

# Real Property

The newsletter of the Illinois State Bar Association's Section on Real Estate Law

## From the Chair

BY WILLIAM J. ANAYA

I can only imagine the stress that you and your clients are experiencing during this time of national crises. COVID-19 has upended the world and impacted you, your practices and your clients, as well as our clients' businesses, in ways that are unprecedented in our lifetime.

The Illinois State Bar Association and your Real Estate Law Section Council have been active in responding to the needs of our member attorneys and their clients. I have been particularly impressed with the response of ISBA members willing to share information concerning the application

of new federal and state legislation and executive orders designed to address issues related to COVID-19 – including the CARES Act, Payroll Protection Program, Family First Act, the Emergency Paid Sick Leave and Medical Leave Expansion Act, Remote Signing for Wills and Deeds requiring Notaries, as well as changes to unemployment benefits, the WARN Act and its Illinois counterpart referred to as the Mini-Warn Act, OSHA and the SBA Loan Program.

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## COVID-19: Implications on Illinois Contract Law and the Doctrine of Commercial Frustration

BY THADFORD A. FELTON

COVID-19 is impacting businesses and their operations, and parties are looking for guidance in the event that one or the other party to a contract is, or claims to be, unable to fulfill its contractual obligations. Whether or not the COVID-19 pandemic excuses contract performance largely depends on the language of the contract and the facts that either support excusing performance or not. For example, following the 1918 Spanish Flu Epidemic, a court in California excused prompt performance,

but not complete performance, after carefully analyzing the contract and the facts incident to delayed performance. See *Citrus Soap Co. v. Peet Bros MFG., Co*, 50 Cal. App. 246 (1920).

### Nuances of the Doctrine of "Commercial Frustration"

Courts in Illinois strictly interpret contracts, and in the absence of a clear intention to excuse or delay performance,

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for example, as expressed in an unambiguous *force majeure* clause, courts will be reluctant to excuse or delay performance due to COVID – 19. However, one legal theory that may be available to contracting parties without reference to *force majeure* is that of “commercial frustration.”

In Illinois, the doctrine of commercial frustration is alive and well. The doctrine of commercial frustration will render a contract unenforceable if a party’s performance under the contract is rendered meaningless due to an unforeseen change in circumstances. Put another way, the doctrine of commercial frustration excuses performance only when the parties’ overall contractual intent and objectives have been completely thwarted by an unforeseen event. However, courts do not apply the doctrine of commercial frustration liberally, and a party seeking to excuse performance has a high hurdle to overcome.

### Satisfying The Two-Part Test

In Illinois, in order to apply the doctrine of commercial frustration, there must be a frustrating event that was not reasonably foreseeable and the value of the parties’ performance must be totally, or almost completely, destroyed by the frustrating event. Specifically, the party seeking to excuse performance under the doctrine of commercial frustration must satisfy the following, “rigorous,” two-part test.

- First, the event that has caused the commercial frustration must not have been reasonably foreseeable.
- Second, the value of the parties’ performance must be totally, or nearly totally, destroyed by the frustrating cause.

According to the Illinois Supreme Court, commercial frustration applies to:

cases where the cessation or nonexistence of some particular condition or state of things has rendered performance impossible and the object of the contract frustrated. It rests on the view that where from the nature of the contract and the surrounding circumstances the parties when

entering into the contract must have known that it could not be performed unless some particular condition or state of things would continue to exist, the parties must be deemed, when entering into the contract, to have made their bargain on the footing that such particular condition or state of things would continue to exist, and the contract therefore must be construed as subject to an implied condition that the parties shall be excused in case performance becomes impossible from such condition or state of things ceasing to exist.

*Leonard v. Autocare Sales & Service Co.*, 392 Ill. 182 (1946).

### Examples of Note

The doctrine of commercial frustration has been invoked in various breach of contract claims. Some examples are set forth below:

- Doctrine of commercial frustration found to apply where lessee entered into a lease for an adjacent property to expand its store and the main store was subsequently destroyed by fire. Court upheld lessee’s defense of commercial frustration finding that: (1) while it might be foreseeable that the main store would be destroyed by fire and the leased premises would remain intact, it was a remote contingency to provide for it in the lease and was not reasonably foreseeable; and (2) although it would not be physically impossible to operate the store from the leased premises as a separate entity, the evidence revealed that operations would have had to have been changed drastically and that the leased premises was never intended to be autonomous. *See Smith v. Roberts*, 54 Ill. App. 3d 910 (4<sup>th</sup> Dist. 1977).
- Doctrine of commercial frustration found to apply where lessee entered into a lease to operate a movie

theater and thereafter the applicable zoning was changed to prohibit the operation of a movie theater at that location. As a result of the zoning change, the lessee was unable to conduct any of its intended business. *See Scottsdale Limited Partnership v. Plitt Theatres, Inc.*, 97-C-8484, 1999 WL 281085 (N.D. Ill. March 31, 1999).

- Doctrine of commercial frustration found not to apply to lessee where federal government appropriated leased premises for a portion of the lease term for war purposes. The court found that since the subject matter of the lease, i.e., the property, had not been destroyed and was still in existence, the federal government’s appropriation merely carved out a short term occupancy and did not destroy the lessee’s lease-hold estate. *See Leonard v. Autocare Sales & Service Co.*, 392 Ill. 182 (1946).
- Doctrine of commercial frustration found not to apply to a natural gas utility that sought to excuse performance under a naphtha supply contract where demand for utilities’ services was decreasing and the price of naphtha was increasing because of federal decontrol of natural gas supplies and increase in crude oil prices which increased the price of naphtha. The court found that “the only certainty of the market is that prices will change” and that the frustrating events were to a large extent foreseeable. *See Northern Illinois Gas Company v. Energy Cooperative, Inc.*, 122 Ill. App. 3d 940 (3d Dist. 1984).

### Next Steps

Again, courts refuse to apply the doctrine of commercial frustration liberally. Parties seeking to excuse performance because of COVID-19 should carefully review the contract and analyze clauses, such as the *force majeure* clause, if any, in order to determine if the contract addresses the COVID-19

Pandemic.

And, of course, facts are critical. Be prepared to address the following issues:

- Is there evidence that supports the application of the doctrine of commercial frustration?
- What was the purpose of the contract?

- Was COVID 19 reasonably foreseeable?
- And, has the purpose of the contract been destroyed as a result of COVID-19?

If you have any contract questions, please contact Thad Felton or visit Greensfelder's COVID-19 resources page at: <https://www.greensfelder.com/covid-19-resources.html>.

[greensfelder.com/covid-19-resources.html](https://www.greensfelder.com/covid-19-resources.html).  
Greensfelder, Hemker & Gale, P.C. has offices located in Chicago, Belleville and St. Louis. ■