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Market Change Risks

MARKET CHANGE HAZARDS

A market is a location where "goods or services are bought and sold."[1] It is also a "geographic area or demographic segment considered as a place of demand for particular goods or services" and "the demand there is for any particular article."[2] In this latter sense, a market is an activity of individuals, demanding goods, services, and other items of value and supplying such items to satisfy that demand.

A change in supply or demand is a change in the market for the good, service, or other item of value so demanded and supplied. Such a change may be comparable to the uncontrollable events described in chapter 11 when no party to the transaction controls its occurrence, and it may or may not be foreseeable. Market changes are the cumulative effects or aggregation of the results of individuals' buying and selling goods, services, and other items of value; usually no specific individual controls such effects or aggregation. The exception is a "thin" market, which is defined as a market "in which the number of offerings is relatively low." Such a market may be controlled or influenced by a few individuals in a way uncontrollable events are not. Still, the market changes even in a thin market may be beyond the control of both parties to a transaction. The reference to "market forces" enhances the comparison to other uncontrollable events: like earthquakes, lightning, and the like, changes in supply and demand seemingly deny a party affected thereby the ability to perform or realize a benefit or compel or pressure it to make a choice between two adverse outcomes. The analogy is far from perfect, however, as explained as follows.

Adverse Outcomes of Market Changes

Each market change whose occurrence or nonoccurrence is beyond the parties' control and affects their transaction can be described using the three variables used for other uncontrollable events:

- whether such change was (1) the occurrence of an event that was not expected to or was hoped would not occur or (2) the failure to occur of an event that was expected to occur or was hoped would occur;
- whether the change affected (a) benefit realization or (b) task completion; and
- whether benefit realization or task completion was as a result of such change partly or wholly (i) reduced, (ii) delayed, or (iii) made more expensive.

The market changes discussed in this chapter are assumed to be beyond the control of the parties. The previous variables can be combined to describe each market change. For example, an increase in a contractor's labor and material costs purchased in the open market would be a (1)(b)(iii) scenario: a market change that increases costs at the time of performance. If additional delay is also the result, because labor and materials take longer than anticipated to procure, the scenario would be (1)(b)(ii), as well.

The impact of uncontrollable events on task completion may also be repeated for market changes. The impact on task completion may be that (A) task completion is impossible, impractical, or difficult or (B) a choice is created between completing the task and suffering adverse consequences, on one hand, and breaching and avoiding the adverse consequences, on the other. When task completion is impaired, partly or wholly, or delayed by a market change, it can be further described by whether, if task completion is affected, the task is intended to be completed for (I) the benefit of the party completing it or (II) the other party. These previous variables can be combined with the first three groups to describe each uncontrollable incident. If the contractor was unable to procure an item needed for construction, it would be unable to perform its obligation to the owner. Such scenario is (1)(b)(i)(A)(II).

Contingencies and Nonoccurrences

A nonoccurrence of a market change is comparable to the nonoccurrence of an uncontrollable event and can adversely affect a transaction. In both instances, a transaction is structured such that benefit realization or task completion can be achieved only if an anticipated event or market change occurs. The passage of time without its occurrence results in such benefit not being realized or task not being completed. The hazard is proceeding with a transaction assuming or hoping such event or change will occur.

Columbian National Title Insurance Co.,[3] summarized in chapter 10,[4] may illustrate such a structure. Either the demand for title insurance in the county title insurance market had changed after contract formation, precluding the entry of new insurers in that market, or the demand for the new insurer's insurance policies did not develop after contract formation, as hoped. Viewed as the latter, which seems a more accurate description of events, the agent's realization of the benefits of the contract depended upon the occurrence of a market change. Accordingly, the agent's claim implied that he had not assumed responsibility for the risk of such nonoccurrence. Rather, both parties had jointly assumed responsibility for the risk of such nonoccurrence, and he could terminate the contract. Each party would have had to bear its losses. The title insurer's successful claim that the agent could not terminate the contract implied that the agent had assumed responsibility for the risk the market would not develop as anticipated.[5] So viewed, the case illustrates a (2) (a)(i) scenario (nonoccurrence of event precludes benefit realization).

Benefit Impairment

Several market changes are frequent hazards to benefit realization: first, a decrease in the demand or offtake for or the price of the goods, services, or other items of value, the sale of which is expected to yield an anticipated benefit; second, an increase in supply of such items, depressing their price in the market; and third, inflation that diminishes the relative value of the prices realized from such sales.

Demand and Offtake. Chapter 10 describes the risk to a party in a supply chain transaction that can occur when an offtaker does not perform as expected. The offtaker's repudiation or breach in a second transaction diminishes or destroys the value of the benefit the party hoped to realize in a first transaction, wherein it would receive a good, service, or other item of value to be used to perform in the second. Chapter 10 assumes an offtaker has or could have been identified. This chapter assumes no offtaker has been identified and explains the risk to a party (P2) where no offtaker can be identified because demand for an item, if it previously existed, has collapsed. This is an extreme case, when demand for goods, services, or other items have vanished. In other instances, discussed later in this chapter, demand may be weak, reducing the price of such items. When demand has collapsed, the result is the same for P2 as breach or repudiation by the offtaker: the value of the benefit of the first transaction correspondingly decreases with the loss of value in the second transaction. But the hazard described in this chapter is a change in the market, a drop in demand, not a failure of the offtaker to perform.

The following illustrate such a hazard:

- *OWBR LLC v. Clear Channel Communications, Inc.*[6]: In November 2000, conference organizers booked 2,270 hotel rooms for conference scheduled for February 2002. They also agreed to pay, as liquidated damages, the full rates for such rooms if the conference was canceled 30 or fewer days before the event. The organizers canceled the event within a 30-day period, citing the "events of September 11th coupled with the fragile condition of the U.S. and international consumer economies," which had "resulted in the withdrawal of commitments to this event from many of our sponsors and participants."[7] Whatever demand for the conference that existed at contract formation had dried up by January 2002 due to the combined effects of the 9/11 events and the subsequent downturn in the economy, which were the hazards to the transaction. (The hotel, the conference organizers, and attendees were P1, P2, and P3 respectively; the value of the P1-P2 contract was destroyed by the drop in demand by potential P3s.) If responsibility for the risk of such a drop was not assumed by the conference organizers, as they implied in their claim, it was borne by both parties, and the organizers could terminate. Each party would be left to bear its losses. The hotel's successful claim that the organizers could not terminate implied that responsibility for the risk had been assumed by them. This case also illustrates a (1)(a)(i) scenario, where the market change is a drop in demand.
- *Karl Wendt Farm Equipment Co., Inc. v. International Harvester Co.*[8]: Because of a sharp downturn in the demand for farm equipment, a manufacturer sold its farm equipment division through an asset sale, assigning most of its contracts with its distributors to the buyer. It did not assign the contract with Karl Wendt (KW) because the buyer already had a distributor in the area in which KW sold farm equipment. The drop in demand did not prevent the manufacturer from selling equipment to KW; it made continued operation unprofitable. The drop in demand, together with the buyer's existing contract with another distributor, reduced the value or benefits of the KW contract to the manufacturer because he could not assign it to the buyer. If responsibility for the risk of such a drop in demand was not assumed by the manufacturer, as the manufacturer's claim implied, it was borne by both parties and the manufacturer could terminate. Each party would be left to bear its losses. KW's successful claim implied that responsibility for such risk had been assumed by the manufacturer, who could not terminate and who breached the contract by selling the division without assigning the contract.[9] (The manufacturer, distributor, and customers were P1, P2, and P3, respectively. Because P2's commitment to buy from P1 did not have to exceed the demand from P3, P1 bore responsibility for the risk of demand for farm machinery declining. The decline in demand by P3 decreased the value of the P1-P2 contract to P1.) This case illustrates a (1)(a)(i) scenario, where the market change is a drop in demand.

Quantity and Price Changes. Demand for a good, service, or other item may decrease without entirely disappearing, or the supply may increase dramatically. If a party can pass through to its supplier to whom it has committed to buy items the reduced demand by taking less or fewer of the supplied items, responsibility for the risk of a drop in demand is also passed through to, and assumed by, the supplier. Another result of a decrease in demand may be a drop in the price in the market for the goods, services, or other items a party expects to sell. A similar result may occur because the supply is increased more quickly than a corresponding increase in demand. If a party can pass through to its supplier the reduced price by paying less for the supplied item, responsibility for the risk of a drop in demand is also passed through to, and assumed by, the supplier. If such party cannot pass through to its supplier the reduced demand or price for items because it has agreed to take a fixed or minimum quantity or pay a fixed price, then it bears responsibility for the risk of such drop in demand or price, unless it is otherwise excused. In either case, the value of the supply contract to the supplied party is diminished by the reduction of demand or price, resulting in a lower quantity or prices being desirable.

The following illustrate such hazards:

- *Great Lakes Gas Transmission Ltd. Partnership v. Essar Steel Minnesota, LLC*[10]: In September 2006, a pipeline company agreed to transport a quantity of gas each day from a receiving point to a delivery point for a steel producer. The contract term was to begin July 1, 2009. In 2008, a global financial crisis began, and steel prices dropped to a six-year low. The steel producer claimed its duty to pay the tariff was excused because the demand for steel had dropped, steel prices were low, and financing for the construction of the steel plant was unavailable due to the shortage of credit in the financial market. The drop in demand for steel did not make the steel producer's performance impossible: it could still pay the agreed tariff even if it did not transport any gas; the value or benefit of the contract had been diminished by the drop in demand for steel. The risk allocation implied in the steel producer's claim was that responsibility for the risk of decreased demand and steel prices was shared with the pipeline. It was entitled to reduce or delay (or both) its demand for the transportation services to reflect its own delay and reduction in production.[11] (The pipeline, the steel producer and its customers were P1, P2, and P3, respectively. The value of the P1-P2 contract was reduced by the reduction in demand and prices prospective P3s were willing to pay.) This case is also a (1)(a)(i) scenario, where the market change is a drop in demand and price that affects the value of the anticipated benefit.

