



## COVID 19 RESOURCES FOR NONPROFITS

# CONTRACTS ISSUES DURING COVID-19

# TABLE OF CONTENTS

What is a contract? 1

Have I entered into a contract? 2

What documents should I review? 2

If I need to change or cancel a contract, where should I look first? 3

How can I change or cancel a contract? 3

What are some issues that come up with government contracts? 6

What happens if a party breaches a contract? 8

What is a “breach”? 8

What damages will a court award? 9

How are contractual damages impacted by insurance coverage? 10

How can I negotiate a contractual change with my counterparty? 12

How do I enforce a contract? 16

What should I think about for new contracts during COVID-19? 16

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# CONTRACT BASICS

Some examples of common contracts for nonprofit organizations that may be relevant to you include: event contracts, service contracts, insurance contracts and equipment leases.

Local laws and regulations — and how they are interpreted by state courts — will have a big role in how your contracts operate. So, you or your attorney will need to pay close attention to the laws applicable to your contract (which are usually specified in the contract).

## WHAT IS A CONTRACT?

A contract is an agreement between two or more people or entities that creates obligations that are enforceable in court. For there to be a valid a contract, there must be an “offer” by one party that is “accepted” by the other party in exchange for “consideration.”

- **Offer.** The offer must be adequately communicated and it must contain sufficiently certain terms about the key elements of the transaction (usually, the price, amount and any other key terms).

- **Acceptance.** The offer must be accepted without changes. An offer can be accepted in writing or, in most cases, orally. It can also be accepted by silence if the one party takes steps to receive the benefits from the other.
- **Consideration.** Consideration is what the parties have agreed to exchange. For example, I will work for you for eight hours, if you pay me \$15 per hour. Both parties must benefit in some way from an agreement. Examples of consideration include money, employment, goods and

services, and promises to do (or not do) something.

### HAVE I ENTERED INTO A CONTRACT?

While contracts are often thought of as formal agreements, a contract can be formed on a much more informal basis. However, some contracts must be in writing to be enforceable. These contracts include:

- contracts for the sale of goods over \$500;
- contracts that cannot be completed in less than one year;
- leases for a period of less than one year (under New York state law);
- assignments of insurance policies (under New York state law); and
- contracts for the sale of real estate.

### WHAT DOCUMENTS SHOULD I REVIEW?

When reviewing your contract, be sure to collect and review the full set of documents that make up the contract. These documents might include:

- amendments and renewals (common in leases and in government contracts);
- riders (common in leases);
- other agreements or documents referenced in the main contract, such as requests for proposals and proposals in government contracts;
- subcontracts or subleases; and
- schedules, annexes and exhibits.

# CHANGING OR CANCELING A CONTRACT

## IF I NEED TO CHANGE OR CANCEL A CONTRACT, WHERE SHOULD I LOOK FIRST?

Certain clauses in a contract will say when and how the contract can be amended or terminated. Look for paragraph headings and words such as “amendment,” “termination,” “cancellation,” “breach,” “material adverse change,”

“repudiation,” “force majeure” and “Act of God.” Remember to review the entire agreement to understand how these particular provisions operate — a particular section might depend on or be modified by other sections.

## HOW CAN I CHANGE OR CANCEL A CONTRACT?

### Amendments

With an amendment, you can add, delete or correct a part of the contract without completely replacing the contract. This can be helpful if, for example, you want to postpone

or reschedule an event due to the outbreak of COVID-19 instead of cancelling it.

## COVID 19 RESOURCES FOR NONPROFITS

First, look for an “amendments” provision in the contract to find out who has the right to amend and what is required to amend. For example, amendment provisions often require that the amendment be in writing and approved by the

### Cancellation

Depending on your circumstances, you may want to cancel the contract. This will depend on whether you want to “undo” the contract altogether and are comfortable giving up its benefits and potentially paying a cancellation penalty.

First, look for a “cancellation” or “termination” clause, which will tell you whether cancellation is an option and explain the process you will need to follow to cancel. Some contracts do not provide an option to cancel, which means that you may be considered in “breach” of the agreement if you decide to not comply with your obligations. In that case, you should seek legal advice before taking any steps that the other party may view as you not complying with your obligations.

counterparty. These provisions also often include notice requirements.

You may find it helpful to work with an attorney to negotiate and draft the amendment.

You may be able to request a refund for a deposit or other amounts already paid. On the other hand, the contract may say that you have to pay a fee if you cancel, such as all or part of your deposit. This is sometimes called “liquidated damages.”

