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COMMERCIAL LEASING ALERT *FORCE MAJEURE*

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Force majeure is the clause *du jour* in commercial leasing during the pandemic

"Force majeure" clauses are enjoying their day in the sun this year. Historically a boilerplate contract provision that excused performance in the event of some "act of God," "war or insurrection," or other unforeseen calamity likely never to occur, force majeure clauses were for years more frequently invoked by contracts professors and bar examiners than in the real world. COVID-19 changed that. Now, as businesses across the economic spectrum grapple with unprecedented supply-chain disruptions, employee unavailability, mandatory quarantines, government shutdown orders, and other impacts of the outbreak, force majeure has become the contract clause *du jour*.

One area in which force majeure clauses have become highly relevant, and litigated, is in the commercial leasing context. Commercial tenants in the restaurant, retail, fitness, and other "non-essential" industries lost all or partial use of their facilities for months under the patchwork of state shutdown orders across the country, and with the virus continuing to surge out of control as cold and flu season approaches, many of these businesses are now bracing for the possibility of another mandatory shutdown. Those tenants and their landlords are increasingly at odds, as lease payments go unpaid.

Not surprisingly, the law in this area has not kept pace with the spread of the virus. Few courts have addressed the interplay between COVID-19 and force majeure clauses, and even fewer have done so in the context of lease disputes. However, a recent decision by the Bankruptcy Court for the Northern District of Illinois indicates that a substantial rent reduction, and potentially a complete rent abatement, may be available to a tenant during the period of a government shutdown order.

Information about COVID-19 and its impact on local, state and federal levels is changing rapidly. This article may not reflect updates to news, executive orders, legislation and regulations made after its publication date. Visit our COVID-19 resource page to find the most current information.

In the case of *In re: Hitz Restaurant Group, N.D. Ill. Bankr. No. 20 B 05012* (Jun. 3, 2020), a commercial landlord filed a motion in its tenant's bankruptcy case to force the tenant to pay post-petition rent on its restaurant space. The tenant argued that its rent obligation was excused by the lease's force majeure clause, which stated in pertinent part that the tenant's lease obligations would be excused "so long as the performance of any of its obligations are prevented or delayed, retarded or hindered by… laws, governmental action or inaction, orders of government." The clause further stated that "[l]ack of money shall not be grounds for Force Majeure." The tenant argued that this force majeure clause was triggered by the Illinois governor's order that restaurants suspend dining service and offer only carryout and delivery. The landlord, on the other hand, argued that governor's shutdown order did not physically prevent the tenant from mailing in its rent checks, that the tenant's failure to pay rent was due to a "lack of money" fitting within the clause's express exception, and that the tenant could have obtained the money to pay its rent by applying for an SBA loan.

The bankruptcy court rejected each of the landlord's arguments and held that the governor's shutdown order was a triggering event under the plain language of the lease's force majeure clause because it was a "government action" or "order" that prevented, at least in part, the tenant's ability to generate revenue and pay rent. But the court did not let the tenant off the hook entirely. Because the governor's executive order permitted and encouraged restaurants to continue to offer carryout and delivery service, the court held that the tenant's obligation to pay rent was only reduced in proportion to its reduced ability to generate revenue due to the executive order. Based on the tenant's admission that the kitchen was still usable for carryout and delivery services and comprised 25 percent of the restaurant's square footage, the court preliminarily fixed the rent reduction at 75 percent for the period of the shutdown order.

The *Hitz* case provides an early indicator of how courts may respond to disputes between commercial tenants seeking a rent reduction or abatement for the period of a government shutdown and commercial landlords seeking enforcement of their leases. The *Hitz* court's usable square-footage analysis may be workable in the context of a restaurant that can still use its kitchen for carryout or delivery service. It will be less workable for other businesses – for example, gyms – whose entire premises are likely to be rendered unusable in the event of a mandatory shutdown. The analysis may vary from state to state, as real estate leasing issues are a matter of state law, and may also vary outside of the bankruptcy context where courts' equitable powers are more constrained.

Even in the absence of a force majeure clause, *Hitz* could guide courts considering damages in lease disputes. A tenant impacted by a government shutdown may still argue for a rent reduction or suspension based on the common-law doctrines of impracticability of performance or frustration of purpose. Famous for the latter doctrine is the old English case of *Krell v. Henry*, commonly referred to as "the coronation case." In it,

the court held that Krell was excused from paying Henry for an apartment he had rented for two days to view the coronation of King Edward VII after the king fell ill and the coronation was cancelled, thereby frustrating Krell's purpose in renting the apartment. By analogy, a fitness center, for example, may argue that its purpose in leasing a facility is frustrated for so long as the gym is ordered shut down by the state, and a court could apply the *Hitz* court's usable square-footage analysis in determining rent due.

This is a good time for commercial tenants and their landlords, across all industries, to review their lease agreements with fresh eyes on their rights and obligations related to force majeure. The next renewal may be an opportunity to grapple with force majeure language.

For more information please contact Jared Klaus, Matt Moberg or any member of Porter Wright's Real Estate or Insurance Litigation practice groups.