- *Kyrocera Corp. v. Hemlock Semiconductor, Inc.*:[12] Between 2005 and 2008, a manufacturer of solar panels agreed in four contracts to buy a certain quantity of polysilicon annually at a fixed price over a period of ten years. Beginning in 2010, Chinese companies flooded the international market with solar panels at reduced prices. Chinese companies gained 75 percent of the global solar panel market, causing more than 20 US and European manufacturers to go out of business and solar panel prices to decline precipitously. The continued purchase by the manufacturer of components used in its manufacture of solar panels became uneconomic. The supplier agreed to lower prices for 2011 and 2012, but not beyond. The manufacturer sued for a declaration that it was no longer bound to buy polysilicon pursuant to the contracts because of the lower market prices for solar panels attributable to the actions of Chinese suppliers and government. The lower prices did not prevent the manufacturer from performing its contract with its supplier: it could still take delivery of polysilicon in the agreed quantities and pay the agreed price or pay the agreed minimum without taking delivery of any amount. The depressed prices diminished the value of the supply contract to the manufacturer. (The supplier, the manufacturer, and its customers were P1, P2, and P3, respectively. The value of the P1-P2 contract was diminished by the drop in solar panel prices.) The P1-P2 contract effected a risk allocation usually effected by a fixed price take-or-pay contract for an item like polysilicon: first, the manufacturer or buyer assumes responsibility for the risk the contract price of the item will be higher than the market price as and when the item is required, and second, the manufacturer assumes responsibility for the risk that its need for polysilicon will be less than the minimum quantity it agreed to buy.[13] The case is another illustration of scenario (1) (a)(i): a drop in demand for a party's products reduced the value to that party of the contract with its supplier for the components used in making the products.

Inflation. Inflation, defined as "[a] general increase in prices coinciding with a fall in the real value of money,"[14] erodes the value of benefits when amounts received are fixed over a period of time. Inflation could create risks in a supply chain transaction comparable to the effect of price decreases due to drops in demand or increases in supply. For example, if a party buys goods, services, or other items and pays market price, over time that price could increase consistent with inflation and those increases could not be passed through to offtakers because the party had agreed to sell its products at a fixed price; the value of the offtake contract would diminish over time, as inflation erodes its benefits. This is also true when the transaction is not one in a supply chain. For any party who anticipates realizing value over a period of time, inflation will reduce that value unless it is increased consistently with inflation or the contract can be terminated.

The following illustrate inflation hazards:

- *Shell Oil Co. v. Kapler*[15]: In 1939, a landlord leased property for five years. The lease was later renewed for another five years. The lease granted the tenant an option to purchase the leased property for a fixed price of $25,000 and a right of first refusal. Before the expiration of the second five-year term, the tenant exercised the option. The landlord responded, stating it had another offer for $35,000 and insisted that the tenant meet this price or relinquish its right to buy. The tenant sued for specific performance. The owner contended that relief should be denied because of "the increase in the value of the property and the depreciation in value of money since the lease agreement was entered into by the parties."[16] The landlord remained capable of performing, selling the property. Neither the increase in the value of the property nor the decline of the purchasing power of the fixed price prevented the landlord from selling. The benefit of the fixed price had eroded. The landlord's claim that the tenant should match the higher price or lose the option implied that responsibility for the risk of inflation rested with the tenant. If both parties shared responsibility for the risk of inflation eroding the value of the fixed price, the option would have no longer been effective. The tenant's successful claim that the option was enforceable notwithstanding the reduced value of the fixed price implied that the landlord had assumed responsibility for that risk.[17] This case also illustrates a (1)(a)(i) scenario, but the market change was the erosion of the value realized due to inflation.
- *Cumberland Trust v. Maritime Electric Co. Ltd*.[18]: In 1853, a landlord leased to a gas light company four parcels of land in Charlottetown, Queens County, Prince Edward Island, for 999 years at a fixed annual rent of £18 local currency (which amounted to C$58.40 in Canada's 2000 currency). In 1999, the landlord applied to the court to increase the rent and limit the term to 20 years, claiming that inflation has eroded the value of the rent to the owner, which was used for charitable purposes. Had the tenant alone bore responsibility for inflation, as the landlord's position implied, the landlord would have been entitled to increase the rent to its value adjusted for inflation. If both shared responsibility for the risk of inflation, the landlord could have terminated the lease when the value of the rent had been substantially reduced, as it was. The landlord could not increase the rent or terminate the lease, however, if it alone assumed responsibility for inflation, as the tenant's successful claim implied.[19]

Task Completion

The unwillingness of even a single supplier to supply a good, service, or other item of value that is needed to complete the task and was previously available is a market change that can prevent or impair task completion. We ignore an increase in prices due to short supply because price increases are discussed later in this chapter. Supply of a necessary item may become temporarily or permanently unavailable because its suppliers discontinue supplying it altogether. Procurement of an item may become more difficult. The difficulty or unavailability cannot be attributable to the party's inability to procure the item. Procurement has to be infeasible, i.e., no one can procure the item in the market. The disruption in the supply of an item cannot be due to an uncontrollable event, such as a storm destroying a crop in a region, because the unavailability or increased price of the item would be the result of such event and not market changes. Such a market change—change in supply availability—is a hazard only in a supply chain transaction: task completion in one transaction depends upon identifying, contracting with, and the performance by a supplier in a separate, concurrent, or earlier transaction.

The following illustrate such hazards:

- *Gander Mountain Co. v. Islip U-Slip LLC*[20]: A tenant rented premises for 15 years, aware of the history of flooding in an area. It agreed to obtain an all-risk policy of insurance covering its merchandise, trade fixtures, furnishings, equipment, and all other items of its personal property and all buildings and improvements on the premises. Two years later, the premises were severely flooded by the nearby stream, and again by a tropical storm six years later. The tenant was unable to obtain all-risk insurance because of these incidents and the history of flooding before it rented the premises and sued for a declaration that the lease was terminated as a result, claiming impossibility or frustration of purpose. (The insurer, tenant, and landlord were P1, P2, and P3, respectively. Obtaining the insurance under the P1-P2 contract would satisfy P2's obligation to P3 under the lease.) The tenant's position was comparable to a loan applicant who could not qualify for a loan. The required insurance was available in the market but not to the rented premises because they did not qualify, given the history of flooding. Put another way, satisfying the insurance company's requirements was feasible in appropriate circumstances, but the rented premises did not qualify. The tenant's claim implied both landlord and tenant shared responsibility for the risk the tenant would lose its ability to obtain the insurance. Each could terminate without liability for breach when the tenant could not obtain insurance. The landlord successfully claimed the tenant assumed responsibility for the risk it would be unable to obtain the required insurance.[21]
- *Kel Kim Corp. v. Central Markets, Inc.*[22]: A tenant leased premises to operate a roller skating rink open to the public and agreed to maintain public liability insurance with aggregate liability of $1,000,000 for the ten-year term of the lease. After five years it was unable to obtain renewal or replacement of such insurance because the reinsurer of its insurer had become insolvent. The best replacement insurance the tenant could obtain limited coverage to $500,000. The tenant claimed its failure to obtain the policy was excused by impossibility and the force majeure clause. Whether procuring the required insurance was infeasible because the insurance market had changed—reinsurers were no longer willing to reinsure liability insurance for roller skating rinks—is unclear. If not, this was another case of inability. Assuming the case was one where the market had changed, the tenant's claim implied that the landlord bore the risk of an adverse change in the insurance market that prevented the tenant from complying with the insurance requirement; the tenant could continue to rent the premises while not having to comply with that requirement. The landlord's successful claim implied the tenant had assumed responsibility for the risk it would be unable to obtain the required insurance.[23]
- *Hoosier Energy Rural Elec. Coop., Inc. v. John Hancock Life Ins. Co.*[24]: A power plant lease obligated the lessee to maintain a credit default swap with a qualified counterparty for the benefit of the lessor and to replace such swap within 60 days if the swap provider ceased to be qualified. The lessor could demand payment under the swaps if they were not replaced within that period. During the 2008 financial crisis, the swap provider's credit rating dropped below the required level. The lessee sought a replacement swap provider but could not find a qualified counterparty because of the crisis. The lessee sued for an injunction to prevent the lessor from demanding payment under the swaps when the swap provider was not replaced within the 60-day period, claiming temporary impossibility. The change in the market was that some of the potential previously qualified counterparties ceased to be so; the supply in the market had shrunk to a point where such counterparties were not readily available. It was the clearest case where compliance with the requirement had become infeasible because of a shortage of suppliers.[25] The lessee's claim implied the lessor bore responsibility for the risk qualified counterparties would not be available, at least temporarily; the lessee could continue to lease the power plant without having to comply with the credit default swap requirement so long as qualified counterparties were in short supply. The landlord's unsuccessful claim implied the tenant had assumed responsibility for the risk it would be unable to obtain the credit default swap.[26] This and the previous case illustrate (1)(b)(i)(A)(II) scenarios: a change in the insurance and credit default swap markets prevented an obligor from completing a task for the benefit of the other party.[27]
- *CERAbio LLC v. Wright Medical Technology, Inc.*[28]: This case is summarized in chapter 4.[29] CERAbio (C) sold its business, which made a bone replacement product, to a buyer for two payments of $1.5 million each and royalties, the first at closing and the second when the buyer verified the product could be made following the protocol agreed by the parties. After closing, the parties learned the sole supplier of a key ingredient used to make the product no longer supplied it. C believed that with a change to the protocol the product could be produced using a new ingredient. The buyer was unwilling to make the change and claimed fraud.[30] The market in the key ingredient was indeed very thin. The loss of the supplier of that ingredient was a change in that market. C's claim implied that responsibility for the supply risk was shared by the buyer, which had to use a substitute for the key ingredient if one was available. The buyer's unsuccessful claim implied that C assumed responsibility for the risk. (Any supplier of the ingredient, C, and the buyer would have been P1, P2, and P3, respectively. The absence of a supplier precluded a P1-P2 contract and P2's ability to supply P3 with the ingredient required to run the test protocol.) This case illustrates a (1)(b)(i)(A)(I) scenario: C was not obligated to have the buyer run the test protocol. Doing so was a condition to its receiving the second payment, a benefit of the sale. A change in the supply of the key ingredient would have prevented it from completing a task for its benefit as much as for that of the other party but for the availability of the substitute.

Increased Costs

An increase in the price of goods, services, and items of value procured in the open market for use by a party can be a hazard to benefit realization and task completion. If the additional costs are paid directly by the ultimate offtaker who consumes such items when realizing the benefits of a transaction, it cannot recoup such costs by raising its own prices. The hazard to the offtaker is that the market price of such inputs will increase beyond its expectations. Such instances are scenario (1)(a)(iii). If the additional costs are paid by a supplier who uses such items to perform obligations, it may be able to recoup the additional costs by charging higher prices for the items it supplies. Price increases are a hazard to such a supplier to the extent it cannot match its increased costs with increased prices to its offtaker. Such instances are scenario (1)(b)(iii) (B)(II).

