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## Legal Alert -- COVID-19 and Contracts

Community Development Project  
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### Contractual and Practical Considerations for Nonprofit Organizations and Small Businesses Due to COVID-19 Outbreak

The COVID-19 outbreak has had an expansive impact on a variety of industries and has caused disruptions to the operations of both nonprofit organizations and small businesses alike. Such disruptions include the inability of nonprofit organizations and small businesses, or their counterparties, to perform obligations under existing contracts. In the event of such a disruption, a party to a contract may have a defense if they are unable to perform under that contract. This alert discusses common defenses to the failure to perform under a contract as well as steps to take if you are unable to perform under a contract. The discussion below applies to both nonprofit and for-profit entities. (Note - this discussion is not intended to address leases).

#### Force Majeure

Force majeure, which literally means "superior force," is a provision included in many contracts that frees both parties from their obligations under a contract if an event beyond the parties' control (such as a natural disaster or an act of terrorism) prevents one or both parties from fulfilling their contractual obligations. A review of a specific contract's terms will reveal whether the contract specifically provides for excuse, or suspension, of performance of contractual obligations due to a "force majeure" event, and the extent and scope of such excuse or suspension. Without the inclusion of a force majeure clause in the contract at issue, courts likely will not accept a party's defense to nonperformance based upon a claim of a force majeure event. A force majeure clause may also provide a right of termination if a force majeure event has continued for a designated amount of time.

If your contract has a force majeure clause, you should read it carefully to understand whether it applies and how it can be exercised. For example, some contracts may impose notice requirements upon a party attempting to invoke a defense to performance due to a force majeure event. Such notice requirements should be carefully followed to ensure a force majeure claim is not waived simply as a result of the failure to notify the counterparty (and to avoid other unfavorable ramifications). Force majeure clauses in contracts may also impose an obligation on the party experiencing the effects of a force majeure event to avoid or mitigate such effects. In determining whether a defense to performance may be available based upon a COVID-19-related force majeure claim, it will be necessary to carefully review the language in the force majeure clause, the extent of the COVID-19 outbreak's specific impact on the party in question, the particular facts and circumstances surrounding the party's failure to perform, and the applicable law of the relevant jurisdiction.

## **Defenses Based on Doctrines of Impossibility, Impracticability, and Frustration of Purpose**

In some jurisdictions, including California, a party unable to perform under a contract may be able to invoke other defenses in addition to force majeure to excuse performance of contractual obligations. These other defenses include the legal doctrines of impossibility, impracticability, and frustration of purpose. The threshold to a finding of impossibility, impracticability, or frustration of purpose may be very high and is dependent on the availability of the defense in the applicable jurisdiction. The defense of impossibility generally requires the intervening event that prevents performance of the contract to (i) be unexpected, (ii) be of such a nature that the absence of that intervening event was an underlying assumption of the contract, and (iii) render the terms of the contract impossible to perform. The doctrine of impracticability generally excuses performance where a party's performance is still possible but has become exceedingly expensive and onerous due to an intervening event. Jurisdictions that recognize "frustration of purpose" defenses may excuse contractual performance where the initial purpose of the contract at the time of its execution has been substantially frustrated by an intervening event that makes the contract essentially valueless. An analysis of whether an intervening event may give rise to a defense of impossibility, impracticality, or frustration of purpose is extremely fact-specific and dependent on the availability of the defense in the relevant jurisdiction. It may also be affected by the presence of a force majeure clause in the underlying contract.

## **Breach**

Contracts will often provide remedies if one party fails to perform its obligations under the contract, which is referred to as a "breach" of the relevant term of the contract. If a party improperly asserts one of the above-described defenses (force majeure, impossibility, impracticability, and frustration of purpose), this may amount to a breach of the contract by the party improperly claiming the defense. If that happens, the non-breaching party may then be entitled to contractual remedies for the breach, including the payment of monetary damages.

## **Waiver of Breach and Request for Concessions in Light of Change in Circumstances**

To the extent nonprofit organizations and small businesses are facing potential breaches of contracts for their non-performance of contractual obligations due to hardship created by the impacts of the COVID-19 outbreak, measures should be taken to (i) identify the contractual counterparties affected by the nonperformance, and (ii) determine whether such counterparties are currently offering relief or concessions amid the widespread change in circumstances caused by the outbreak. Certain municipalities, utilities, and other entities have announced that relief will be provided for certain breaches of contract due to COVID-19. For example, Southern California Gas Company has suspended service disconnections for the time being and waived late payment fees for small business customers, and the Los Angeles Department of Water and Power announced that it has deferred disconnections for non-payment. Nonprofit organizations and small businesses should identify whether they qualify for, and may avail themselves of, relief measures offered by contractual counterparties in the event of a breach of contract. Further, loan and grant opportunities may be available for nonprofit organizations and small businesses to assist in avoiding breaches of contracts, such as the [Economic Injury Disaster Loan Program](#) offered by the U.S. Small Business Administration and [emergency small business loans provided](#) via the CARES Act.

Additionally, nonprofit organizations and small businesses may consider approaching

contractual counterparties to request a waiver of certain contractual obligations or the renegotiation of terms of the existing contract in light of the unprecedented changed circumstances. However, caution is required when approaching contractual counterparties for relief in the form of waivers or renegotiation, as such requests can potentially result in the relinquishing of rights or an admission of liability under the contract.

## Conclusion

Nonprofit organizations and small businesses may find that they are unable to perform their contractual obligations due to impacts of the COVID-19 outbreak. Defenses to the failure to perform contractual obligations may be available, but require a fact-specific analysis in conjunction with a careful review of the relevant contract's provisions and the governing law. Nonprofit organizations and small businesses should assess whether any concessions or waivers are currently being offered by their contractual counterparties or if they are subject to relief measures that have been extended by municipalities, government agencies or recent legislation. Nonprofit organizations and small businesses may also consider proactively approaching contractual counterparties to reach an agreement regarding onerous contractual provisions in light of the public health crisis. Nonprofit organizations and small businesses which provide essential public services may be particularly well positioned to obtain such relief.

For more resources on COVID-19 for nonprofits, small businesses, and child care providers, please visit [\*\*this page on our website\*\*](#).

If your organization or small business has questions about legal obligations with respect to COVID-19, please contact Public Counsel's Community Development Project at (213) 385-2977, x 200.

## Our Legal Services

The Community Development Project (CDP) builds strong foundations for healthy, vibrant and economically stable communities by providing comprehensive legal and capacity building services to organizations serving people struggling with poverty in the Los Angeles area. CDP provides **free legal assistance** on a wide range of matters to community organizations. For examples of why your organization may need legal assistance, click [here](#).

*If your organization needs legal assistance, please visit our [website](#) or call (213) 385-2977, ext. 200.*

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