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# Legal Update

## An Act of God, or Another Failing Restaurant? Illinois Bankruptcy Court Rules on *Force Majeure* Clause in the Wake of COVID-19 Shutdown Order

The ongoing COVID-19 pandemic has raised pressing questions about how a *force majeure* provision in a lease will affect a tenant's obligation to pay rent. A recent decision from a bankruptcy court in Illinois provides useful instruction as to both how courts may analyze claims of *force majeure*, and how property owners may consider tailoring such clauses in the future.[1]

*In re: Hitz Restaurant Group* raised the question of whether a contractual *force majeure* clause excused a restaurant's post-bankruptcy failure to meet its rent obligations while dine-in restaurant service was banned in Illinois. Although the *force majeure* provision was fairly clear that governmental orders would constitute a *force majeure* event, the U.S. Bankruptcy Court for the Northern District of Illinois (the "Court") had to resolve three related questions: (1) the degree of causal connection between the *force majeure* event and the inability to perform contractual obligations; (2) the interpretation of the contractual provision "Lack of money shall not be grounds for Force Majeure"; and (3) the extent to which companies will be required to mitigate the effect of *force majeure* events.

### Background

On February 26, 2019, Hitz Restaurant Group, LLC ("Hitz") signed a ten-year lease with The South Loop Shops, LLC, to operate a bar and restaurant along South State Street in Chicago.[2] The lease contained the following *force majeure* clause:

> **Force Majeure.** Landlord and Tenant shall each be excused from performing its obligations or undertakings provided in this Lease, in the event, but only so long as the performance of any of its obligations are prevented or delayed, retarded or hindered by act of God, fire, earthquake, flood, explosion, actions of the elements, war, invasion, insurrection, riot, mob violence, sabotage, inability to procure or general shortage of labor, equipment, facilities, materials or supplies in the open market, failure of transportation, strikes, lockouts, action of labor unions, condemnation, requisition, laws, governmental action or inaction, orders of government or civil or military or naval authorities, or any other cause, whether similar or dissimilar to the foregoing, not within the reasonable control of the party or its agents, contractors or employees (each,

> individually and collectively, an event of "Force Majeure"). Lack of money shall not be grounds for Force Majeure.[3]

The restaurant took its premises in October 2019 as Giglios State Street Tavern.

Hitz was apparently having trouble paying its rent by at least November 2019, and on January 2, 2020, the landlord filed a complaint in state court.[4] On February 24, 2020—a day before the state-court action was scheduled for trial[5]—Hitz filed for bankruptcy in the Northern District of Illinois;[6] the Chapter 11 petition automatically stayed the state-court proceeding pursuant to 11 U.S.C. § 362(a).

COVID 19 was not yet known at the time of the state-court action,[7] and though it had entered the public consciousness by Hitz's bankruptcy, it had not yet caused mass shutdowns; while Chicago was home to one of the first confirmed cases in the United States, the state of Illinois had only two confirmed cases when Hitz filed its petition.[8] The pandemic quickly mushroomed, however, and Governor Pritzker of Illinois signed an executive order banning in-person restaurant service:

> Beginning March 16, 2020 at 9 p.m. through March 30, 2020, all businesses in the State of Illinois that offer food or beverages for on-premises consumption—including restaurants, bars, grocery stores, and food halls—must suspend service for and may not permit on-premises consumption. Such business are permitted and encouraged to serve food and beverages so that they may be consumed off premises.[9]

The ban was extended by subsequent executive orders, remaining in full effect through the end of May and at least partial effect afterwards.[10]

In response to Hitz's bankruptcy petition, the landlord filed a motion to enforce the payment of post-petition rent.[11] The landlord argued that Hitz remained responsible for paying rent under 11 U.S.C. § 365(d)(3), which states that a debtor-in-possession must "timely perform all the obligations of the debtor . . . from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected."