The following are cases that illustrate such mismatch hazards:

- *Maple Farms, Inc. v. City School District of Elmira*[31]: A milk supplier agreed to supply milk to a school district for $.0759 per half pint, at which time the mandated price of raw milk was $8.03 per hundredweight (cwt). Subsequently, the price of raw milk increased 23 percent to $9.89 cwt. In the prior three years, the price of raw milk ranged from $6.73 cwt to a high of $7.58 cwt, or 12 percent. The supplier sued for a declaration that its performance had been rendered commercially impracticable by the price increase, citing as the unforeseen causes the "agreement of the United States to sell huge amounts of grain to Russia and to a lesser extent to unanticipated crop failures."[32] The price mismatch was between the market price at which the supplier bought and the fixed price at which the supplier sold milk. The supplier's claim implied that both parties shared responsibility for the risk that the market price of milk would increase beyond the level the supplier anticipated, and as a result the supplier would be able to terminate its contract with the school district. The school district's successful claim implied that responsibility for the risk had been assumed by the supplier.[33]

- *Staffordshire Area Health Authority v. South Staffordshire Waterworks Co*.[34]: In 1929, a water company agreed to supply a hospital authority with the first 5,000 gallons per day of water for free and additional water at a fixed price per 1,000 gallons "at all times hereafter." The water company's costs rose eighteen times over the next forty-five years. In 1975, the water company terminated the contract and offered to supply the first 5,000 gallons of water per day free and additional amounts at its normal rates. The mismatch was between the market prices the water company paid for labor and materials and the fixed price it charged the hospital authority. The water company's successful claim implied that both parties shared responsibility for the risk the water company's prices might increase over time, allowing the water company to terminate when they dwarfed the payments from the authority. The authority's unsuccessful claim implied the water company assumed responsibility for the risk of such price increases.[35]
- *Bernina Distributors Inc. v. Bernina Sewing Machine Co., Inc*.[36]: A sewing machine importer agreed to pay its Swiss supplier prices denominated in Swiss francs but agreed to sell the machines to its US distributor at prices denominated in US dollars. Those prices were subject to change to the extent the invoice price to the importer or duty charges were increased or decreased and to the extent the importer's insurance, freight, handling, broker, and port fees, and similar charges, were increased 20 percent or more over such charges at contract formation. When the value of the US dollar decreased relative to the Swiss franc, the importer treated its increased cost in US dollars (to buy the additional francs) as an increase in the invoice price. When challenged by the distributor, it also claimed it could terminate the contract, as the drop in the value of the dollar frustrated the contract. The mismatch was buying at prices in Swiss francs and selling at prices in dollars. The importer's first claim, that it could pass through to the distributor its higher costs resulting from unfavorable swings in the exchange rate, implied the distributor bore the risk of the dollar's decline in value relative to the Swiss franc (but not the benefit of declines in the value of the Swiss franc).[37] The second claim implied the parties shared responsibility for that risk, allowing the importer to terminate. The distributor's successful claim that the importer could not charge for the higher cost of Swiss francs or terminate implied responsibility for the risk had been assumed by the importer.
- *Eastern Air Lines, Inc. v. Gulf Oil Corp*.[38]: In June 1972, Gulf agreed to sell jet fuel to Eastern for four and one-half years at prices calculated using the posted prices for West Texas sour crude oil, as published in *Platt's Oilgram Crude Oil Supplement*. In 1973, the price of crude oil produced outside the United States increased, such that the unregulated price of foreign crude exceeded that for domestic crude. The government adopted a tiered pricing regulation for crude oil produced in the United States. One result was that the posted price continued to reflect the regulated, and not the higher foreign or unregulated, domestic market prices of crude oil. Gulf demanded a price increase, threatening to cut off supplies to Eastern, which sought an injunction to compel performance. Gulf claimed it was not bound by the contract because the posted price was lower than the foreign and unregulated domestic prices; its performance had become commercially impracticable. The mismatch was between the prices of unregulated foreign and domestic crude, on one hand, and regulated domestic crude, on the other. One view of Gulf's claim was that its costs of the crude oil used to produce jet fuel soared with the increase in the price of foreign crude, rendering the contract with Eastern less profitable or unprofitable. Implicit in Gulf's claim was that responsibility for the risk of such price mismatch was shared, allowing Gulf to terminate. Another view of Gulf's claim was that sale of jet fuel to Eastern at the posted price for West Texas sour crude was less profitable than sales at a price that reflected the market price of crude. In effect, Gulf was comparing the benefit it agreed to accept at contract formation with a more valuable benefit created by the increase in the price of foreign crude. That implied a different risk allocation: the risk that a change in the market price of crude would make the agreed price less profitable than another price, a risk responsibility for which Gulf's claim implied was shared by the parties. Responsibility for the risk remained with Gulf, as Eastern successfully claimed.[39]

Impairment and Choice

As explained in chapter 11, an uncontrollable event can create a predicament for an obligor where it must choose between performing a contractual obligation and thus suffering an adverse consequence and avoiding such consequence by not performing and thus incurring potential liability for breach of contract. Performance is not prevented or necessarily more difficult as a result of such an event. A supply shortage does not create such a predicament because it eliminates the choice of compliance and with it the ability to perform. An increase in the prices of inputs does create such a choice: between continuing with performance and incurring the higher costs, on one hand, and avoiding the higher costs and breaching, on the other. A drop in demand by offtakers or the value of benefits also creates a choice: between performing and realizing less or no value, thus avoiding such realization, and breaching the contract. In *Karl Wendt Farm Equipment Co., Inc*.,[40] for example, the manufacturer had to choose between honoring its contract with the dealer and incurring financial losses and avoiding those losses and breaching that contract. This is true of all cases in which benefits are impaired, whether as a result of an act of God or a third party or a drop in demand or value. The pressure created by a change in the price of an input or the demand or value is financial or economic: the obligor must give or invest more value to perform than it than anticipated or realize less value or incur more losses than anticipated from performance.

Oversight, Etc.

Like uncontrollable events, the potential for market changes may be overlooked, recognized but rejected as unimportant to transaction planning, misunderstood because of bad information or incorrect processing of good information, and be highly uncertain as to both their nature and probability of occurrence. Oversight of market changes is evident in cases where it is claimed such changes were unforeseeable, notwithstanding that they frequently occur, though perhaps due to different and unusual events. Unforseeability admits ignorance of the potential event at contract formation. In *Northern Illinois Gas Co. v. Energy Coop., Inc*.,[41] a naptha buyer claimed naptha price increases and natural gas price decreases (it used the naptha to produce the gas) could not have been foreseen, and these circumstances made its purchase of naptha so financially burdensome that the contract should be terminated. Holding the supplier was entitled to summary judgment on this claim, Justice James Heiple unsympathetically commented, "Changing and shifting markets and prices from multitudinous causes is endemic to the economy in which we live. Market forecasts by supposed experts are sometimes right, often wrong, and usually mixed."[42] The buyer had either overlooked or recognized and rejected as significant such potential price fluctuations. In *Bernina Distributors Inc.*,[43] the importer claimed it should not be bound by the mismatch between the prices to be paid and received because it was "unaware of the risk of an exchange rate fluctuation" and "ignorant of the term of the contract (as construed by the trial court)."[44] Because the importer was aware of currency fluctuations, it had not overlooked their potential; rather, it did not appreciate or appreciated and rejected their importance to the transaction. The importer seemingly incorrectly processed correct information about exchange rate fluctuations to reach the wrong conclusion about the significance of their risks.

MARKET CHANGE RISK MANAGEMENT

Diligence

Diligence on market changes has the same objectives as that on uncontrollable events: to identify, assess, and determine the potential changes that should be considered as hazards for purposes of the transaction; which, if any, such changes have already occurred at contract formation; and which, if any such changes might occur after contract formation. Because courts are nearly always hostile to claims that failures to perform should be excused because market changes made performance or benefit realization more onerous, expensive, or impossible, identifying and allocating responsibility for the risk of such a change is all the more important to a transaction participant who would expect to be excused or compensated. Just as it is outside the scope of this text to explain what diligence on such events should be undertaken in any specific or specific type of transaction, it is beyond the scope of this book to explain the diligence that should be undertaken on market changes in any transaction or type of transaction.

Firm Commitments

Like risks of an uncontrollable event, responsibility for the risk of an adverse market change is allocated, first, by a commitment to perform or complete a task, notwithstanding such a change; second, when applicable, one or more of the legal doctrines of unilateral and mutual mistake, supervening impossibility and impracticability, and frustration of purpose; and third, by an express term included in a contract that is intended to allocate responsibility for such risk. A commitment to complete a task includes an assumption of responsibility for the risk that a market change may adversely affect completion. The commitment is overridden by the legal principles of unilateral and mutual mistake, supervening impossibility and impracticability, and frustration of purpose; when applicable, performance is discharged. The commitment and such legal principles may be further overridden by an express contractual term that stipulates when a market change excuses performance.

In principle, arrangements and terms similar to those used to manage uncontrollable events risks can be used to manage market change risks; the principal devices that allocate market change risks are conditions precedent and subsequent, obligor and third-party covenants, representations and warranties, and force majeure clauses.

Fixed or Minimum Offtake and Supply. Responsibility for the risk that the market demand for or the offtake of an item might be less at the time of sale than the level anticipated at contract formation can be allocated to one or more offtakers by having it or them commit in advance of their procurement to buy such items instead of a seller disposing of them on the open market as and when it decides to sell them. By covenanting to buy an item at some time after contract formation, the buyer who expects to resell it assumes responsibility for the risk that the demand in the market for it may at the time of purchase be less than was anticipated at contract formation. A take-or-pay contract is an example of such an offtake contract: an offtaker agrees to pay for a fixed or minimum amount when it elects to accept delivery of less than an agreed or minimum quantity of such items. The take-or-pay or other contract to buy a fixed or minimum quantity allocates only responsibility for offtake risk; it does not allocate or mitigate responsibility for the risk prices that might fluctuate.

