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Force Majeure: Allocating Risk in Commercial Real Estate Agreements in the Wake of COVID-19

Now that we have lived through a long-term force majeure event, what have we learned for purposes of drafting a fair provision? The first consideration that comes to mind is the definition itself—the existence of a pandemic should count as a force majeure event.

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Now that we have endured more than one year of living in a pandemic, the question arises: how has it affected the manner in which commercial real estate transactions should be negotiated and documented? The negative impact on the already distressed retail and office markets is self-evident. There is little need to maintain a storefront if customers either cannot or will not shop there. The need for facetime in an office environment has proven to be overstated. If a tenant's business is no longer viable for reasons beyond its control, how should that circumstance be addressed in a lease?

The term *force majeure* literally refers to a "superior force"—one that is "neither anticipated nor controlled." *New Jersey Dept. of Envtl. Prot. v. Bayshore Reg'l Sewerage Auth.*, 340 N.J. Super. 166, 168 n.1 (App. Div. 2001). A force majeure clause provides a means by which contracting parties contemplate in advance certain uncontrollable events or effects that will render performance impracticable and conditions a party's obligation to perform upon the non-occurrence of such enumerated events. *Facto v. Pantagis*, 390 N.J. Super. 227, 231-32 (App. Div. 2007). Thus, in drafting this common contractual term, at least some degree of anticipation is required.

While most commercial leases contain force majeure clauses, they are not often the subject of intense negotiations. Force majeure is typically defined to include acts beyond a party's reasonable control: inclement weather, strikes and labor shortages, governmental states of emergency, fire, flood or other casualty to name a few. Some clauses permit only the landlord to invoke an event of force majeure to excuse performance; others apply to both landlord and tenant and may be invoked to excuse performance of obligations other than the payment of rent. These are generally considered to be short-term events.

Because force majeure clauses, perhaps until now, are viewed by most as boilerplate, these terms have not been extensively litigated in New Jersey. But courts having considered the issue will strictly enforce force majeure clauses as written, therefore highlighting the importance

of careful drafting. For example, in *Facto v. Pantagis*, the Appellate Division upheld the dismissal of a newlywed couple's breach of contract claim against a catering hall, which, less than an hour into their wedding reception, was evacuated due a power outage. *Id.* at 229-32. The court had little trouble concluding the catering hall was relieved of the obligation to perform because the force majeure clause specifically captured the event at issue—an "act of God (e.g., flood, power failure, etc.)." *Id.* at 228. However, when a specific event is not stated, courts construe force majeure clauses narrowly to include "only events or things of the same general nature or class as those specifically enumerated." *Seitz v. Mark-O-Lite Sign Contractors*, 210 N.J. Super. 646, 650 (Law Div. 1986).

The *Facto* court nonetheless observed that absent a force majeure clause, performance would have been excused due to impracticability because the area-wide blackout was outside the control of the catering hall, and without electricity, there was no music, no photos or videos and—alas—no air conditioning in the hot summer month of August. 390 N.J. Super. at 233. Impracticability, and its sister concepts of impossibility and frustration of purpose, may provide useful backstops for contracts lacking a force majeure clause, or for unforeseeable circumstances that are not specifically stated in the clause. These common law defenses, although a meager substitute for artful drafting, "excuse … a party from having to perform its contract obligations, where performance has become literally impossible, or at least inordinately more difficult, because of the occurrence of a supervening event that was not within the original contemplation of the contracting parties." *JB Pool Mgmt. v. Four Seasons at Smithville Homeowners Ass'n*, 431 N.J. Super. 233, 246 (App. Div. 2013).

Enforcement of a force majeure clause ordinarily relieves both parties of their obligations to perform. *Facto*, 390 N.J. Super. at 233-234. Yet parties should not assume that mere triggering of a force majeure event will fully excuse performance; a clause may specify that one party will bear the risk should force majeure occur. *See 476 Grand v. Dodge of Englewood*, A-2048-10T1, 2012 WL 670020, at *4 (App. Div. Mar. 2, 2012) (holding a lease's force majeure term, which stated, "Nothing herein shall be deemed to relieve Tenant of its obligation to pay Rent when due," did not discharge the tenant's obligation to pay rent "regardless of any supervening circumstance, occurrence or non-occurrence beyond its control").