If the contract allows cancellation, note that cancellation clauses often require giving the counterparty advance written notice of your intent to cancel. The contract may also specify cutoff dates after which the cancellation process becomes more complicated and expensive.

In some cases, cancellation of a contract, if permitted under the agreement and done correctly, may be the most favorable outcome for all parties.

### “Force Majeure” Clauses

Your contract may also have a “force majeure” clause that offers another way of terminating a contract or excusing or postponing some of the parties’ obligations. Generally, a force majeure clause says that a party does not have to continue with its obligations under the contract if its performance becomes impractical, illegal, impossible or inadvisable due to certain events that are outside the control of either party (such as acts of God, war, strikes, etc.).

Some force majeure clauses specifically include epidemics or pandemics, and/or events resulting from governmental laws, regulations or actions. These kinds of clauses provide the strongest basis for a party to argue that it does not have to comply with its obligations under the contract because of COVID-19 and/or government stay-at-home orders. On the other hand, a force majeure clause may specifically exclude pandemics, which makes it much more difficult for the parties to use the force majeure clause to get out of the contract. Other force majeure clauses are more general. In that case, whether the clause applies will depend on its

specific language as well as any other relevant provisions of the contract and the specific circumstances around the contract.

In New York, if a force majeure clause contains specific examples, a court will typically find that only the types of events listed as examples apply. If the clause also includes a catchall provision (such as “and any other events”), courts will generally limit it to include only events of the same kind as the listed examples. Similar to cancellation clauses, a force majeure clause may have a notice requirement and/or a penalty (such as the loss of a deposit). There may also be an obligation for parties to attempt to lessen damages, as discussed below.

As a result, a force majeure clause should be reviewed closely to determine whether it allows the parties to excuse or postpone their obligations under their contract or whether it specifically prevents the parties from relying on COVID-19 to modify or terminate their responsibilities.

## COVID 19 RESOURCES FOR NONPROFITS

### Impossibility and Frustration

Even if your contract does not have a termination or force majeure clause, you may be able to rely on “impossibility” and “frustration of purpose” to excuse your performance.

“Impossibility” is difficult to establish. It excuses a party’s performance only if the performance is truly and objectively impossible, for example, due to the destruction of the venue for the performance or due to a government law making performance illegal. The impossibility must also be the result of an unanticipated event that could not have been guarded against in the contract. Similar to force majeure, courts generally only allow impossibility in extreme situations. However, a court could find that a government stay-at-home order made performance impossible.

“Frustration of purpose” is similar to impossibility, but focuses on whether a specific event has completely

undermined the purpose of the contract. The event must have been unexpected and it must also render the contract entirely valueless to the affected party (and not simply more expensive, at least under New York law). In addition, the parties must have understood that the now-frustrated purpose was the sole reason for entering into the contract. Depending on the scenario, frustration of purpose could be another argument to not comply with a contract as a result of COVID-19, although this will be highly context-specific. For example, if an organization previously agreed to lease a venue for an event that must be cancelled due to COVID-19, the organization may be able to argue that the sole purpose of the contract — obtaining a venue for the event — has been frustrated.

## WHAT ARE SOME ISSUES THAT COME UP WITH GOVERNMENT CONTRACTS?

Government contracts are usually lengthy and often refer to many other documents. The analysis for these contracts

will likely involve reviewing any COVID-related government orders and guidance issued by the relevant federal, state



## COVID 19 RESOURCES FOR NONPROFITS

or local authority. You should closely monitor relevant guidance issued in your jurisdiction and by the particular agency with which your organization has contracted, and consider how that guidance impacts the terms of each of your relevant government contracts.

For example, certain of New York City's service contracts provide that the City may suspend the contractor's operations if there is a state of emergency declared by the Mayor without incurring any damages. At least some of the City's service contracts also include force majeure clauses governing termination by the contractor or the City. On the other hand, certain of New York State's contracts give only New York State the right to invoke a force majeure and not comply with its obligations and do not address what happens if an event makes it impossible for the other party to perform.

Federal government contracts may contain numerous provisions relevant to issues raised by COVID-19, including:

- (i) excusable delay provisions, providing protections for delays triggered by events outside the parties' control, which may include epidemics and quarantine restrictions;
- (ii) changes clauses, authorizing the contracting agency

to enter into a changes order; (iii) stop-work order clauses, which may authorize the contracting agency to order a contractor to stop all work called for by the contract for a specified period; and (iv) termination for convenience clauses permitting the contracting agency to terminate the contract at the government's discretion. Certain of these clauses may allow for an adjustment of the contract to account for reasonable increases or decreases in costs due to the change or stop-work order. Such clauses may also require the contractor to take steps to minimize the incurrence of further costs to the government.