Resources Investment Co. v. Enron Corp.[45] illustrates such an arrangement: sellers and buyers entered into 32 contracts over 18 years for the sale and purchase of natural gas. Each contract included typical take-or-pay obligations, by providing that if in any year the buyers did not accept delivery of the amount specified to be purchased during that year, the deficiency in purchases would nonetheless be paid for. Provision was made for gas paid for but not used to be carried forward to subsequent years. In response to a sharp downturn in demand for natural gas, the buyers stopped taking delivery of the minimum quantities and failed to make the payments for those quantities under the contracts, claiming the take-or-pay obligations violated public policy (burdening consumers contrary to certain statutes), were unconscionable (imposing oppressive terms), constituted penalties, were based on a mistake of fact (unexpected changes in demand), and were discharged by the impossibility and frustration principles and the force majeure clause (due to changes in demand for natural gas). The buyers' claims implied that the take-or-pay clause was ineffective to allocate responsibility for the risk of a drop in demand for natural gas; responsibility for that risk was shared by buyers and sellers, and the former could terminate when demand dropped. The sellers' successful claim that termination was not permitted implied the buyers had assumed responsibility for the risk of changes in demand for natural gas.[46]

The mirror image of the offtake risk allocation effected by a take-or-pay contract is the supply risk allocation effected by a deliver-or-pay contract. The risk that the available supply in the market of an item might be less at the time of purchase than the level of supply anticipated at contract formation can be allocated to one or more suppliers by having them commit in advance of their delivery to sell and deliver such items instead of buying them on the open market. By covenanting to sell an item at some time after contract formation, the seller who expects to buy it beforehand assumes responsibility for the risk that the available supply in the market for it may at the time of sale be less than was anticipated at contract formation. A deliver-or-pay contract is an example of such a supply contract: a seller agrees to pay a fixed or minimum amount when it fails to deliver an agreed or minimum quantity of such items over an agreed period of time. As with the take-or-pay contract, the deliver-or-pay or other contract to sell a fixed or minimum quantity allocates only supply risk; it does not allocate or mitigate the risk that prices to be paid might fluctuate.

A contract can combine take-or-pay and deliver-or-pay arrangements, and a contract that commits a seller to sell and a buyer to buy a fixed quantity is a foundation for such arrangements. The buyer commits to buy a minimum quantity of an item over a period of time or pay a fixed amount, thereby assuming responsibility for the risk that demand for such item will be less than at the time of sale. The seller commits to sell a minimum quantity of such item over the same period of time or pay a fixed amount, thereby assuming responsibility for the risk the available supply will be less at the time of sale. Either risk allocation can be unilateral, rather than reciprocal, by using an option: a contract can grant a seller a right without an obligation, or an option, to sell a minimum quantity of items to a buyer, in which event the buyer assumes responsibility for the offtake risk as described in the take-or-pay arrangement, but until the option is exercised, the seller does not assume responsibility for the supply risk as described in the deliver-or-pay arrangement. A contract can grant a buyer a right without an obligation, or an option, to buy a minimum quantity of items from a seller, in which event the seller assumes responsibility for the supply risk as described in the deliver-or-pay arrangement; but until the option is exercised, the buyer does not assume responsibility for the offtake risk as described in the take-or-pay arrangement.

Fixed Offtake and Supply Prices. Responsibility for the risk that the price that a seller can obtain from its offtaker in the market at the time it sells an item will be less than the price that at contract formation was expected for such sale is allocated by having an offtaker agree to buy at a fixed price. The offtaker by covenanting to buy at a fixed price assumes responsibility for the risk that the market value of the item it buys will be lower at the time of purchase than the market price. It assumes responsibility for the risk of such adverse changes in the market price of the item. Without such commitment from its offtaker, the seller bears responsibility for the risk the price it will receive for its product in the market will be lower than anticipated.

Health-Chem Corp. v. Baker[47] illustrates how a fixed price protects one party against and exposes another party to market changes in price. To settle a shareholder dispute, a principal shareholder of a publicly traded company resigned as director and agreed to sell his shares to the company over a period of time for $13.50 per share. The company wanted to avoid a single sale or even a series of sales of the stock over a short period, as these might have precipitated a drop in the share price. Shortly after contract formation, in October 1987, the stock market crashed. The company's share price dropped to $3.875. The company sued the shareholder to amend the contract, claiming mutual mistake of fact, commercial impracticability, and frustration of purpose. The chance share prices would drop after contract formation was a risk to one or both parties. To the shareholder the risk was that it would receive less over time if the price dropped and it was paid the market price for his shares; to the company the risk was that it would overpay if the price dropped and it paid a fixed price for the shares. If the shareholder bore responsibility for the risk that share prices would drop, as the company's claim implied, the shareholder would have remained obligated to sell its shares but at the lower market price; the fixed price would have been effectively overridden by the frustration doctrine. The shareholder's successful claim that the commitment to pay the fixed price was unaffected by the change in the share price in the market and not subject to the frustration doctrine implied that the company assumed responsibility for the risk of a price drop.[48] The case illustrates how a fixed price contract allocates responsibility for the risk in scenario (1)(a)(i) and the zero-sum game implicit in such risk allocation.

The mirror image of the offtake price risk allocation effected by a fixed price offtake contract is the supply price risk allocation effected by a fixed price supply contract. The risk that the price that a buyer must pay in the market at the time an item is bought for use or resale will be higher than the price at contract formation is allocated by having a supplier agree to sell at a fixed price. The supplier by covenanting to sell at a fixed price assumes responsibility for the risk that the market value of the item it sells will be higher at the time of sale than the market price. It assumes responsibility for the risk of adverse changes in the market price of the item. Without such commitment from its supplier, the buyer bears responsibility for the risk the price it will pay for an input in the market will be higher than anticipated.

The following illustrate supply arrangements that allocate supply price risk as previously described:

- *Louisiana Power & Light Co. v. Allegheny Ludlum Industries, Inc.*[49]: A supplier agreed to supply tubes for a fixed price, subject to increases of three percent if shipment was ordered between 30 and 36 months after contract formation and 10 percent if shipment was delayed beyond that time. Fifteen months after contract formation, the supplier asked for a price increase because its costs had increased: for example, electrolytic nickel, low carbon ferrochrome, and labor had increased 24 percent, 185 percent, and 21 percent, respectively. The buyer responded, demanding assurances the supplier would perform. The supplier claimed its performance was excused by mutual mistake and commercial impracticability. The increase in the prices of raw materials and labor was a risk to both parties. If the buyer bore responsibility for the risk of extraordinary price increases, as implied in the supplier's claim, the buyer would have had to buy the tubes at the higher prices; the mutual mistake doctrine, about the extent to which prices would rise, would have trumped the risk allocation in the fixed price and adjustment clauses. As the buyer successfully claimed, the supplier had to sell at the agreed prices, implying that responsibility for the risk of price increases beyond those contemplated in the contract had been assumed by the seller.[50] The case illustrates how a fixed price contract allocates responsibility for the risk in scenario (1)(b)(iii)(B)(II) and the zero-sum game in such price risk allocation.
- *Aluminum Corporation of America v. Essex Group, Inc.*[51]: Alcoa agreed to smelt alumina for Essex for twenty years, beginning in 1968. Essex agreed to pay Alcoa initially fifteen cents per pound, a fee that consisted of two components: a demand component of five cents per pound, which would increase in proportion to changes in the Engineering News Record Construction Cost-20 Cities Average Index published in the *Engineering News Record*, and a production component of ten cents per pound, which itself consisted of three components —a fixed component of four cents per pound, a nonlabor production cost component of three cents per pound, which was to be varied in proportion to periodic changes in the Wholesale Price Index-Industrial Commodities (WPI-IC) published by the Bureau of Labor Statistics of the United States Department of Labor, and a labor production cost component of three cents per pound, which was to be varied in proportion to periodic changes in Alcoa's average hourly labor cost at the Warrick, Indiana, works. The adjusted price was also subject to an overall "cap" price of 65 percent of the price of a specified type of aluminum sold on specified terms, as published in a trade journal, *American Metal Market*. Alcoa's purpose was to ensure that the price paid by Essex covered increases in its production costs, while preserving its net income covered in the fixed component of four cents per pound. Beginning in 1973, Alcoa's electricity costs rose much faster than allowed for in the WPI-IC because increased oil costs forced utilities to raise electricity rates. Alcoa estimated that instead of making an annual profit of $6,000,000, it would lose $60,000,000 over the remaining term of the contract. Each price component allocated to Alcoa responsibility for the risk that the price it would pay for labor, materials, and services included in such component in the market would exceed the amount by which it could increase its price to Essex. The overall cap further allocated responsibility for the risk to Alcoa that the aggregate of its cost increases might exceed that cap. Alcoa, Essex unsuccessfully argued, had superior knowledge of its costs in

operating the Warwick facility and knew the inherent risks in proposing the WPI-IC as the index for adjusting for nonlabor costs. It chose to protect itself against the fluctuations in nonlabor costs measured by the WPI-IC and to leave itself exposed to the risk of fluctuations that were not measured by that index. According to Essex, "[T]he parties made a calculated gamble with full awareness that the future was uncertain, so the contract should be enforced despite the mutual mistake."[52] Alcoa argued that the contract should be reformed, as it was based on a mutually mistaken assumption: the variation in nonlabor costs would not vary from the WPI-IC by more than five percent. This cap was nowhere stated in the contract. Implicit in this claim was that the limitations on price adjustments in the component formula and overall cap was subject to the mutual mistake doctrine, and as it bore that risk, Essex bore responsibility for the risk of the increase in nonlabor costs above five percent. The case illustrates how the limitations in a formula-based price may be functionally equivalent to a fixed price in allocating responsibility for supply price risk in scenario (1)(b)(iii)(B)(III) and also how such risk allocation can be trumped by the mutual mistake doctrine.[53]

Either price risk allocation can be unilateral, rather than reciprocal, by using an option: A contract can grant a seller an option or a "put" to sell items to a buyer at a fixed price, in which event the buyer assumes responsibility for the risk that the price it pays will be higher than the market price at the time of sale, but the seller does not assume responsibility for the risk that market prices at the time of sale will be higher than the contract price because it has no commitment to sell until it exercises the option to sell. A contract can grant a buyer an option to buy items from a seller at a fixed price, in which event the seller assumes responsibility for the risk the price at which it sells will be lower than the market price at the time of sale, but the buyer does not assume responsibility for the risk that market prices at the time of sale will be higher than the contract price because it has no commitment to buy until it exercises the option to buy.