Hitz replied that the restrictions imposed by the executive orders had been "catastrophic," and claimed that it was "unable to operate under these circumstances, with a decimated customer base and most of its leasehold unusable."[12] Under the *force majeure* clause in the lease, it argued, its "ability to meet its obligations or enjoy its rights under the lease are impaired by 'governmental action or inaction' and 'orders of government.'"[13] Hitz thus concluded that it was "relieve[d] of its obligation to pay post-petition rent during the pendency of this crisis."[14]

The landlord, in turn, replied that Hitz remained obligated to pay because despite the executive orders, Hitz remained technically capable of payment: the orders had not "halted, prohibited, or otherwise hindered a person's ability to transfer . . . money to another."[15] It also pointed to the fact that the *force majeure* clause stipulated "[l]ack of money shall not be grounds for Force Majeure," and claimed Hitz could have attempted to stay afloat by offering delivery or takeout service, or by applying for a Small Business Administration loan.[16] Yet while the landlord noted that Hitz had failed to pay rent *after* its Chapter 11 filing, it did not argue that Hitz's *prior* delinquency showed that the executive orders were not, in fact, the cause of its distress.[17] Rather, it took the tack that Hitz "made poor decisions and elected not to operate its business" during the pandemic.[18]

## *In re: Hitz Restaurant Group*

The U.S. Bankruptcy Court for the Northern District of Illinois decided the dispute in a memorandum opinion issued on June 2, 2020.[19] The Court's analysis focused on the lease's *force majeure* clause. "Under Illinois law," it wrote, "a force majeure clause will only excuse contractual performance if the triggering event cited by the nonperforming party was in fact the proximate cause of that party's nonperformance."[20] The Court "reject[ed] out of hand" the landlord's claim that Hitz remained capable of payment, terming it "a specious argument" that "lacks any foundation in the actual language of the force majeure clause."[21] It determined that the executive orders were "unquestionably" the type of "governmental action" or "orders of government" contemplated by the *force majeure* clause; that the executive orders "hindered" Hitz's ability to perform, as required by the cause; and that "the order was unquestionably the proximate cause of Debtor's inability to pay rent, at least in part, because it prevented Debtor from operating normally and restricted its business to take-out, curbside pickup, and delivery."[22]

In reaching its conclusion, the Court specifically rejected the landlord's argument that Hitz failed to pay its rent due to a "lack of money."[23] The Court found that the executive orders were the proximate cause of Hitz's failure to pay rent, not lack of funds, and that the lack-of-money clause was thus inapplicable.[24] To the extent there was any conflict between the two provisions of the clause—on the one hand, specifically excusing performance due to "governmental action," and on the other, generally not excusing performance due to lack of funds—the Court found that as a matter of contractual interpretation, the more specific provision should prevail.[25] And the Court dismissed the landlord's suggestion that Hitz could have filed for a Small Business Administration loan, saying the landlord had not offered any supportive citations to case law, or to relevant provisions of the lease.[26]

Despite concluding that the force *majeure clause* applied, the Court found that Hitz "is not off the hook entirely."[27] Because the restaurant could still offer food for delivery or takeout—roughly calculated at 25 percent of the restaurant's utility—the Court ordered Hitz to pay 25 percent of the rent for April, May, and June; March had to be paid in full because that month's rent came due before the first executive order, while after June, the Court suggested rental payments would likely increase as restrictions are lifted.[28]

# Analysis

## The Proximate Cause of Nonperformance

The Court recognized that a *force majeure* clause will only excuse contractual performance under Illinois law if the triggering event is the proximate cause of the nonperformance, and found that the proximate cause of Hitz's failure to pay rent was "unquestionably" the executive orders. It wrote that the landlord's argument that post offices could still deliver a check, and the banks cash it, was "specious" and not relevant to the issue before the Court.

The Court was correct that the proximate cause was unquestioned. The landlord claimed that the executive orders neither a) hindered the ability to *mail* payment nor b) prevented Hitz from operating a takeout restaurant, but did not directly dispute the causal connection between the executive orders and Hitz's failure to pay rent. Nor did the landlord question whether Hitz's failure to operate a profitable restaurant, which had already resulted in Hitz's failure to pay rent in the pre-COVID-19 days of 2019 and 2020 and likely would have continued even without an executive order, was the proximate cause of its failure to pay rent. Thus, the Court did not have to decide whether the proximate cause of Hitz's failure to

pay rent was the issuance of the executive orders or Hitz's general inability to operate a profitable restaurant.

