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Illinois Bankruptcy Court Takes First Swing at Applying Force Majeure to Nonperformance Due to COVID-19

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With the onset of closures and quarantines early this year due to the spread of COVID-19, businesses across the country were confronted with the issue of how to perform their contractual obligations while they were unable to operate under normal conditions (or, in some cases, unable to operate at all). In many instances, they could not. The extraordinary circumstances of state and local governments ordering the closure of businesses and prohibiting the congregation of groups of people mean that many businesses that found themselves in this position will likely turn to force majeure clauses to excuse their nonperformance.

How will the courts treat the application of force majeure to these circumstances? Where a contract contains a force majeure clause, the contractual language supersedes any common law doctrines such as impossibility. As a result, the ultimate outcome in a contractual dispute will be heavily dependent on: (i) the specific language of the clause, (ii) the particularities of the industry involved, and (iii) the language of the relevant government order(s) that caused the nonperformance.

The importance of each of these three factors was exemplified in the recent ruling issued by an Illinois bankruptcy court. *In re Hitz Restaurant Group* is the first case in the United States to consider how a force majeure clause applies to a claim of nonperformance resulting from closures ordered by the government to stop the spread of COVID-19. *In re Hitz Restaurant Group*, No. 20 B 05012, 2020 WL 2924523 (Bankr. N.D. Ill. June 3, 2020). The case involved a landlord suing the bankruptcy estate of a restaurant business for payment of overdue rent. The tenant, Hitz Restaurant Group ("Hitz"), which was in bankruptcy, argued that it was not obligated to pay rent because payment was excused by the lease's force majeure clause when Illinois' Governor issued an executive order curbing the operation of businesses due to COVID-19. The Bankruptcy Court concluded that Hitz should be excluded from its rent obligation but only "in proportion to its reduced ability to generate revenue due to the executive order." *Id.* at *3.

In reaching its decision that Hitz was partially excused from its obligation to pay rent, the court placed heavy emphasis on the language of the force majeure clause, the restrictions imposed (and not imposed) by the Illinois Governor's executive order, and the ability of Hitz to operate on a take-out and delivery basis. *Id.* at *2-*4. Specifically, the force majeure clause excused nonperformance when performance was "delayed, retarded or hindered by . . . laws, governmental action or inaction, orders of government," but it included an exception that "[l]ack of money shall not be grounds for Force Majeure." *Id.* at *2. Meanwhile, the Governor's order mandated that restaurants "suspend service for and may not permit on-premises consumption" but still "permitted and encouraged" restaurants "to serve food and beverages so that they may be consumed off-premises." *Id.*

The court determined that the executive order "unquestionably constitutes both 'governmental action' and issuance of an 'order' as contemplated by the language of the force majeure clause." *Id.* As a result, the court concluded that the force majeure clause "was unambiguously triggered" by the executive order. *Id.* at *2.

The court then rejected three defenses raised by the landlord. First, the court rejected as "specious" the landlord's argument that the "executive order did not shut down the banking system or post offices in Illinois, and [Hitz] therefore would have physically been able to write and send rental checks." *Id.* at *3. Second, it rejected the landlord's argument that any inability to pay rent was due to "lack of money" and therefore specifically excluded from the force majeure clause. *Id.* The court noted that under Illinois law, when two provisions of a contract conflict, the more specific provision will prevail over more general language. *Id.* at *3 n.2. Thus, "[t]o the extent that there is a conflict between the lease's general provision that 'lack of money' does not trigger the force majeure clause, while the lease's more specific provision that a 'governmental action' or 'orders of government' does, . . . the 'governmental action' or 'orders of government' provision must prevail." *Id.* Finally, it rejected the landlord's argument that Hitz could have borrowed money to pay its rent, finding that nothing in the force majeure "clause requires the party adversely affected by governmental action or orders to borrow money to counteract their effects." *Id.* at *3.

While the court found that the force majeure clause was triggered, it did not allow Hitz to avoid rent payments entirely. Instead, it reasoned that the executive order did not prohibit restaurants from performing carry-out, curbside pick-up, and delivery services, so "to the extent that [Hitz] could have continued to perform those services, its obligation to pay rent is not excused by the force majeure clause" but is instead "reduced in proportion to its reduced ability to generate revenue due to the executive order." *Id.* Pending an evidentiary hearing, the court required Hitz to pay 25% of the rent because Hitz had estimated that 75% of its space was rendered unusable by the executive order. *Id.* at *4. The court thus used the percentage of space rendered unusable as a proxy, at least preliminarily, for the percentage of revenue lost.

As more courts begin to grapple with the application of force majeure clauses to COVID-19 shutdown orders, it will be interesting to see how courts apply those clauses. Of particular interest is whether courts follow *Hitz* in similar cases to conclude that performance is partially excused and, if so, how they determine what percentage is excused. In the meantime, *Hitz* signals that businesses that are unable to fulfill their contractual duties (or have a contractual counterparty that is unable to fulfill its contractual duties) in part or in full as a result of government-ordered closures due to COVID-19 should speak to counsel regarding the particulars of their situation, focusing especially on the force majeure language in the contract, the language of the relevant government order(s), and the degree to which performance is impaired.

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