Inflation Adjustment. The risk that inflation will reduce the value or relative purchasing power of a partly or wholly fixed price that a seller can obtain over the period it sells to the offtaker is allocated by adjusting that price to reflect inflation. The choice of an index to measure inflation is itself a risk: the index may understate or not be a measure of the true extent of the inflation that affects the seller, and the offtaker assumes responsibility for the risk that such adjustment overstates inflation. As with any fixed price, the offtaker by covenanting to buy at price adjusted for inflation also assumes the risk that the inflation adjusted price will exceed the market value of the item.

The following cases illustrate how clauses adjust for inflation and how they are themselves subject to risks:

- *Printing Industries of Northern Ohio, Inc. v. International Printing and Graphics Communications Union, Local No. 56* [54]: Collective bargaining contracts between employers and the unions provided for a two cent per hour cost of living adjustment to the employees' wages for each one-point increase in the Consumer Price Index for Urban Wage Earners and Clerical Workers, new series, for Cleveland, Ohio (Cleveland CPI-W). In 1982, the U.S. Bureau of Labor Standards expanded the geographic reach of its sample beyond the Greater Cleveland area because too few home sales were recorded in the Greater Cleveland area over the relevant period. The result was that the variance between National CPI-W and the Cleveland CPI-W increased from 3.7 points to 17.9 points in 1982 and 21.5 points in 1983. The adjustment clause protected the union members against inflation eroding their wages. What the clause did not expressly cover were changes to the data used to calculate the index stipulated to be used in that clause, which changes were distinct uncontrollable events, creating still another risk that a governmental agency would modify calculation of Cleveland CPI-W, thereby reducing or increasing the annual adjustment. The employers' organization sued to reform the contract, claiming mutual mistake of fact and frustration of purpose: that the Cleveland CPI-W no longer represented a cost of living adjustment but effected a wage increase the employers would not have accepted. The employers' claim implied that they had not assumed responsibility for the risk that changes in the calculation of index could increase wage increases above those that would have been made in the absence of such change. They were entitled to continue paying wage increases as if no change had been made. The union's successful claim implied that each party by agreeing to the clause assumed responsibility for the risk of adverse changes and were not subject to the mutual mistake doctrine. In this instance, the employers suffered the loss.[55]
- *Waegemann v. Montgomery Ward & Co.*[56]: A commercial lease for ten years, followed by two additional five-year terms at the tenant's option, provided that the rent would be increased annually by the percentage by which the real estate taxes on the property were increased. Because property values were annually appraised by assessors to calculate real property taxes, the adjustment clause reflected the increase in property values, which were likely higher than inflation. During the initial 10-year term, Proposition 13 passed by referendum in California, limiting increases in real estate valuations to two percent per year. Accordingly, rent increases under the lease were also limited. The landlord sued for a declaration that the lease was no longer binding, its purpose having been frustrated by the limitation on rent increases that was an unintended consequence of Proposition 13. The landlord's claim implied that the adjustment clause, while allocating inflation risk, did not allocate responsibility for the risk that a change in law would modify how property value increases would be measured for the purpose of calculating real estate taxes; responsibility for that risk was shared by the parties, and the landlord was entitled to terminate the lease. The tenant's response, accepted by the court, implied that the risk allocation effected by the clause had not been trumped by the frustration doctrine. In this instance the landlord suffered the losses.[57]

Conditions Precedent and Subsequent

Conditions precedent and subsequent can allocate market change risks. A condition precedent can state an obligor has no obligation to perform until a market change that must occur has occurred or a market change that must not occur has not occurred; the failure of such a condition allows the obligor to terminate the contract, in which event each party is responsible for its own losses unless otherwise specified in the contract. A condition subsequent can state that an obligor may suspend, terminate, or reopen the negotiation of the terms of its obligation to perform upon the occurrence of a market change that must not occur or upon the nonoccurrence of a market change that must occur by a date certain. Conditions precedent and subsequent can thus be used to allocate responsibility for all market change risks, usually, but not always, to both parties, because termination will ordinarily result in both parties losing their investment in the transaction without further liability to each other.

Pan Am Corp. v. Delta Air Lines, Inc.[58] illustrates how a condition can allocate responsibility for risks of market changes. Delta agreed to purchase certain of Pan Am's routes and assets and to extend credit to Pan Am, subject to certain conditions, one of which was that since the date of the agreement "there shall have been no material adverse change in the business, financial position, results of operations or prospects of . . . [Pan Am's business remaining after the acquisition]."[59] Between the contract formation and scheduled sale dates, Pan Am's revenues and projected revenues declined materially more than forecast: for example, in November 1991 Pan Am reduced its revenue forecast prepared only two months earlier by $19.5 million or 17.1 percent. Passenger demand for Pan Am's flights declined dramatically during these and the following months. Delta successfully claimed a material adverse change in Pan Am's business and financial condition had occurred, and it was not obligated to close the sale. The condition allocated to both Delta and Pan Am responsibility for the risk that the demand for its flights would decrease between the dates of contract formation and sale. Delta was not obligated to complete the sale or compensate the other for the failed transaction.[60] Nor was Delta entitled to compensation from Pan Am. The case illustrates how a condition precedent allocates a scenario (1)(a)(i) risk for the occurrence of a change that was not to occur: a drop in demand for a Pan Am's products reduced its value to Delta, the buyer of a portion its business.

Force Majeure Clauses

Force majeure clauses have been invoked by parties to excuse their failure to perform when market changes have adversely affected their realization of the anticipated benefits or their completion of tasks. Such parties usually confront difficult challenges in doing so: First, the litany of trigger events in a force majeure clause—earthquakes, hurricanes, strikes, and the like—do not usually include any of the adverse market changes previously described. In principle, a force majeure clause could be, and on occasion has been, expanded to include them. Second, with the exception of unavailability of supply in the market and financial distress, none of the hazards previously described render the obligor unable to perform or otherwise prevent it from performing. Any pressure on an obligor not to perform is financial or economic. Third, almost none of the market changes previously described is truly unforeseeable. The usual requirement that an uncontrollable event must be unforeseeable would have to be omitted from and not otherwise implied in the force majeure clause.

Drop in Demand or Offtake. A drop in demand for an item an obligor expects to sell in the market to realize the benefit of a procurement contract will present a difficult choice but not necessarily impair its ability to perform the procurement contract. Because the value of the procurement contract to the obligor depends upon its realizing in sales to offtakers in the market the value of what it procures, it will have to choose between procuring items it cannot resell (and realize value therefrom) and thus performing and avoiding losses on such procurement but breaching. Since it remains able to perform, it is not disabled by the drop in offtake.

Sabine Corp. v. ONG Western, Inc.[61] illustrates the difficulty of using a force majeure clause to allocate responsibility for a drop in demand risk. A buyer agreed to take or pay for a minimum quantity of gas to be supplied by the supplier each year. When demand from the buyer's customers dropped, partly due to energy conservation and partly due to the availability of gas at lower prices from other suppliers, the buyer claimed its obligation to take or pay for the minimum was excused under the force majeure clause, which listed the usual events but did not specifically mention changes in demand or price for gas.[62] For the buyer's claim to succeed, the force majeure clause had to be interpreted to include such market changes as force majeure events and to apply when those changes did not impair its ability to perform but presented it with a costly choice between performing and losing on purchases of gas that could not be resold at a price that would yield a profit and breaching and avoiding those losses. Both conclusions would have been a far stretch to reach in the facts of the case.[63] In addition, the force majeure clause had to trump the take-or-pay clause. The buyer's claim implied the parties shared the risk that demand for the buyer's gas would drop, allowing the buyer to terminate the contract, whereas the seller's claim, accepted by the court, implied that the buyer had expressly assumed responsibility for that risk when it agreed to the take-or-pay clause.[64]

However, a drop in offtake can be devastating to an obligor's financial ability, as when it is nearly total or total, and the obligor is entirely or nearly entirely dependent upon that offtake to survive financially; the obligor will likely become insolvent and unable to pay its supplier (or for that matter any other party). It is unable to perform financial obligations, and that inability is the result of market change in demand for its products. A force majeure clause constructed to apply to such scenario would have to include insolvency as equivalent to an inability to perform.

Compare the following cases in which efforts were made to shoehorn financial distress into the list of events excused under force majeure clauses:

- *Urban Archaeology Ltd. v. 207 East 57th Street LLC* [65]: The tenant agreed to lease premises for 10 years, intending to operate an upscale store for the sale of luxury goods. A year later, the 2008 financial crisis occurred, demand for its products severely dropped, and the tenant became financially unable to pay the rent and claimed its delay in doing so was excused under the force majeure clause. The force majeure clause in the lease provided:

  > The obligation of each party hereunder to perform all of the covenants and agreements hereunder on the part of such party to be performed shall be excused by the period of Unavoidable Delay, as it relates to the particular obligation affected by such Unavoidable Delay and such party's inability to perform shall not relieve the other party of its obligations to perform under this Lease.[66]

  The lease defined an "Unavoidable Delay" as

  > a delay resulting from strikes or labor troubles or accident, or from any cause whatsoever beyond Landlord or Tenant's reasonable control (other than Landlord or Tenant's financial hardship), including, but not limited to, acts of foreign and/or domestic terrorism, laws, governmental preemption in connection with national emergency or by reason of any requirements of any governmental authority, or by reason of the conditions of supply and demand which have been or are affected by war or other emergency.[67]

  While the definition specifically included "supply and demand," it also specifically included the words "other than Landlord or Tenant's financial hardship." The parties contemplated events such as a downturn in the economy resulting in hardship could occur but excluded it from the clause. This implied that responsibility for the risk of a downturn so reducing demand for the tenant's products that it could not pay rent was thus allocated to the tenant.

- *In re Old Carco (f/k/a Chrysler LLC)*[68]: In 2000, Chrysler agreed with a city and a county in Ohio to invest in and to exercise reasonable efforts to retain a number of full-time positions at a plant located there. The city and county each agreed to grant a 50 percent tax exemption for eligible new tangible personal property acquired in conjunction with the project. Following the bankruptcy and reorganization of Chrysler during the 2008–2009 financial crisis, in 2010 Chrysler decided the plant was too financially burdensome to keep open. The drop in demand for its cars resulted in the benefits of operating the Ohio plant and the corresponding contracts with the city and county having little or no value to Chrysler. However, the force majeure clauses in the contract with the city and county required that Chrysler be unable to perform to be excused:

> [Chrysler] shall not be considered . . . in default in the performance of its obligations under this agreement as a result of any cause beyond its reasonable control, including but not limited to severe and unusual weather, acts of God, or explosion, riot, acts of civil disobedience or sabotage, *change to economic conditions and productivity* and technological changes, power failures or shortages, restraint by court order or order of public authority, action or omission by any government agency, labor strikes or other labor disturbances[69] (emphasis added).

