



Force Majeure: The Effect of COVID-19 on Contracts

BY BRANDI SMITH

As we roll into a second month of stay-at-home orders triggered by the COVID-19 pandemic throughout Texas, the commercial real estate industry is beginning to fully feel the impact. Non-essential retailers have been forced to shut their doors, in some cases eliminating all potential for revenue. Those employees, furloughed or laid off, face a similar dilemma: how do you pay your mortgage or rent when no money is coming in? The answer for some is to turn to the “force majeure” clause of their contract, if they negotiated one.

“Typically a force majeure clause has been something that people don’t pay much attention to. It’s one of the boilerplate paragraphs toward the end of the contract,” said David Groff, shareholder with Wilson Cribbs + Goren, a 20-attorney law firm that focuses on commercial real estate. “That doesn’t mean it’s any less important than any other provisions in the lease, but it sometimes doesn’t get the attention it requires because people get so comfortable for so long.”



David Groff



Scott Clinton

WILSON CRIBBS + GOREN
REAL ESTATE LAW

Joined by senior partner Scot Clinton, the pair offered insight into what force majeure is, how courts have responded to it and how both tenants and landlords can respond during REDNews’ April 9 webinar on the topic.

“The gist to identify specific types or categories of events that will relieve parties of their duty to perform. In Texas, the general approach to interpreting force a majeure clause, if there is one, really does boil down to the actual terms of the clause,” Clinton explained.

WHAT IS “FORCE MAJEURE”?

At its heart, a force majeure clause addresses potentially unforeseeable circumstances that might prevent a contract from being fulfilled. However, Groff was quick to point out that it’s no “get out of jail free” card.

“It’s not a card you can play to get out of your lease. It merely is a mechanism to delay a performance when there is something occurring that’s specifically allowed in the lease to defer performance until that interruption is removed,” he said. “So any thoughts such as “I can terminate my lease because there’s a pandemic” probably won’t be workable.”

He and Clinton stressed that execution of the clause weighs heavily on its language, which is rarely duplicated contract to contract due to alterations or modifications negotiated between parties.

“[The contract language is] where the analysis, scope and application is going to be determined,” said Clinton. “A close review of the terms that you may have is really key. We can’t underscore that enough.”

WHAT’S IN A CLAUSE?

Common categories outlined in force majeure clauses include government action, law and regulations; labor and material shortages; act of God; and catchall. Groff pointed out that epidemic/pandemic can be found in existing clauses, typically in the health care industry.

Noting that this was new to many people - landlords, tenants, lawyers, bankers, etc. - and that information changes on a daily basis, Groff said negotiations will change as well.

“It’s been conspicuously absent from a lot of the form lease language that I’ve seen and even used over the past however many years,” he said. “You can bet that moving forward that the words “epidemic,” “pandemic” or “government shutdown” will start being used in everybody’s form force majeure language.”

Analyzing the “government action, law & regulations” category, Clinton said past legal interpretation suggests the action, law or regulation must be specific to the lessee.

“At the very least, it’s unclear whether a government law or regulation is going to be in and of itself sufficient to reach the type of situations that we’re seeing here,” he said, noting that the courts haven’t weighed in on the current situation. “We’re not seeing orders at the state, federal or local level that are specific to individual parties.”

Clinton expressed doubt the “act of God” would apply in this case either, as it is typically reserved for forces of nature, such as hurricanes.

“The analysis may go into whether the force majeure event is having directly to do with the pandemic itself or if it’s related to other issues that are within the series of events that are affecting the ability to perform,” he said.

Finally, there’s the issue of the “catch-call” in the clause, which addresses other circumstances that may otherwise hinder the ability of the party to perform. Per Clinton, the courts generally lean on the ejusdem generis doctrine.

“The idea is that if there’s a catch-all provision, the list of items and categories of events described in the preceding portion of the clause,

whatever may come after that, the catchall will be limited to things in the former,” he said. “The initial list is going to lay out the parameters of what follows after that.”

It’s also worth noting that the Court of Appeals held that catch-all provisions in force majeure clauses do not include foreseeable events in the TEC Olmos, LLC v. ConocoPhillips Co. ruling. Previous outbreaks, such as SARS in 2003 or H1N1 in 2009, could be used in an argument that this kind of crisis can be foreseen.

“There’s an interesting discussion about whether the courts may look at those types of issues and think that issues of pandemics or epidemics are, going forward, foreseeable and ones that parties should be more expectant of and more actively negotiate,” said Clinton.

IF THIS IS A FORCE MAJEURE ...

If a party believes in good faith that a force majeure event has occurred, two basic questions must be answered: when did it begin and when will it end?

“Generally speaking, a force majeure event is not going to last into perpetuity. There’s going to be a beginning and an end,” Clinton said.

The next concern is how it applies. That all depends on the language in your lease agreement or loan documents.

“There’s often going to be found a carve out that says specifically that force majeure will not apply in the case of a monetary obligation,” Groff said. “So whether or not you have a force majeure, in a good number of leases, there is not going to be an exception for the payment of rent.”

However, there are other clauses within some retail leasing agreements that could be triggered by the current shutdown, the first being a co-tenancy clause. Many major tenants require that landlords maintain open and operating neighbors within a shopping center to support traffic and customer base. If the landlord is unable to meet those requirements, the tenant may exercise certain relief as outlined in the clause. That could be interpreted as reduced rent, free rent or, in some cases, termination if co-tenancy isn’t met for a period of time. The landlord could, in that instance, invoke force majeure in response.

“As this plays out, it’s going to get very interesting,” said Clinton.

Another clause worth noting addresses “continuous operations,” which outlines that retailers must remain open, as well as fully staffed and stocked during certain days and times. Clinton expressed that arguments surrounding this clause haven’t been made yet, but he sees them on the horizon.

LANDLORDS, WHAT’S THE NEXT STEP?

The road ahead isn’t one we’ve traveled before, but Clinton and Groff offered up a kind of map to help landlords navigate how to move forward.

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First, have a conversation with tenants about the state of their business and review their contract.

“Not every lease is going to be the same. Not every interaction between landlord and tenant will be

the same. Not every right of force majeure will be the same,” Groff said. “Each negotiation has the potential to be significantly different than any other based on the circumstances of that particular event.”

He emphasized that tenants will need relief and that needs to be understood. However, relief can be defined depending on the tenant. Options include rent abatement, rent deferral or a rent extension. In most cases, these are considered temporary.

“The groundwork for those discussions changes on almost a daily basis. Something a landlord may have offered last week is off the table. Something a tenant may have tried to offer or be willing to accept a week ago is off the table,” said Groff. “Everything is very fluid and people are just trying to find their footing on where all of this is headed.”

A landlord offering relief is still obliged to pay his or her debts. Groff and Clinton encouraged those with loans to talk to lenders about what’s happening at their properties.

“Bring them in early, make sure they know they know the situation,” Groff said, contrasting it with the idea of suddenly asking for a forbearance months down the road. “Bringing them in would be a good idea at this time.”

GOING FORWARD

Throughout this process, Groff stressed that these are temporary times and that, in the near future, we’ll have learned something from it. People will go back to work and leases and contracts will get back to performance stage. When they do, expect to see changes roll out in future versions of form documents.

“You’re going to see a lot of language talking about pandemics and epidemics as well as government-required business cessations, closures and interruptions,” said Groff. “I think, looking forward, there’s going to be a lot of change and the legal industry will address it.”

You can watch the full webinar, along with many others produced by REDNews parent company REjournals, here: <https://www.rejournals.com/videoreplay> ■

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