The above are only examples of the types of provisions that you may find in your government contracts. The government contracts applicable to your organization will likely differ, and you should review (or consult with a lawyer about) their specific provisions and how to interpret them in light of COVID-19.

# ENFORCING A CONTRACT: BREACH AND DAMAGES

## WHAT HAPPENS IF A PARTY BREACHES A CONTRACT?

If attempts at renegotiating contract terms because of COVID-19 are unsuccessful, a party might consider breaching a contract — simply not performing some or all of its obligations. It is important to understand what types of

behaviors may be considered a breach, because a breach by one party may entitle the other party to damages unless there is a legal defense for non-performance (such as a force majeure clause, impossibility or frustration of purpose).

## WHAT IS A “BREACH”?

A breach is a failure, without legal excuse, to perform all or any part of a contract. Breaches of contract can be minor or material. A breach is likely material if it is a serious enough violation of the contract that it defeats the overall purpose of the agreement. A minor breach, on the other hand, occurs when a party fails to perform part of the contract, without violating the entire contract.

Typically, the breaching party must be given a chance to correct the breach. So, even if you believe your counterparty is in breach of its obligations, you may not be able to stop complying with your own obligations immediately and instead may need to wait. When a breach happens (typically at the time for delivery of goods or performance of services), the non-breaching party may stop any performance it

## COVID 19 RESOURCES FOR NONPROFITS

owes to the breaching party and resort to any remedies available for breach of contract. For example, imagine you have hired a caterer to provide food for an event that you have cancelled due to a shelter-in-place order. After being

### Legal Remedies for Breach of Contract

The main remedies for breach of contract if you pursue litigation are monetary damages and specific performance.

- Monetary damages are meant to compensate the non-breaching party for losses suffered due to the other party's breach. These include direct damages resulting from the breach as well as indirect damages that are sufficiently connected to the breach.
- Specific performance requires the breaching party to perform its obligations under the contract. This remedy is usually difficult to obtain.

## WHAT DAMAGES WILL A COURT AWARD?

There are three types of damages that may be awarded by a court:

- **Expectation damages**, which are meant to put the other

notified, the caterer would be entitled to stop preparing the food and, after confirming that you do not intend to go forward with the contract, pursue legal remedies.

- For a sale of goods, if there is a breach by the seller, the buyer can cancel the contract, recover the goods or seek specific performance. If there is a breach by the buyer, the seller can withhold goods if they have not yet been delivered, recover goods if they have been delivered, or, in limited circumstances, force the buyer to accept the goods.

party in the position they would have been in if the breach had not occurred. This is the most common form of damages.

## COVID 19 RESOURCES FOR NONPROFITS

- **Reliance damages**, which are intended to put the injured party in the position they would have been in if the contract had never been made.
- **Restitution**, which is intended to ensure that the breaching party is not unjustly benefited by the breach. The breaching party must restore to the non-breaching party any benefit it gave to the breaching party. Where both parties are unable to fully meet their obligations under a contract, such as due to COVID-19, a court may use restitution as a way to reach a fair result by compensating each party based on the extent of its performance under the contract.

In all cases, the non-breaching party must take steps to minimize — or “mitigate” — its damages, and therefore will

not be awarded for losses that it could have reasonably avoided. The parties may also agree by contract to exclude certain kinds of damages or include additional requirements on parties to mitigate damages.

A contract may also include liquidated damages provisions, which set damages at a specific amount and would not require going to court. If challenged in a litigation, liquidated damages provisions will generally be upheld if the specified amount is proportional to the likely loss and the amount of actual loss is impossible or difficult to calculate. On the other hand, courts will not enforce liquidated damages provisions if the specified amount is clearly disproportionate to the likely loss.