For the clause to excuse the plant closure and repudiation of the agreements with the city and county, as Chrysler successfully claimed it did, first, the drop in demand for Chrysler's cars had to be a "change to economic conditions and productivity." That claim seemed superficially plausible: a drop in demand for cars is a change in the economic conditions for a car manufacturer. Nowhere is there any comment about how much the drop must be for it to qualify under the clause. Second, Chrysler's default had to be "as a result" of such conditions. That implied a causal link. One interpretation would be that the change in conditions either disabled or rendered Chrysler unable to perform. The logic of such a claim would be that Chrysler had insufficient funds to continue its operations at the Ohio plant and elsewhere; as a result, it had to choose which operations to continue. That economic compulsion had to satisfy the causal requirement. Chrysler's successful claim implied that the force majeure clause allocated responsibility for the risk of Chrysler having to make such a choice to the city and county.[70] While the case illustrates a successful application of a force majeure clause to a downturn in demand for products, it also illustrates how far the logic of the clause must be stretched to achieve that result.

Short Supply. A supply shortage can more directly preclude an obligor from performing an obligation. Such an obligor cannot procure an item that it must have to perform; as a result, it cannot perform. Its inability may be due to a change in the market: suppliers previously willing are no longer willing to supply, and other potential suppliers have not stepped in to cover the gap. Its inability may be due to suppliers no longer willing to supply the obligor. Where they once judged the obligor as eligible or qualified to buy, they no longer do so. A force majeure clause constructed to apply to the former scenario would have to include a short supply that results in the unavailability in the market of the required item. It would allow an obligor to be excused only where no one can procure the required item. A force majeure clause constructed to apply to the latter scenario would have to include changes in suppliers' attitudes toward the obligor. It could more liberally allow an obligor to be excused even though other buyers can procure the item in the market. It is disabled by a market change when other firms would not. The distinction between the two clauses is also analogous to objective and subjective impossibility and infeasibility and inability. Force majeure clauses can thus be used to allocate supply shortages.

Kel Kim Corp.[71] illustrates the challenge of using a force majeure clause to allocate a supply shortage risk. The case is previously summarized.[72] A tenant who operated a roller skating rink could not procure public liability insurance consistent with the lease terms. The force majeure clause in the lease excused either party's failure to perform if such performance was "delayed or prevented . . . by reason of labor disputes, inability to procure materials, . . . Acts of God, or other similar causes beyond the control of such party."[73] The clause did not specifically mention an inability to procure insurance. For the clause to have applied to the tenant's failure to procure the required insurance, as the tenant claimed, either "inability to procure materials" or "other similar causes" had to include such inability or the unwillingness of insurers to insure the tenant even if insurers were willing to insure operations similar to the tenant's.[74] The tenant's claim that the force majeure clause excused the insurance requirement so long as it could not procure the required insurance implied that responsibility for the risk of a supply shortage was borne by the landlord, as the tenant could continue to enjoy the benefits of the lease without having to perform the excused obligation.

Price Changes. Similar to a drop in demand, a drop in price for an item, the sale of which is anticipated to yield the buyer the benefit of its procurement contract with its supplier, presents that party with a difficult choice but does not impair its ability to perform the procurement contract. This predicament exists only where the price received for its item is less than the price it pays for that item or the input to make the item. The buyer must choose between procuring items it cannot resell at the anticipated price (and thus realize anticipated value therefrom) and performing and avoiding losses on such procurement but breaching. Because it remains able to perform, it is not disabled by the drop in offtake. A force majeure clause constructed to apply to the former scenario would have to include a reduced price from offtakers as a force majeure event. It might allow a buyer to be excused only when the drop in price subjects the buyer to financial pressure or severe financial pressure to make such choice. Such a clause would acknowledge the buyer is not disabled from performing by the drop in offtake prices and being confronted with such difficult choice is sufficient to excuse a decision not to perform. Such a clause might omit the requirement of financial pressure on the obligor and excuse its decision not to perform because doing so would be unprofitable or highly unprofitable. The difficulty of obtaining agreement to such a clause may be a reason why the wording in the force majeure clause *In re Old Carco (f/k/a Chrysler LLC)*[75] referred to an inability to perform.

Seaboard Lumber Co. v. United States[76] illustrates an effort to apply a force majeure clause to such a drop in prices. A contractor agreed to cut, remove, and pay a fixed price for a quantity of timber on US Forest Service lands. Prices for lumber dropped after contract formation due to depressed demand for lumber in the housing market. Deregulation of savings and loan institutions and the imposition of monetary controls may have contributed to the drop in demand for lumber. The contractor refused to perform, claiming force majeure, impossibility, commercial impracticability, and frustration of contract. The force majeure clause excused delays in performance due to one or more of events listed in the clause.[77] For the force majeure clause to apply, the trigger events would have had to include the changes in government policy affecting the economy generally and lumber prices specifically. The clause would also have had to apply when the contractor had to choose between performing and thus suffering a loss and breaching and avoiding that loss. The lower price did not actually prevent the contractor from cutting and selling timber. The contractor's unsuccessful claim that its contract should have been extended under the force majeure clause implied that the government bore responsibility for the risk of price decreases, as it could neither terminate nor hold the contractor in breach so long as such condition existed.[78]

An increase in the price a buyer pays its supplier is the mirror image of a decrease in the price the buyer receives from its offtaker. An increase in the price a buyer pays for an item, the sale of which at a fixed price is anticipated to yield the buyer the benefit of its procurement contract with its supplier, presents the buyer with a difficult choice but does not impair its ability to perform the procurement or the offtake contract. This predicament exists where the price received does not at least match the price paid for an item. It may have to choose between procuring items it cannot resell at the anticipated price (and thus realize anticipated value therefrom) and thus performing and avoiding losses on such procurement and thus breaching. Alternatively, it may have to choose between selling items it cannot buy at the anticipated price and thus performing and avoiding losses on such sale but breaching. Since it remains able to perform, it is not disabled by the increase in procurement prices. A force majeure clause constructed to apply to the former scenario would have to include an increased price from suppliers as a force majeure event. It could allow a buyer to be excused when the increase in price subjects it to financial pressure or severe financial pressure to make such choice. Such a clause would acknowledge the buyer is not disabled by the increase in procurement prices and being confronted with the difficult choice is sufficient to excuse a decision not to perform. As in the case of a drop in price for the products a party sells in the market, a force majeure clause might omit the requirement of financial pressure on the obligor and excuse its decision not to perform because doing so would be unprofitable or highly unprofitable. Again, the difficulty of obtaining agreement to such a clause may be a reason why examples of such clause cannot be found.

Hudson v. D & V Mason Contractors, Inc.[79] illustrates an effort to use a force majeure clause to cover the increases in a contractor's labor and material costs. A contractor agreed to build a house for a fixed price. Between the contract formation and scheduled completion dates, construction costs increased 10 to 15 percent. The contractor notified the owner that the work could not be completed at the agreed price but could be at a higher price. Two clauses were relevant. The first read:

> If for any reason Seller's title is not good and marketable and Seller shall be unable to perfect such title, or if for any other reason Seller is unable to construct or complete said premises or make title as herein provided, Seller shall return to the Purchaser the sum or sums paid on account of the purchase price, without interest, and this agreement shall thereupon become cancelled, null and void, and the Seller shall have no further liability whatsoever to Purchaser.[80]
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> The other clause provided:
>
> This agreement is conditioned upon the ability of Seller to complete the above described property under conditions similar to those presently existing in the home building industry. If Seller is unable to procure promptly, as and when needed, labor and material required for construction as aforesaid, or if Seller for any reason cannot complete these premises due to any present or future rules, regulations or restrictions (particularly those involving priorities or material allocation) by the federal, state or municipal governments, or their agencies, then, and in any such event, Seller is hereby given the option to cancel this contract upon written notice to Purchaser, in which event the full deposit money shall be returned to Purchaser without interest, and this agreement shall thereupon become cancelled, null and void, and Seller shall have no further liability whatsoever to Purchaser.[81]

For the first clause to apply to the seller's increased labor and materials costs, "any other reason" would have to have included an increase in such costs, and "unable to construct or complete" would have to have included the choice the contractor was compelled to make, between performing and suffering a loss, on one hand, and breaching and avoiding the loss, on the other. For the second clause to apply, "conditions similar to those presently existing in the home building industry" would have to include the labor and material costs at contract formation, and the second sentence would have to have been inapplicable. No additional requirement would have to be satisfied for the contractor to be excused under the first sentence of the second clause. The report of the case is unclear on whether the contractor simply demanded an increase in price to cover its higher costs or confronted the buyer with a choice: to pay more or suffer termination of the contract. The former implied that the buyer bore the risk of increase labor and material costs, while the latter implied that the parties shared the risk, allowing the contractor to terminate when such costs increased. In either event, the force majeure clause, as the buyer successfully claimed, did not allocate responsibility for the risk.[82]

"Reopener" Clause

As observed in chapter 11, a party may be willing to concede at contract formation that certain uncontrollable events, while not automatically entitling the other party to any specific relief from performance or to compensation or indemnification, may be grounds for a request from the other party to discuss or negotiate an amendment to the contract that grants the other party appropriate relief. Such uncontrollable events can include all market changes: loss or a material deterioration of the benefits, an increase in the costs of performing obligations for the benefit of the other party or completing a task that enables a party to realize its benefits, and delays in such performance, completion, or benefit realization. Such a clause that allows the affected party to request reconsideration of the bargain combines a condition subsequent, the occurrence of an adverse market change, with an agreement to negotiate or agree modified terms. As noted in chapter 11, the party unaffected by the event may be under little or no legal obligation to accommodate the affected party's concerns, but nonetheless it may have good financial and other business reasons for doing so. As with a reopener clause for uncontrollable events, the failure to reach agreement on such relief may leave the affected party in the same position as if the reopener clause had not been included in the contract.

