

CONTRACTS AS EMERGENCY LAW: *Injecting Certainty to Uncertain Times*

Professor Xuan-Thao Nguyen
Gerald L. Bepko Chair in Law
Director, Center for Intellectual Property & Innovation
Indiana University, McKinney School of Law --USA
xunguyen@iu.edu

Outline

United States Emergency Laws, in
General

Missing from U.S. Emergency Laws

Contract Law as Emergency Law

China's Approach to the Contracts
Emergency

Last Thoughts?

Emergency Laws, in General

Emergency Laws?

- All legislations referring to the state of emergency
- Empower government to perform actions or impose policies that it would normally not be permitted to undertake.

State of Emergency?

- Natural disaster
- Civil unrest
- Armed conflict
- Medical/Public Health Pandemic/Epidemic

Emergency Laws, in the United States

In the United States:

- The Framers of the Constitution did not grant the “Emergency Powers” to the Executive Branch.
- The Legislative Branch has the power to legislate.
- The Legislative Branch passed the Emergency Powers & Framework Statutes:
 - **National Emergencies Act**, 50 U.S.C. §§ 1601-1651: imposes procedural requirements on the President to declare “a national emergency”. There are **136 statutes** dictating when powers become available for the President after the declaration of a “national emergency.”
 - **Public Health Act**, 42 U.S.C. §247d, empower the Secretary of Health & Human Services to declare a public health emergency,
 - **Robert T. Stafford Disaster Relief & Emergency Assistance Act** (or earlier known as the “Disaster Relief Act): Allows a governor to petition the President for a declaration of a major disaster or emergency”, 42 U.S.C. §§ 5121 *et seq.*
 - Source: https://www.brennancenter.org/sites/default/files/2019-10/AGuideToEmergencyPowersAndTheirUse_2.13.19.pdf;
<https://www.brennancenter.org/our-work/research-reports/guide-emergency-powers-and-their-use>

Emergency Laws, in the United States

In the United States:

- Can Congress also declare a “national emergency”?
 - Legislative Branch: passed 123 statutes that allow the Executive Branch/the President to utilize after the President declares “a national emergency” per the National Emergencies Act, 50 U.S.C. §§ 1601-1651.
 - In addition, there are 13 statutes that are available when Congress declares “a national emergency”

Emergency Laws, in the United States

In the United States:

- **Federalism:** Federal government and State government share powers
- 50 States with their own Emergency Laws
 - State and Local governments share power

Emergency Laws, in the United States

In the United States:

- State and Local governments share powers:
 - Recent example, NYC Mayor Bill de Blasio declared a state of emergency to give him new powers to combat Covid-19 when 95 residents were sicken.
 - The declaration means de Blasio's government has the power to, among other things:
 - *Implement curfews*
 - *Shut down public transit*
 - *Close public spaces*
 - *Restrict street access*
 - *Regulate where vehicles can go within the city*
 - *Direct hospitals to postpone elective procedures*
 - *Ration goods and impose price caps*
 - *Suspend or limit the sale of alcohol, firearms, or explosives*

Missing in Emergency Laws & Their Framework?

What to do with Agreements between contracting parties when there is a state of emergency?

- Relationships between individuals
- Relationships between entities
- Fundamental in all sectors of the economy and society.
- Suspension, Nonperformance, Breach, Damages
- Countries with Robust Contract Law and Legal System vs. Countries Without?

Missing in Emergency Laws & Their Framework?

Think of all the Contracts, Breach and Nonperformance during Covid-19

- Global Supply Chain (\$\$ Billion USD)
- Travel Industry
- Hospitality Industry
- Insurance Industry
- Sports & Entertainment Sector
- Labor/Employment
- Leases (Buildings, Rentals, Auto, Tangible Property); Licenses (Intangible Property)
- Etc.

Contract Law as Emergency Law

Throughout history ...Human and Contractual Relationships are Frequently Interrupted by War, Plague, Natural Disasters, etc.

From Ancient Time to the Present
(*Western perspective*): The Development of Contract Law Addresses Unexpected State of Emergency

Contract Law as Emergency Law

Impossibility Doctrine

Frustration of Purpose Doctrine

Force Majeure

Duty of Performing in Good Faith

Contract Law as Emergency Law

Impossibility Doctrine

Roman Law Roots: “inpossibilium nulla obligatio est” or “there is no obligation to the impossible”. A party is excused from contract performance when the performance is impossible at the time the contract is made (Initial Impossibility). If the party is not at fault but performance nevertheless becomes impossible after contract creation, the party is excused (Subsequent Impossibility).