## HOW ARE CONTRACTUAL DAMAGES IMPACTED BY INSURANCE COVERAGE?

Insurance coverage may be helpful to protect against any economic loss or liability due to breach or failure to perform as a result of the COVID-19 pandemic. Examples of potentially applicable insurance include

business interruption insurance, event cancellation insurance, commercial general liability coverage, workers’ compensation insurance and specialized insurance. While the terms of insurance policies vary and are generally

## COVID 19 RESOURCES FOR NONPROFITS

modified to account for specific risks applicable to the insured party, consider the following when addressing contract issues during COVID-19:

- As an initial matter, collect and review your existing insurance policies and contact your insurance broker or agent to (i) assess whether you have applicable coverage and (ii) file any claims within the required time period.
- Consult the damages and indemnification provisions of any contracts where you have incurred damages that you would like to recover under an insurance policy. Those provisions may include offset language, which means you would deduct any amount paid out by your insurance company from the amounts owed to you by the other party (and vice versa, with respect to the agreement with your counterparty).
- The availability of insurance may also affect your negotiations with your counterparties. In particular,
  - the counterparty may be less likely to work towards a resolution if it is aware that you are able to recover under an insurance policy.
  - If you are interested in purchasing any new or additional insurance coverage to protect against damages or liabilities incurred during the COVID-19 pandemic, you should consult with your insurance carrier or agent. Note, however, that any such insurance policies would only apply to losses and/or liabilities arising in the future and not those that have already occurred.

# PRACTICAL CONSIDERATIONS IN CONTRACT NEGOTIATIONS AND ENFORCEMENT

## HOW CAN I NEGOTIATE A CONTRACTUAL CHANGE WITH MY COUNTERPARTY?

The legal remedies described above would only apply if you (or your counterparty) are successful in litigation, which can be a very long and costly process. As a result, if there is a contractual dispute or an anticipated or possible breach of an agreement, renegotiating the contract may be the most practical and speedy option for both parties. Due to the uncertainties caused by COVID-19, parties may be more flexible and open to modifying the contract. In planning for and engaging in negotiations with your contractual counterparty, consider the following:

- [Think through how you would like to change the contract and how you expect your counterparty to respond.](#) Consider the ideal scenario and whether the change you seek is a “must have.” It is also important to anticipate how the counterparty might respond to your proposal, including in light of the other alternatives available to it.
- [Consider a preliminary, informal conversation with the counterparty.](#) Depending on the nature of your relationship with the counterparty, initiating an informal,

## COVID 19 RESOURCES FOR NONPROFITS

cordial conversation to understand preferences and sticking points may make further negotiations more productive. This conversation should happen when the issue first comes up, before the discussions escalate to legal formalities (such as giving notice of a potential breach).

- **Analyze contractual provisions applicable to the situation.** The next step will be to review the applicable contract(s) for any relevant provisions, including notice, amendment, termination and force majeure provisions.
  - **Consider the damages to all impacted parties.** As discussed above, damages may include any costs already incurred by the counterparty in performing under the contract as well as the loss of expected profits. In addition, keep in mind the possibility of damages to any third parties, such as subcontractors.
  - **Determine whether there is any ability to mitigate damages.** Because the law usually requires the injured party to mitigate damages, it is important to consider whether you or your counterparty is able to do so, and if so, to take the appropriate steps as quickly as possible.
- **Plan out your negotiation strategy.** The following steps may help you prepare for approaching a counterparty regarding amending or cancelling a contract:
    - Review the details of any prior communications about the parties' obligations under the contract and what each party agreed to. These communications will likely inform your negotiation strategy and the terms you may be able to obtain going forward.
    - Assess your and your counterparty's respective leverage in the negotiation. How much does the language of the contract support or weaken each party's position? Has COVID-19 rendered either party's obligations more difficult and how might that impact the party's willingness to renegotiate certain terms? The goal is to identify negotiation incentives for both parties.
    - Consider whether it is important to your organization to maintain a relationship with the particular counterparty, which will inform the positions you are willing to take and how flexible you can be in the negotiation.

## COVID 19 RESOURCES FOR NONPROFITS

- Determine what your opening negotiation position will be and what you are looking to achieve in an ideal world as well as what you are willing to accept in order to compromise and arrive at a mutually agreeable solution.
- Keeping in mind the above, consider your possible responses to the counterparty's anticipated claims and demands. It may be helpful to engage in a "mock" negotiation in order to prepare your responses and practice responding in a measured and amicable manner.
- Finally, prepare for the possibility that the negotiation may happen in parts, and think through how you would communicate to the counterparty that you would like to pause the negotiations and resume them at a later time. This may come up in a situation where the counterparty offers a solution that requires further thought and/or sign-off from others.
- **Leaving your lawyer out of it (at first).** While consulting with a lawyer when developing a negotiation strategy and reviewing the terms of a contract is advisable, the presence of (or even reference to) lawyers can sometimes make a negotiation more contentious than is necessary.