The alternative procedures for amending a contract so as to entitle a party adversely affected by a market change to relief or compensation for such an event are also comparable to those for a reopener clause for an uncontrollable event: the amendment might be determined by one party, exercising absolute discretion, be proposed by one and accepted by the other, or agreed by both parties. *Novelis Corp. v. Anheuser-Busch, Inc*.[83] illustrates a reopener clause expressly applicable to market changes. Under contracts dating to 1987, Novelis sold Anheuser-Busch, Inc. (A-B) aluminum can sheets at a price calculated using two components: a metal component and a conversion component. The metal component could not be increased above an agreed maximum amount. Another clause stated:

> If during the Term of this Agreement, either party believes that market conditions have changed structurally up or down, in such a manner that causes the current pricing mechanisms to no longer be appropriate, A-B and [Novelis] . . . will meet to discuss a new pricing mechanism with the continued intent to provide competitive pricing to A-B, including without limitation, providing B the Contract Discount set forth above. It is the intent of the parties, however, that if the parties, in each party's sole discretion, are unable to reach a mutually acceptable modification to this Agreement, this Agreement as amended shall remain in full force and effect until the expiration or earlier termination hereof.[84]

In 2008, Novelis invoked this clause, claiming a "rise in energy prices, speculation by hedge funds and other investors, and dramatically increased demand for aluminum from China and other developing countries" had changed the structural price conditions. The parties failed to agree on a new price, and Novelis sued A-B for breach of the obligation to negotiate the new price. The parties clearly identified the risk that Novelis's procurement prices might be higher than could be passed through under the metal component of the price formula. The clause created a condition subsequent that was triggered when a "party believes that market conditions have changed structurally up or down."[85] Novelis's claim that A-B had to negotiate a change in price implied that A-B bore responsibility for the risk of price increases above the cap on the metal component. In effect, that cap would have been trumped by the mistake of fact, frustration, and impossibility doctrines. A-B's successful motion for summary judgment implied responsibility for the risk of procurement price increases was allocated by the cap to Novelis, notwithstanding the clause for renegotiating the terms. Had the clause allowed either party to terminate upon failure to agree new terms, responsibility for the risk would have been shared; each party would have had to bear the loss of its investment in the transaction to the extent not recovered prior to termination and the loss of anticipated benefits that could not otherwise be earned elsewhere. Had the clause stated how new terms were to be determined, responsibility for the risk would have been allocated to the party disadvantaged by the new terms. The case illustrates how a reopener clause applies to a (1)(b)(iii)(B)(II) market change risk: an increase in the market price a supplier must pay for raw materials to perform its obligations to its buyer can trigger a price reopener in the contract with its buyer, but responsibility for the risk remains as allocated by the price formula unless an alternative price can be formulated. Finally, the case illustrates the value of an express disclaimer, in this instance a clear disclaimer of any commitment by A-B to agree to any changes in the compensation payable to Novelis notwithstanding one or more significant market changes. The disclaimer narrowed the scope of the reopener to discussions, with no commitment to negotiate, let alone to agree to an amendment.

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1 BLACK'S LAW DICTIONARY 970 (10th ed. 2014).

2 *Id*.

3 659 F. Supp. 796 (D. Kan. 1987).

4 See text accompanying ch. 10, note 27.

5 The agent claimed termination was permissible because performance was commercially impracticable and frustration of purpose. The court agreed that the purpose of the exclusive agency contract had been frustrated: "When the insurance policies became unmarketable, defendant [the agent] was totally deprived of the benefits of the contract. Although the unmarketability of the policies did not make performance by either party impracticable, it did make performance useless." *Id*. at 804. The court held that the frustration doctrine did not apply because the agent had superior knowledge of local conditions and could have foreseen the change in market conditions. By failing to provide for such change, it had assumed the risk. *Id*.

6 266 F. Supp.2d 1214 (D. Ha. 2003).

7 *Id*. at 1216.

8 931 F.2d 1112 (6th Cir. 1991).

9 KW sued for breach of contract; the manufacturer claimed performance was commercially impractical because of the sharp change in market conditions, citing the fact that the division had been losing $2 million per day. The trial court allowed the jury to consider the defense, and the jury found for the manufacturer. The appeal court reversed, holding that "application of the impracticability defense in this case would allow IH [the manufacturer] to avoid its liability under franchise agreements, allow [the buyer] Case/Tenneco to pick up only those dealerships it sees fit, and leave the remaining dealers bankrupt. In such circumstance, application of the doctrine of impracticability would not only be a misapplication of law, but a windfall for IH at the expense of the dealers." *Id*. at 1118.

10 871 F. Supp. 2d 843, 104 A.L.R.6th 675 (D. Minn. 2012).

11 This case is further discussed in *infra* note 64.

12 313 Mich. App. 437, 886 N.W.2d 445 (Mich. App. 2015).

13 "Specifically, even taking plaintiff's factual allegations as true and construing them in plaintiff's favor, the allegations of the complaint only indicate that the deflation of the market price for polysilicon has rendered plaintiff's contract with defendant unprofitable. The risk of such a deflation of market prices—no matter the cause—was expressly assumed by plaintiff in its take-or-pay contract with defendant. Plaintiff opted not to protect itself with a contractual limitation on the degree of market price risk that it would assume. It cannot now, by judicial action, manufacture a contractual limitation that it may in hindsight desire by broadly interpreting the force-majeure clause to say something that it does not." *Id*. at 452–53.

14 BLACK'S LAW DICTIONARY, *supra* note 1, 898.

15 235 Minn. 292, 50 NW2d 707 (Minn. 1951).

16 *Id*. at 302.

17 The court disagreed, holding, "It is the general rule that ordinarily the fairness of a contract is to be determined in the light of the circumstances that existed at the time of its making rather than by the effect of subsequent events which intervene before specific performance is sought. Adequacy or inadequacy of consideration for the property sold is to be determined as of the inception of the contract rather than according to the increased or decreased value of the property at the time of trial." *Id*.

18 2000 PEISCTD 1 (2000).

19 Justice Armand DesRoches refused the request, rejecting application of the frustration doctrine to the case, though expressing some reluctance about the result. "The respondent's payment of an annual rental of $58.40 for four prime city waterfront lots appears clearly to result in it enjoying a hugh (sic) economic advantage under the lease for which it pays virtually nothing. This economic advantage is

especially striking when measured against the fact that the annual rental is used by the Cumberland Trust for the awarding of educational scholarships and prizes." *Id*. at 17.

20 923 F. Supp. 2d 351 (N.D.N.Y. 2013).

21 The court dismissed the tenant's claims, holding that however the defense was characterized, the inability to obtain insurance was foreseeable, and as such, neither defense was available. The market in all-risk insurance did not materially change after contract formation; rather, the insurers' willingness to insure the specific property declined because of the flooding, together with the prior history of flooding.

22 70 N.Y.2d 900, 524 N.Y.S.2d 384, 519 N.E.2d 295 (N.Y. 1987).

23 The landlord notified the tenant of the default, and the tenant responded that obtaining the replacement insurance was impossible and sued for a declaration that its performance was excused. The trial court awarded summary judgment to the landlord. The New York Court of Appeal affirmed, holding the tenant's "inability to procure and maintain requisite coverage could have been foreseen and guarded against when it specifically undertook that obligation in the lease, and therefore the obligation cannot be excused on this basis." *Id*. at 902. The court also held the force majeure clause did not apply to the tenant's inability to procure the required insurance, stating, "[T]he events listed in the force majeure clause here are different in-kind and nature from *Kel Kim's* [the tenant's] inability to procure and maintain public liability insurance." *Id*. at 903.

24 582 F.3d 721 (7th Cir. 2009).

25 "[I]f no one could have foreseen the extent of the credit crunch in 2008—and if it really made performance impossible, a subject on which the parties profoundly disagree—then the sort of argument that Hoosier Energy [the lessee] makes could satisfy the requirements of *Kel Kim*." *Id*. at 729.

26 The district court found in favor of the lessee. Affirming the decision, Chief Judge Frank Easterbrook added an important qualification: "So although we affirm the district court's preliminary injunction, we conclude that, if Hoosier Energy [the lessee] has not produced a replacement for Ambac [the credit swap provider] by the end of 2009, the time will have arrived when the court must let John Hancock realize on its security." *Id*. at 730.

27 *See also* Ner Tamid Congregation of North Town v. Krivoruchko, 638 F. Supp.2d 913 (N.D. Ill. 2009), where a contract for the sale of property did not include a condition that the buyer obtain the financing it required to complete the purchase, the buyer being confident it would be able to obtain such loans. When he failed to close the purchase, the seller sued and moved for summary judgment, which was granted. The buyer's argument that the recession in 2007 to 2009 had made it impossible for him to obtain the loans was dismissed. The court held the risk of the recession was irrelevant: "It is precisely because inability to obtain financing is a foreseeable (and significant) risk that can be readily guarded against in the parties' agreement that financing contingency provisions are common in both commercial and residential real estate contracts." *Id*. at 928.

28 410 F.3d 981 (7th Cir. 2005).

29 See text accompanying ch. 4, notes 23 and 24.

30 The seller sued for the second payment and royalties, and the buyer counterclaimed for fraud. The trial court dismissed the buyer's claim, and the jury awarded a verdict in favor of the seller.

31 76 Misc.2d 1080, 352 NYS2d 784 (N.Y. Sup. Ct. 1974).

32 *Id*. at 1082.

33 The court disagreed, finding the price increase of 10 percent during the year running up to contract formation should have made the supplier "aware of the general inflation in this country during the previous years and of the chance of crop failures." *Id*. at 1085.

34 [1978] 3 All ER 769, [1978] 1 WLR 138.

35 The hospital authority took out an originating summons to have the contract declared enforceable, and the trial court found in its favor. The appeal court allowed the water company to terminate the contract.

36 646 F.2d 434 (10th Cir. 1981).

37 The trial court determined that the contract did not allow the importer to increase the price for exchange rate fluctuations and the appeal court affirmed. The importer claimed the exchange rate fluctuations rendered its performance under the contract impractical under the Utah version of Uniform Commercial Code section 2-615. The appeal court disagreed, citing a letter from the importer before contract formation: "Importer's letter to Distributor concerning a 7% devaluation of the dollar in relation to the franc, sent three weeks prior to the contract execution, shows clear foreknowledge of the possibility of currency fluctuations (Ex. 41) and, thus, supports the finding that section 2-615 is inapplicable." *Id*. at 439. The court added, "Finally, cost increases alone, though great in extent, do not render a contract impracticable." *Id*.

