

Insights: Alerts

## Excused Non-Performance-Governments Order Construction to Halt Amid COVID-19 Outbreak

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*Please note: The below information may require updating, including additional clarification, as the COVID-19 pandemic is dynamic and continues to develop. Please monitor this site and/or your email for updates.*

State and local governments are taking aggressive actions to contain the COVID-19 virus by limiting the number of people exposed. These actions have included official and unofficial quarantines and cancellation of public events. For example, San Francisco has issued a Public Health order requiring residents to stay at home and shutting down all businesses except essential stores such as grocery markets, pharmacies, banks and gas stations. Boston has shuttered construction sites.

Government orders that frustrate the performance of a private contract may provide a defense to the non-performing party. Restatement (Second) of Contracts § 264, titled “Prevention by Government Regulation or Order,” states that the performance of a contractual duty made impracticable by having to comply with a domestic or foreign governmental regulation or order may excuse performance where compliance was not an assumed risk of the contract. In *McDonnell Douglas Corp. v. Islamic Republic of Iran*, 591 F. Supp. 293 (E.D. Mo. 1984), the court excused McDonnell Douglas from supplying military aircraft parts to the Republic of Iran following the overthrow of the Shah under an agreement. The United States suspended trade and imposed an export ban, among other actions that prevented performance. The court determined: “*Even absent the force majeure article of the contract MDC would be excused from performance under the Basic Order Agreement because of legal or practical impossibility.*” 591 F. Supp. at 299. Likewise, a quarantine or shutdown of a work site because of a public health order would fall under Section 264.

In *Eastern Air Lines, Inc. v. McDonnell Douglas Corp.*, 532 F.2d 957 (5th Cir. 1976), the court reversed a jury verdict in favor of Eastern Air Lines on its breach of contract claim where McDonnell Douglas delivered 99 commercial airplanes late because it had diverted resources to fulfilling defense contracts during the Vietnam War. McDonnell Douglas argued that the excusable delay provision and the exoneration provisions of the 1950 Defense Production Act excused performance. The contract was executed in 1965. The United States military involvement ramped up the following year with the United States engaging in a “jawboning policy” to encourage manufacturers to prioritize military contracts over commercial contracts. This jawboning policy was sufficient to excuse McDonnell Douglas delays. This aspect of the opinion is particularly important here where businesses are encouraged, but not required, to reduce services and workers are encouraged to work remotely. Even informal action by state and local governments may suffice to excuse performance.

In the construction industry, contractors may have claims against owners for delay costs as well as for costs of ramping down and then ramping up work at the construction site. The contractor would allege the owner failed to make the site available. The owner would then assert government regulation prevented performance.

The rule should be read in conjunction with a *force majeure*, change in law and excusable delay provisions in the contract, if any. As noted in *Eastern Airlines*, a court may construe these clauses broadly even if quarantines or epidemics are not express events excusing performance. However, the language of these provisions still is important. The rule likely would not apply where the contract expressly allocates the risk of a quarantine to one party. In that circumstance, the occurrence of that event would not excuse performance.

Also, this rule should be read in connection with the obligation to mitigate damages as well as the rule stated in Restatement (Second) of Contracts § 272, which allows restitution to avoid injustice. Either party may be entitled to some remedy from the other party to address acts it has performed in furtherance of the contract before the government order. These analyses are fact specific.

#### **Conclusion**

The actions by federal, state and local governments restricting business activities through quarantines and other measures may excuse contract performance whether or not there is an express contract provision. It is important to review each contract to determine whether epidemics or government orders are addressed and to comply with any notice requirements and other procedures. It also is important to track the duration of any delays and all of the cost impacts and to comply with any relevant notice requirements.

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