The standard of judging impossibility to excuse contract performance, however, is objective or absolute, not subjective or personal.

- The party cannot escape liability “if performance is merely beyond his power” but beyond “anyone’s power”.
- the party cannot avoid liability “merely because he was not at fault in the ordinary sense of the word.”

Contract Law as Emergency Law

Impossibility Doctrine

Canon Law Roots: Canon Law's Doctrine of Changed Circumstances.

- Under Canon law, although breaking a promise is morally wrong, a party can legitimately break a promise when circumstances have sufficiently changed.
- St. Augustine, according to Gratian's Decretum, stated that "one need not keep a promise to return a sword to a person who has become insane."
- Decretum included that the condition for a promise was "if matters remain in the same state."
- The medieval Italian jurist Baldus de Ubaldis later read this condition concerning promises into the civil law as *clausula rebus sic habentibus* or frustration of purpose as known by common law.
- The great Thomas Aquinas, in the thirteenth century, relied on theory of equity to argue that a promise is a kind of law, and the law is not binding in circumstances that the promisor did not intend to be bound.
- In the subsequent 16th and 17th centuries, Thomas Aquinas' view continued that the promisor is not bound if the change of circumstances constitutes the "unique reason" or "unique cause" to performance of the promise or the "presumption of facts" for the condition.
- One of leading English cases in contract law embracing the doctrine of changed circumstances is *Taylor v. Caldwell* of 1863 in which Judge Blackburn released the owner of a music hall from contract obligation after the hall was destroyed by fire.

Contract Law as Emergency Law

Modern Approach in Contract Law as Emergency Law

- Old English cases in *Abbot of Westminster v. Clerke*, 63 (K.B. 1536)(act of law); *Hyde v. Dean of Windsor* (1597, death); *Lawrence v. Twentiman*, (1668, plague): changes of the circumstances render contract performance to impossibility.
- In modern time, courts consider hardship, high costs due to market price changes and war outbreak causes different routes be taken for the fulfillment of the contract, are changes beyond anticipation and control.
 - 10x, 30x the anticipated cost, extreme cases of higher costs.
 - The doctrine is very rarely applied. Impossibility must be absolute.
 - Courts want to preserve the contracts as agreed by the parties. Courts don't want to redraft or add new terms/provisions to contractual agreements. Courts want parties to have freedom of contracts and freedom from contracts.

Contract Law as Emergency Law

Impossibility Doctrine; Spanish Influenza of 1918 (killed 700,000 Americans and closed down the nation for several months from fall 1918 to spring 1919):

- *Sandry v. Brooklyn School Dist. No. 78 of Williams County*, (Supreme Court North Dakota 1921)
- *Montgomery v. Board of Education of Liberty Twp., Union County* (Supreme Court of Ohio 1921)
- *Crane v. School District. No. 14 of Tillamook County* (Supreme Court of Oregon, 1921)
- Employers refused to pay school bus drivers during school closure per government's public health order in 1918-1919. Employers asserted impossibility defense to their nonperformance (refused to pay per the contract).

Contract Law as Emergency Law

As war, epidemics, pandemics, natural disasters frequently occur (think, in 13 years the global community witness 3 pandemics SARS, H1N1 and Covid-19)

Contract agreements: allocate the risk of loss

Force Majeure: *contract provision that allocates the risk of loss if performance becomes impossible or impracticable as a result of an event or effect that the parties could not have anticipated or controlled.*

If a force-majeure clause lists specific force-majeure events, there is no need to prove that the force-majeure event was unforeseeable, only that **it happened**. TEC Olmos Conoco v. Phillips Co., 555 S.W.3d 176, 183 (Tex.App.—Houston [1st Dist.] 2018); Eastern Air Lines, Inc. v. McDonnell Douglas Corp., 532 F.2d 957, 992 (5th Cir.1976).

Force Majeure: allow contracts to address emergency.

Contract Law as Emergency Law

Duty of Performing in Good Faith

Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.

Restatement (Second) of Contracts § 205.