38 415 F. Supp. 429 (S.D. Fla. 1975).

39 After hearing the evidence, District Judge James Lawrence King held in favor of Eastern. He found that the parties "intended to be bound by the specified entries in Platt's, which has been published at all times material here, which is published today, and which prints the contract reference prices. Prices under the contract can be and still are calculated by reference to Platt's publication." *Id*. at 439. Some 60 percent of Gulf's production was still subject to price regulation. The judge found that Gulf had not met its burden of proof on the commercial impracticability defense because he could not determine Gulf's cost of production of crude outside the United States. Gulf's domestic subsidiaries bought crude oil from its foreign subsidiaries at prices determined by Gulf. *Id*. at 441.

40 931 F.2d 1112 (6th Cir. 1991).

41 122 Ill. App.3d 940, 461 N.E.2d 1049 (Ill. App. 1984).

42 122 Ill. App.3d 940, 952.

43 646 F.2d 434 (10th Cir. 1981).

44 646 F.2d 434, 439.

45 669 F. Supp. 1038 (Colo. 1987).

46 "The purpose of the take-or-pay clauses is to apportion the risks of natural gas production and sales between the buyer and seller. The seller bears the risk of production. To compensate seller for that risk, buyer agrees to take, or pay for if not taken, a minimum quantity of gas. The

buyer bears the risk of market demand. The take-or-pay clause insures that if the demand for gas goes down, seller will still receive the price for the Contract Quantity delivered each year." Universal Resources Corporation v. Panhandle Eastern Pipe Line Company, 813 F.2d 77, 80 (5th Cir. 1987); *quoted at* 669 F. Supp. 1038, 1041.

47 915 F.2d 805 (2d Cir. 1990).

48 The district court granted the shareholder summary judgment on these issues.

49 517 F. Supp. 1319 (E.D. Lou. 1981).

50 The alleged mutual mistake was that the clauses providing for escalation of the price would be sufficient to cover the supplier's cost increases, and the commercial impracticability was the assumption that labor and material would not rise so sharply. The district court, granted the buyer's motion for summary judgment on both issues. *Id*. at 1326.

51 499 F. Supp. 53 (W.D. Pa. 1980).

52 *Id*. at 68.

53 Alcoa and Essex had acknowledged the risk that nonlabor costs could deviate significantly from the WPI-IC, assessed the probability of the risk occurring to be low, and chose not to address it. The judge concluded that "the absence of an express floor limitation can only be understood to imply that the parties deemed the risk too remote and their meaning too clear to trifle with additional negotiation and drafting." *Id*. at 69.

54 584 F. Supp. 990 (N.D. Ohio 1984).

55 The court found that the employers' organization had not proved that it was an assumption of the contract that the Cleveland CPI-W would not deviate from the National CPI-W or the parties intended that the union members enjoy a cost of living adjustment that would accurately and closely reflect the inflation rate in Cleveland.

56 713 F.2d 452 (9th Cir. 1983).

57 The court denied relief to the landlord, holding frustration was available only when "the difference [between what had been and what was now required] be so excessive as to make performance extremely impracticable." *Id*. at 454.

58 175 B.R. 438 (Bankr. S.D.N.Y. 1994).

59 *Id*. at 492.

60 The bankruptcy court found this condition was not satisfied because after contract formation Pan Am's revenues and projected revenues had declined materially more than forecast.

61 725 F. Supp. 1157 (W.D. Okl. 1989).

62 *Id*. at 1166.

63 The court, while acknowledging demand for the buyer's gas had shrunk, concluded demand was still sufficient to keep the contract effective. "While Defendant has submitted evidence that it has lost some of its customers and that its customer base is smaller, it is implicit in affidavits submitted by Defendant and in Defendant's arguments that Defendant has customers who still need a supply of gas and that its parent's division, as a public utility, is still obligated to supply customers with gas." *Id*. at 1179.

64 The court held that neither a decline in demand nor price was a force majeure event within the meaning of the clause. "[T]he Court must reject an interpretation of the force majeure clause which would render the take-or-pay and price redetermination provisions, pursuant to which Defendant ONG clearly assumed the risk of a decline in market demand and market price." *Id*. at 1171. *See also* Great Lakes Transmission Ltd. Partnership v. Essar Steel Minnesota, LLC, *supra* note 10. The force majeure clause in the contract read, "Neither Shipper nor Transporter shall be liable in damages to the other for any act, omission or circumstances occasioned by or in consequence of: any acts of God, strikes, lockouts, acts of the public enemy, wars, blockages, insurrections, riots, epidemics, landslides, lightning, earthquakes, fires, storms, floods, washouts, arrests and restraints of rulers and peoples, civil disturbances, explosions, breakage or accident to machinery or lines of pipe, line freeze ups, . . . or the binding order of any court or governmental authority which has been resisted in good faith by all reasonable legal means, and any other cause, whether the kind herein enumerated or otherwise. . . ." *Id*. at 851–52. The shipper sued for a declaration that the contract was no longer enforceable because the facility could not be built, financing being unavailable because of the financial crisis. The supplier moved to dismiss for failure to state a cause of action. The court granted the motion. Judge Susan Richard Nelson held the force majeure clause inapplicable because financial crisis was not included in the list of force majeure events, the contract expressly stated that payment obligations were not excused, and the contract was for the transportation of gas and did not state it was conditioned upon the construction of the facility. She similarly dismissed the shipper's commercial impracticability defense. "It was completely foreseeable that ESML [the shipper] might not secure the necessary financing for the Nashwauk facility. Given that possibility, MSI/ESML could have conditioned its performance on obtaining such financing. It failed to do so." *Id*. at 858.

65 34 Misc.3d 1222(A), 951 N.Y.S.2d 84 (Table), 2009 WL 8572326 (N.Y. Sup.), 2009 NY Slip Op 52825(U) (N.Y. Sup. Ct. 2009), *aff'd*. 68 A.D.3d 562, 891 N.Y.S.2d 63. (N.Y. App. 2009).

66 2009 NY Slip Op 52825(U), at 3.

67 2009 NY Slip Op 52825(U) at 3–4.

68 452 B.R. 100, 55 Bankr. Ct. Dec. 72 (S.D.N.Y. 2011).

69 *Id*. at 107.

70 The court held that while economic considerations would not normally excuse a failure to perform, in this case, where the clause expressly mentions "change to economic conditions," such considerations would excuse where they caused the plant's closure. *Id*. at 119–20. The court found the financial crisis of 2008–2009 qualified as "change to economic conditions." It also found that such events were beyond Chrysler's control. The court forged the causal link between such events, and the plant closure by finding Chrysler had "little or no choice" but to close the plant: "Further, the determination by New Chrysler not to continue operations at the Plant was simply a business decision of New Chrysler based on its anticipated production needs. The substantial carrying costs associated with the Plant would have rendered Old Carco's retention of the Plant impossible, or at the least, unreasonably expensive. . . . Absent a continuation of the license agreement with New Chrysler or some other similar arrangement, Old Carco, having no business to conduct at the Plant, and in the process of liquidating all its remaining assets, was left without any alternative except to close the Plant." *Id*. at 124–25.

71 70 N.Y.2d 900, 524 N.Y.S.2d 384, 519 N.E.2d 295 (N.Y. 1987).

72 See text accompanying notes 22 and 23.

73 The complete force majeure clause read, “If either party to this Lease shall be delayed or prevented from the performance of any obligation through no fault of their own by reason of labor disputes, inability to procure materials, failure of utility service, restrictive governmental laws or regulations, riots, insurrection, war, adverse weather, Acts of God, or other similar causes beyond the control of such party, the performance of such obligation shall be excused for the period of the delay.” 70 N.Y.2d at 902, footnote.

74 “Here, of course, the contractual provision does not specifically include plaintiff’s inability to procure and maintain insurance. Nor does this inability fall within the catchall ‘or other similar causes beyond the control of such party.’ The principle of interpretation applicable to such clauses is that the general words are not to be given expansive meaning; they are confined to things of the same kind or nature as the particular matters mentioned.” *Id*. at 903.

75 452 B.R. 100 (S.D.N.Y. 2011).

76 308 F.3d 1283 (Fed. Cir. 2002).

77 The contract entitled the contractor to an adjustment if it “experiences delay in starting scheduled operations or interruption in active operations either of which stops removal of Included Timber from Sale Area through curtailment in felling and buckling, yarding, skidding and loading, hauling or road construction, as scheduled under B6.31, for 10 or more consecutive calendar days during a Normal Operating Season due to causes beyond Purchaser’s control, including but not limited to acts of God, acts of the public enemy, acts of Government, labor disputes, fires, insurrections or floods.” *Id*. at 1292.

78 The court’s comment on the force majeure defense is illustrative: “Seaboard entered into a fixed-price contract with the Forest Service. The contract allowed for term adjustment if acts of government prevented removal of timber. At most, the government’s acts indirectly made performance of the . . . contract unprofitable. The timber was of sufficient quality, and Seaboard simply made a business decision not to harvest. Timber prices fell and Seaboard must bear this market risk in the absence of contractual language that directs otherwise. For these reasons, the Court of Federal Claims did not err in holding that Seaboard’s force majeure defense fails as a matter of law.” *Id*. at 1294.

79 252 A.2d 166 (Del. Sup. Ct. 1969).

80 *Id*. at 168.

81 *Id*.

82 Judge Robert O’Hora applied the rule that the court would construe these clauses against the contractor. He said, “Unavailability of labor and materials and existence of rules and regulations making completion impossible are the only factors which will excuse performance under paragraphs 13 and 26 [quoted above] of the contract. Nowhere does the contract say that increased cost to the Seller will excuse performance.” *Id*. at 169.

83 559 F. Supp. 2d 877 (N.D. Ohio 2008).

84 559 F. Supp. 2d 877, 880.

85 The buyer moved for summary judgment. The court granted the motion, finding the buyer had met and discussed changing the price as it was obligated. “Ultimately, these two international corporations negotiated and renegotiated at arm’s length a detailed and complex contract governing hundreds of millions of dollars in sales. If they intended the price to automatically change along with market conditions, they would have omitted the price ceiling and explicitly provided in the contract for an adjustment to the price in accordance with the market conditions.” Footnotes omitted. 559 F. Supp. 2d 877.