## Similar Results May Be Avoided—and Provisions Such as "Lack of Money Shall Not Be Grounds for Force Majeure" May Be Bolstered—by Adding Tailored Language to Future *Force Majeure* Clauses

The Court next addressed the question of whether the tenant's failure to pay rent fell within the *force majeure* exception that "[l]ack of money shall not be grounds for Force Majeure." In rejecting this argument by stating that Hitz "has not argued that lack of money is the proximate cause of its failure to pay rent," the court appears to have interpreted this provision as meaning that a lack of money shall not be considered a *force majeure* event. Textually speaking this is probably the correct interpretation, although when drafted, the landlord likely intended the phrase to mean that monetary obligations are not excused by events of *force majeure*.

Similar results may be avoided by adding more tailored language to future *force majeure* clauses. For example, a clause that begins "Landlord and Tenant shall each be excused from performing its non-monetary obligations or undertakings in this Lease . . ."—and/or that ends with the line, "In no event will any *force majeure* event excuse Tenant's monetary obligations, including its obligation to pay rent"—would be more likely to protect a landlord's intent in the eyes of a court, because such language focuses on which obligations are not subject to excuse even if a *force majeure* event exists.

## Property Owners May Wish to Consider Adding Provisions Requiring Tenants to Take All Reasonable Measures to Offset a *Force Majeure* Event

The third issue the Court implicitly addressed was the extent to which a party exercising a *force majeure* provision must mitigate the effect of the *force majeure* event. Although this obligation was not stated in the contract, many courts imply a duty to mitigate or to exercise due care to avoid the effect of the *force majeure* event.[29] In this case, the Court found that because the executive order permitted Hitz to perform carry-out, curbside pick-up and delivery services, Hitz could have generated some revenue from the property, and therefore was obligated to pay at least some portion of the rent amount (the Court estimated the amount at 25 percent of the rent due).

Still pressing its "lack of money" focus, the landlord argued that Hitz could have avoided "lack of money" if it obtained funds through a Small Business Administration loan. The Court, however, found no language in the *force majeure* clause requiring Hitz to mitigate its lack of funds, perhaps because Hitz was not claiming a lack of funds as a *force majeure* event. By contrast, in circumstances where the tenant was claiming that a *force majeure* event excused its rental obligations, the Court found the tenant had an obligation to mitigate the event: here, by performing carry-out service. Courts have acknowledged that the duty to mitigate requires only "bona fide" and not "heroic" efforts,[30] and where the line dividing the two is ultimately drawn will be determined by a reviewing court. In order to better ensure that a duty to mitigate is found when a party is seeking equitable relief, parties may wish to consider including an express contractual provision requiring the party invoking the *force majeure* clause to use all efforts reasonable under the circumstances to mitigate the impact of such *force majeure* event on its ability to perform.

## Conclusion

*In re: Hitz Restaurant Group* offers an early take on how at least one court may treat *force majeure* clauses when interpreting tenants' obligations to pay rent during COVID-19-related shutdowns. Although the Court does not seem to have been presented with what may have been the landlord's best argument with respect to whether the executive orders were the proximate cause of the tenant's failure to pay rent, and although a court's analysis will always hinge on the specific terms of the applicable *force majeure* clause and the particular circumstances at issue, the opinion demonstrates how some courts may interpret *force majeure* provisions. Contract parties may also be able to avoid unintended results by adding more precise language to future *force majeure* clauses—and by contractually requiring tenants to make all reasonable efforts to mitigate the *force majeure* event.

If you wish to receive regular updates on the range of the complex issues confronting businesses in the face of the novel coronavirus, please subscribe to our COVID-19 "Special Interest" mailing list.

And for any legal questions related to this pandemic, please contact the authors of this Legal Update or Mayer Brown's COVID-19 Core Response Team at FW-SIG-COVID-19-Core-Response-Team@mayerbrown.com.

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## Endnotes

[1] *In re: Hitz Rest. Grp.*, No. 1:20-bk-05012, 2020 WL 2924523 (Bankr. N.D. Ill. June 3, 2020).

[2] Exhibit A, *In re: Hitz Rest. Grp.*, Dkts. 7-1 & 7-2, No. 1:20-bk-05012 (Bankr. N.D. Ill. Mar. 12, 2020).

[3] *Id.* at Dkt. 7-2, § 29.5. The provision included several typos which have been corrected in the quotation.

[4] Complaint, *Kass Mgmt. Servs. v. Hitz Rest. Grp.*, Dkt. 1, No. 2020-M1-700029 (Ill. Cir. Ct. Jan. 2, 2020).

