

Coronavirus (COVID-19) Issues for Real Estate Owners and Operators

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As the economic and social impacts of COVID-19 continue to grow, the costs and consequences of an interruption of a party's ability to operate its business or fulfill its contractual obligations are rising rapidly. Many clients have begun to question (i) whether the force majeure provisions in their various contracts help or hurt them in this crisis; and (ii) whether their business interruption insurance addresses their economic losses.

Coronavirus and Force Majeure

Force majeure provisions in a contract excuse a party from performing its contractual obligations that become impossible or impracticable due to an event that the parties could not have anticipated or controlled. The party with the majority of non-monetary obligations under the contract is typically the main beneficiary of a force majeure provision and generally desires a very broad description of force majeure events. Conversely, the party with primarily payment obligations generally wants a very narrow and limited description of force majeure events. Both clauses typically allow the parties to terminate the contract if the interruption continues for a certain length of time.

Whether the impacts of COVID-19 on your business excuse you from your contractual obligations is solely determined by the specific contract provisions. There is no universally accepted definition of "force majeure" or "acts of God," nor are there any common law implied contractual protections from liability due to events that are beyond the reasonable control of the parties. While some newer contracts incorporate "pandemics" or "epidemics" into the definitions of force majeure, the majority of contracts do not contain such language, and the applicability of a force majeure provision may be dependent on whether the drafting attorney incorporated a broad/non-exclusive or narrow/exclusive definition of force majeure.

Broad/non-exclusive definitions generally define force majeure in a broad and ambiguous manner (such as any "act of God" or "any act beyond the reasonable control of a party") followed by the phrase "including, but not limited to" and a list of specific acts. The delineated list will frequently include some or all of the following:

1. Natural disasters such as floods, earthquakes, and severe weather events.
2. Epidemics and quarantines such as SARS, MERS, and COVID-19.
3. "Acts of God," which is rarely defined and implies natural disasters not otherwise listed within the force majeure definition.
4. Violence, including war, terrorist acts, and civil unrest.
5. Government action, including condemnation, changes in laws or regulations, and government delays.
6. Organized labor activity such as strikes.
7. Interruptions due to shortages of power, supplies, or transportation.

Narrow/exclusive definitions are typically limited to a very specific list of events. If an event is not listed, then it is excluded from coverage by the force majeure provision. Both types of definitions will frequently specifically exclude events that result from changing market conditions or if a party simply runs out of money.

Depending on the relative bargaining position of the contracting parties, force majeure provisions vary widely. Therefore, it is imperative to understand the type of force majeure provision and the specific triggering events in each material contract for a business. If you believe that COVID-19 has made your performance, or the counterparty's performance, impossible or impracticable and your review of the specific provisions supports a declaration of force majeure, you should immediately notify the counterparty in the manner set forth in the contract in order to preserve all your rights under the contract and thereafter follow the process set forth in the contract to document and resolve the issue.

Business Interruption Insurance and Event Cancellation Insurance

Insurance policies covering commercial property losses often include coverage for one or more types of business interruption coverages, including (i) business interruption; (ii) contingent business interruption; (iii) civil authority; (iv) ingress/egress; and (v) extra expense coverages. Unfortunately for

owners, under standard business interruption and contingent business interruption coverage for first-party property insurance, the business interruption loss must be directly tied to *physical* damage to the insured's property caused by the covered peril. Similarly, "ingress/egress" coverage requires a *physical* loss or damage to property that prevents ingress to or egress from the insured's premises, and "civil authority" coverage requires action from a civil authority that prohibits access to the insured's property. Therefore, under typical commercial property insurance business interruption coverage, business damages resulting from a slowdown in economic activity as a result of COVID-19 would not be covered. Operational losses such as a hotel's loss of room revenue would not be covered if it resulted from a decrease in occupancy stemming from the consequences of COVID-19 rather than from physical damage to the hotel itself.

Likewise, most "event cancelation insurance" policies do not cover loss incurred from contagious diseases unless a specific endorsement is negotiated to cover such events.

Nevertheless, the coverage provided by business interruption insurance and event cancelation insurance can vary significantly from policy to policy, and small differences in policy language can result in limited coverage for losses without physical damage to the property. Property and business owners should review their insurance policies with their legal counsel to make a determination whether a claim is viable. If your legal counsel determines that a claim could be viable, most policies require that the insured provide notice to the insurance carrier promptly following the loss, so the policyholder should notify the carrier in accordance with the notice provisions of the policy and should organize and preserve documentation that substantiates the costs and losses as a result of the event.

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