs, but it does not relate to the contract or affect performance, these defenses will be unavailable. Additionally, courts review the terms of the contract to determine whether the event's occurrence was contemplated by the parties and a solution was provided. When an event's occurrence is contemplated, the terms of the contract govern, and the defenses will not provide an excuse for performance. Courts may not excuse performance

when the event is one that the party seeking to be excused should have foreseen and provided some remedy in the contract for the event's occurrence. These three contract defenses may be relied upon to cancel a contract, or they may be used to temporarily suspend a party's performance until the event affecting the contract is over. If the underlying event affecting the contract is temporary, the performance is likely to be suspended as opposed to being cancelled.

Illegality of Performance and Government Regulations. Many state and local governments have enacted various orders regulating business activities during this pandemic. Government regulations that arise after a contract is agreed to can be considered an “event” if the non-existence of the regulation was an assumption underlying the purpose of the contract. Government regulations are considered “events” sufficient to excuse performance when the regulation either prohibits performance or makes performance extremely difficult or unreasonably expensive. However, government regulations that require a party to seek approval from regulatory agencies do not constitute “events” that will excuse a contractual duty.

Uniform Commercial Code. The UCC, which has been adopted by most states and governs the sale of goods, provides a seller's delivery of goods required by a contract may be excused where an event outside the seller's control renders delivery impracticable. The UCC's impracticability approach applies to both delay of delivery and non-delivery of goods. Like impracticability discussed above, the UCC requires that the event not be caused by a party and that the non-occurrence of the event be a basic assumption of the contract. Further, impracticability may excuse the delay or non-delivery of goods if government regulations make delivery impracticable. Additionally, the UCC requires a seller to deliver part of the promised goods if the event only impacts part of the seller's supply. A seller must also notify the buyer that there will be a delay or non-delivery or a partial delivery and the amount of the partial delivery.

Anticipatory Repudiation. While a breach of contract typically occurs when a party fails to perform at the time specified, the doctrine of anticipatory repudiation provides that the non-breaching party may sue for breach of contract if the other party makes a clear and unequivocal statement that they will not perform under the contract at the agreed time. In such a situation, the non-breaching party may immediately assert a claim for damages or wait until performance was to occur and then seek relief. Additionally, when a breaching party makes a clear statement that they will not perform under a contract, the non-breaching party is excused from continuing to perform pursuant to the contract. The non-breaching party must still mitigate their damages under anticipatory repudiation but may still recover contract damages from the breaching party.

If one of these arguments for not performing under a contract applies to me, what should I do? Typically, the first step is to provide notice to the other party to the agreement explaining the basis for non-performance. The notice should detail the reason why some of the above arguments apply (including possibly Force Majeure, which is the subject of separate articles). Obtaining legal counsel prior to providing that notice is critical

because: 1) the application of these arguments is very fact specific and oftentimes involves evaluating both legal and non-legal circumstances; and 2) assertion of these legal arguments can lead to litigation where each of these arguments must be argued and proven in order to avoid being held liable for breaching an agreement.

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