Only a handful cases from other jurisdictions have addressed force majeure clauses in commercial real estate agreements in the wake of

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the pandemic, which has produced conflicting views as to whether performance was excused. One court held that a lease's force majeure clause partially discharged a tenant's rent obligation on property operated as a restaurant during the period in which widespread government restrictions, imposed to curtail the spread of COVID-19, prohibited on-premises consumption of food and beverages. *In re Hitz Rest. Grp.*, 616 B.R. 374, 376-78 (Bankr. N.D. Ill. 2020) (abating rent to the extent COVID-19 restrictions rendered certain square footage unusable for its intended purpose because a force majeure clause excused performance that was "prevented or delayed, retarded or hindered by … laws, governmental action or inaction, orders of government" except due to "[l]ack of money"). Another court reached a similar conclusion based on frustration of purpose, but importantly observed that a force majeure clause did not supersede the defense because it addressed only the risk that performance may become impossible, not that the main purpose of the lease would be entirely frustrated by events beyond the parties' control. *UMNV 205-207 Newbury v. Caffe Nero Ams.*, No.

2084CV01493-BLS2, 2021 WL 956069, at *6 (Mass. Super. Feb. 8, 2021).

By contrast, other courts have declined to rely on force majeure to excuse rent obligations on a commercial lease for circumstances caused by the pandemic. *See 1600 Walnut Corp. v. Cole Haan Co. Store*, No. 20-4223, 2021 WL 11993100 (E.D. Pa. Mar. 30, 2021). In *In re CEC Entertainment*, 2020 WL 7356380, at *5 (Bankr. S.D. Tex. Dec. 14, 2020), the bankruptcy court interpreting several leases for Chuck E. Cheese venues across multiple states concluded that COVID-19 restrictions did not discharge rent obligations where the force majeure clauses expressly excluded the tenant's inability to pay rent as grounds to excuse performance. Moreover, the tenant was precluded from asserting frustration of purpose because the force majeure terms contemplated government restrictions and allocated the risk that such restrictions would impact the ability to pay rent. *Id.* at *11. New Jersey courts have not had occasion to address force majeure terms post-pandemic, but in view of cases like Facto and others, we should expect that our courts will enforce force majeure clauses as written.

Now that we have lived through a long-term force majeure event, what have we learned for purposes of drafting a fair provision? The first consideration that comes to mind is the definition itself—the existence of a pandemic should count as a force majeure event. Force majeure clauses rarely expressly mention pandemics, but their inclusion can often be inferred. A bona-fide pandemic is very likely to have been the subject of governmental orders relating to states of emergency. It might be described as "a widespread outbreak of disease or illness causing a substantial disruption in commercial and financial transactions."

Tenants will argue that if their businesses are no longer viable as a direct consequence of a long-term pandemic, they ought to be able, at some point, to terminate their leases. This right would, of course, negatively impact the landlord. If it's a net lease of a single tenant building, or if many of the tenants in a multi-tenant building terminate their leases, the landlord will argue that such an impact could be catastrophic, leading to foreclosure, bankruptcy or some combination thereof. The landlord's reaction would be to refuse to provide for any termination rights. Conversely, some clauses that are presently being floated give the tenant the unlimited right to abate the rent or delay performance on a day-for-day basis in the case of, for example, performing a build-out. Most landlords will not be amenable to such a provision.

The approach taken with respect to "Good-Guy" guaranties might be of some guidance. (Of course, if a Good-Guy guaranty exists, there may be no need to invoke force majeure). The tenant should be required to give notice, the length of which will depend on the circumstances. Payment of a termination fee might be appropriate, depending on how much time remains in the term and whether the landlord has incurred substantial costs for the fit-up. Brokerage might also be a consideration. For short-term events, abating the rent and extending the term would seem to be reasonable discussion points. As always, the relative bargaining positions of the parties will tend to dictate the result.

We are entering a new era in the commercial real estate arena. How it will shake out is anybody's guess. Clearly, the pandemic has accelerated already existing trends. What does seem certain is that the parties now will pay close attention to the force majeure language when negotiating leases. One hopes that the experience in the marketplace going forward will result in clauses that will, as nearly as possible, fairly apportion the risk.

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