[5] Continuance Order, *Kass Mgmt. Servs. v. Hitz Rest. Grp.*, Dkt. 8, No. 2020-M1-700029 (Ill. Cir. Ct. Jan. 21, 2020).

[6] Voluntary Petition for Non-Individuals Filing for Bankruptcy, *In re: Hitz Rest. Grp.*, Dkt. 1, No. 1:20-bk-05012 (Bankr. N. D. Ill. Feb. 24, 2020).

[7] Cases of "viral pneumonia" were first announced by the Health Commission of Hubei Province on December 31, 2019. *See* Ctr. for Health Prot. of the H.K. Special Admin. Region Gov't, *CHP Closely Monitors Cluster of Pneumonia Cases on Mainland* (Dec. 31, 2019, 7:06 PM), https://www.info.gov.hk/gia/general/201912/31/P2019123100667.htm.

[8] *Coronavirus Confirmed In Chicago*; *Woman In Her 60s Being Treated For Symptoms*, CBS Chicago (Jan. 24, 2020, 9:30 PM), https://chicago.cbslocal.com/2020/01/24/first-case-of-coronavirus-confirmed-in-chicago/; *State of Illinois Public Health Officials Announce New Presumptive Positive COVID-19 Case In Illinois*, Ill. Dep't Pub. Health (Feb. 29, 2020), https://www.dph.illinois.gov/news/state-illinois-public-health-officials-announce-new-presumptive-positive-covid-19-case-illinois.

[9] Ill. Exec. Order No. 2020-07 (Mar. 16, 2020), https://www2.illinois.gov/Documents/ExecOrders/2020/ExecutiveOrder-2020-07.pdf.

[10] Ill. Exec. Order No. 2020-18 (Apr. 1, 2020), https://www2.illinois.gov/Documents/ExecOrders/2020/ExecutiveOrder-2020-18.pdf; Ill. Exec. Order No. 2020-33 (Apr. 30, 2020), https://www2.illinois.gov/Documents/ExecOrders/2020/ExecutiveOrder-2020-33.pdf; Ill. Exec. Order No. 2020-38 (May 29, 2020), https://www2.illinois.gov/Documents/ExecOrders/2020/ExecutiveOrder-2020-38.pdf.

[11] Motion to Enforce Debtor-in-Possession's Obligation to Pay Post-Petition Rent, Dkt. 21, *In re: Hitz Rest. Grp.*, No. 1:20-bk-05012 (Bankr. N. D. Ill. Apr. 14, 2020).

[12] Debtor's Combined Response to Motion of Kass Management Services, Inc. and The South Loop Shops, LLC for Relief from the Automatic Stay and to Compel Payment of Rent at 3, *In re: Hitz Rest. Grp.*, Dkt. 43, No. 1:20-bk-05012 (Bankr. N.D. Ill. May 12, 2020).

[13] *Id.*

[14] *Id.* at 4

[15] Creditors' Reply to Debtor's Response to Creditor's Motion to Compel Payment of Rent and Second Motion for Relief from the Automatic Stay at 3, *In re: Hitz Rest. Grp.*, Dkt. 45, No. 1:20-bk-05012 (Bankr. N.D. Ill. May 26, 2020).

[16] *Id.* At 3–4.

[17] *Id.*

[18] *Id.* at 2.

[19] *In re Hitz Rest. Grp.*, 2020 WL 2924523..

[20] *Id.* at *2.

[21] *Id.* at *3.

[22] *Id.* at *2.

[23] *Id.* at *3.

[24] *Id.*

[25] *Id.* at *3 n. 7.

[26] *Id.* at *3.

[27] *Id.*

[28] *Id.* at *2–4.

[29] *See, e.g., Gulf Oil Corp. v. F.E.R.C.*, 706 F.2d 444, 454 (3d Cir. 1983) ("[W]e conclude that in order to use force majeure events to excuse nonperformance, Gulf must show that it tried to overcome the results of the events' occurrences by doing everything within its control to prevent or to minimize the event's occurrence and its effects.").

[30] *See, e.g., ConEd v. Allied-Gen. Nuclear Servs.*, 731 F. Supp. 850, 860 (N.D. Ill. 1990).