Williston on Contracts, states:

“The duty [of good faith and fair dealing] embraces, among other things, an implied obligation that neither party shall do anything to injure or destroy the right of the other party to receive the benefits of the agreement ... a party to a contract is considered to have breached the implied covenant of good faith and fair dealing if it acts in bad faith, or if it engages in inequitable conduct in the performance of its contractual obligations or undertakings.”

The Duty is imposed on the party asserting Impossibility defense, excuses per Force Majeure, and contract performance/nonperformance.

China's Approach to the Contracts Emergency

If a nation does not have a robust body of contract law as described above as *private* emergency law ...

China's approach:

China Council for the Promotion of International Trade (CCPIT) issued 5,637 force majeure certificates valued at \$72.47 Billion USD to shield Chinese companies from not performing their contracts.

Impact on international partners in these contracts??? Bad faith???

China's Approach:



China's Approach:

Guidance from the Supreme People's Court in the Period of the Prevention and Control of Infectious Atypical Pneumonia" (Fa [2003] No. 72)

Article 3 of the Notice provides that "...disputes caused by the government and relevant departments' administrative measures to prevent the SARS epidemic that directly result in the contract being unable to be performed, or due to the impact of the SARS epidemic, the parties to the contract being unable to perform at all, should be dealt properly in accordance with the provisions of Articles 117 and 118 of the 'Contract Law.'" (provisions that deal with **force majeure**).

China's Approach:

Article 26 of the Interpretation on Certain Issues Concerning the Application of the Contract Law (II) (Fa Shi [2009] No. 5, 《最高人民法院关于适用<中华人民共和国合同法>若干问题的解释(二)》(法释[2009]5号) issued by the Supreme People's Court on 24 April 2009 **introduced the concept of 'change of circumstance,'** which provides that "... [where there are] significant changes that could not be foreseen by the parties at the time of conclusion of the contract, and **such changes are not caused by force majeure and do not constitute commercial risks,** and where continuance of performance will be obviously unfair to one of the parties or will not achieve the purposes for which the contract was concluded, the people's court shall, upon request by a concerned party, determine whether the contract should be modified or terminated on the basis of the **principle of fairness** and by **considering the actual situation** prevalent in the case. "

China's Approach:

The main factors for courts to determine if there has been a change of circumstance include: "(i) has there been a significant change to the circumstances prevailing at the time the contract was signed, when viewed **objectively**; (ii) has the change of circumstance occurred after the conclusion of the contract and before the fulfilment of the obligations due under it; (iii) could the change of circumstance have been **foreseen** when the contract was concluded; (iv) can the change of circumstance be **attributed** to both parties; and (v) would it be obviously **unfair** to oblige the party to continue to perform the contract or will performance not achieve the purposes for which the contract was concluded? "

China's Approach:

On April 20, 2020, China's Supreme People's Court ("SPC") published its Guiding Opinion on Several Issues Concerning Proper Trial of Civil Cases Involving COVID-19 Pandemic (I) (关于依法妥善审理涉新冠肺炎疫情民事案件若干问题的指导意见 (一) ; "Opinion").

The SPC gives lower courts in China guidance on handling civil cases relating to the COVID-19 pandemic.

The Guiding Opinion offers detailed guidance on applying **force majeure and other principles to contracts when their performance is impacted by COVID-19** and addresses a number of other issues that the SPC has identified as affecting judicial processes.

China's Approach:

Guiding Opinion on Several Issues Concerning Proper Trial of Civil Cases Involving COVID-19

Reaffirming the “changed circumstance” doctrine under Chinese contract law (see Article 29 on Contract Law Interpretation issued in 2009 by SPC). The Guiding Opinion states that “if the pandemic or related control measures only make performance more difficult rather than impossible, then the parties should seek to renegotiate contract terms and the court should support continued performance rather than granting contract rescission as a remedy.

If continued performance is unfair to one of the parties, that party can seek judicial support for revisions to the contract's terms. If the pandemic or related control measures render the purpose of the contract unachievable, the court should support either party's request to rescind the contract.”

Contract Law as Emergency Law

Final Thoughts?

- “State of Emergency” laws:
Uncertainty
- Contract Law as *Private* Emergency Law:
 - Anticipate Uncertainty
 - Inject Certainty to the Age of Uncertainty.