As a result, you may want to start with an informal negotiation. Of course, you can and should consult with a lawyer throughout the process.

- **Keep complete records.** Throughout the life of a contract, you should keep clear and detailed records of the actions taken by each party and all related conversations. As a best practice, even if not required, all changes to the contract should be in writing and all written communications saved in a designated location. You should keep contemporaneous notes of any conversations with the counterparty and also save those in a designated location. (At the same time, it is important to remember that anything in writing may be produced in court if there is a future dispute.)
- **Example of copier lease negotiation.** As an example, you want to try to renegotiate an office copier lease, which is currently not in use as a result of shelter-in-place orders. Let's assume that you are happy with the equipment and have a good relationship with the leasing company. When reading through the lease, you don't see a force majeure clause, but you are able to cancel the agreement before the expiration date for a fee, or amend it with the consent of both parties in writing. In preparing for renegotiation, consider the following:



## COVID 19 RESOURCES FOR NONPROFITS

- What are the interests on both sides? You would like to keep your printer and maintain a good relationship with the leasing company, but not pay (or delay payments of) the full amount of the leasing contract if possible. It's likely that the leasing company is suffering as a result of COVID-19-related downturn and wants to maintain its customer base but also needs to maintain cash flow.
- Consider all your options, including:
  - You can cancel the agreement and pay the fee (or attempt to renegotiate for a lower fee). This is likely costly.
  - If your organization has the necessary cash, you can try to negotiate a buy-out of the machine. This may also be costly, and you likely don't want to use limited cash to buy out and actually own the copier.
  - You may ask the leasing company to renegotiate the terms of the agreement and request a reduced rate during the time that your office is closed or a temporary pause in payments in exchange for an extension of the term of the lease. However, the leasing company may be very resistant to changes.
- You can seek another leasing company to buyout the copier lease and negotiate upfront for different payment terms. This would depend on finding another leasing company with good rates that would provide good service.
- Plan for your negotiation, keeping in mind your ideal solution and the concessions you are willing to make along the way. Understand, with the help of your lawyer, your and your counterparty's rights and obligations under the contract, and see if there is a way for both parties to meet their needs. Go into the negotiation with the goal of maintaining a good relationship and attempting to avoid conflict, as this will increase the chances that there will be a mutually agreeable resolution and future conflicts will be minimized.

### HOW DO I ENFORCE A CONTRACT?

If negotiations are unsuccessful, a party may seek to enforce a contract through litigation or arbitration (which is the remedy sometimes required in certain contracts), or through another dispute resolution mechanism, such as mediation. This can happen if you are the party that has stopped complying with the contract or if the other party is the one that has stopped complying with the contract.

There are costs and benefits associated with each of these options, and it is advisable to consult an attorney to determine the appropriate course of action. For many organizations, the hurdles of litigation, arbitration or mediation (substantial cost, time (often years) and the

difficulties of collecting any judgment) will outweigh the benefits. These considerations are especially relevant given the widespread financial impact of the COVID-19 crisis, which has rendered many entities cash-strapped or even insolvent and unable to bear the cost of litigation or pay on a damages judgment.

Thus, before resorting to litigation, it is important to think creatively about mutually beneficial ways to resolve the dispute through negotiation – for example, by modifying contractual terms or deferring obligations under the contract.

### WHAT SHOULD I THINK ABOUT FOR NEW CONTRACTS DURING COVID-19?

If your organization is considering entering into a new contract during the COVID-19 crisis, it is important to consider whether any of the provisions discussed in this guidance are necessary or helpful to protect the

organization's interests if there is a change in circumstances due to COVID-19. For example, if your organization is planning to host a fundraiser next year and negotiates a contract with an event space, you will want to think about



## COVID 19 RESOURCES FOR NONPROFITS

what kinds of provisions are needed to protect yourself if the event is cancelled or postponed due to ongoing social distancing measures. In this case, the parties may want to set detailed terms and conditions around cancelling or postponing the event within a specified period of time prior

to the event, or negotiate a more flexible cancellation policy. Flexibility may be necessary in order to maintain a positive relationship with the counterparty throughout the life of the contract, which could be particularly critical if conflicts arise.

# LEGAL RESOURCES

New York Lawyers for the Public Interest is available to assist you with the various stages of contract formation, negotiation and dispute resolution.



## COVID 19 RESOURCES FOR NONPROFITS

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