

Terminal Contract/Environmental Regulations: Federal Appellate Court Addresses Claims of Excused Performance Related to Coal Shipments



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The United States Court of Appeals, Eleventh Circuit (“Eleventh Circuit”), in a February 17th Opinion addressed a dispute involving a terminal contract with a minimum coal tonnage use provision. See *Drummond Coal Sales Inc. v. Kinder Morgan Operating LP “C”*, 2021 WL 613748.

The issue addressed was whether the inability to meet the minimum tonnage shipping requirements were excused because of the impact of government environmental regulations.

Drummond Coal Sales Inc. (“Drummond”) and Kinder Morgan Operating LP “C” (“Kinder Morgan”) entered into a 10-year contract. Kinder Morgan agreed to allow Drummond to import coal through its Shipyard River Terminal (“Terminal”) in Charleston, South Carolina.

Drummond is stated to have committed to importing between 3, 111,111 and 4,000,000 tons of coal per year through the Terminal. In the event the minimum tonnage requirement was not met, shortfall payments to Kinder Morgan were required.

In year nine of the 10-year contract Drummond stopped making payments when it did not meet its minimum tonnage requirements.

Drummond claimed that new environmental regulations had adversely impacted the coal market around the Terminal reducing demand. The end users for Drummond’s coal was primarily coal-fired power plants. Specifically, Drummond alleged in a Complaint filed in federal District Court:

Over the last several years [] the Environmental Protection Agency (EPA) and various other government agencies have proposed and implemented stringent environmental rules and regulations that greatly impacted the consumption of coal by power plants and other end users in the United States.

Drummond further alleged that since 2010 approximately 40% of the United States coal-fired power plants have been retired. The referenced environmental regulations were alleged to have been “especially harsh on power plants which would have received coal imported through the River Terminal.” The company also argued that due to the new environmental regulations the market for imported coal in the relevant area had essentially ceased to exist.

Drummond’s Complaint in federal District Court asserted five claims for declaratory relief:

1. unforeseeability;
2. frustration of purpose;
3. force majeure;
4. impossibility or impracticability of performance; and
5. excused performance due to Kinder Morgan's inability to perform.

Drummond sought a declaration that it was not required to satisfy the minimum tonnage requirements or remit the penalty payment for calendar year 2015 or the remaining term of the contract.

A Magistrate issued a lengthy opinion which the United States District Court adopted. The Eleventh Circuit ultimately appends and agrees with the Magistrate's Decision.

The Magistrate dismissed Drummond's frustration of purpose, force majeure, and impossibility claims. He allowed the material breach claim to proceed. However, the Magistrate subsequently granted Summary Judgment to Kinder Morgan on the material breach claim.

By way of summary, the rationale for disposing of these claims for each included:

- Unforeseeability. The Magistrate noted that in determining whether a particular event is foreseeable, New York courts have looked to the sophistication of the parties. Drummond and Kinder Morgan were deemed sophisticated. The contract was deemed to have anticipated that environmental regulations could affect the parties' contract expectations. The Magistrate rejected Drummond's argument that even if the environmental regulations were foreseeable, the extent of their impact may have been unforeseeable.
- Impossibility. Under New York law the Magistrate notes that a party to a contract generally must perform or respond in damages for its failure even when unforeseen circumstances make performance burdensome. It is further noted that a party's performance of contractual obligations may be excused under the doctrine of impossibility, stating:

only when the destruction of the subject matter of the contract or the means of performance makes performance objectively impossible. Moreover, the impossibility must be produced by an unanticipated event that could not have been foreseen or guarded against in the contract

Government action can render performance impossible. However, this is only the case if the action was not foreseeable. The Magistrate held that Drummond's Complaint did not plausibly state that the subject matter of the contract had been destroyed. The Magistrate further indicated that the Complaint does not plausibly state the performance of the contract is objectively impossible. Noted was the fact that coal-fired power plants continue to operate in the area that would receive coal from the Terminal. Distinguished is the fact that environmental regulations negatively affect the market for imported coal. A financial hardship does not constitute impossibility.

- Frustration of Purpose. As to frustration of purpose, the Magistrate stated that:

Where, after a contract is made, a party's performance is made impracticable without his fault by the occurrence of an event the non-occurrence of which was a basic assumption on which the contract was made, his duty to render that performance is discharged, unless the language or the circumstances indicate the contrary.

The Magistrate states that events justifying the application of frustration of purpose must be "virtually cataclysmic" and "wholly unforeseeable" and "render the contract valueless to one party." Lower profits or sustained loss is insufficient. The Magistrate held that Drummond's claim for frustration of purpose failed. Also noted was the fact that the contract allocated risks for environmental regulations affecting Kinder Morgan and assigned those risks to Drummond. Drummond is characterized as a sophisticated entity entering into these kind of contracts and it assumed such risks.

- Force Majeure. Force majeure is also described as excusing nonperformance due to circumstances beyond the control of the parties. Further, they are stated to be narrowly construed under New York law. Such performance will only be excused if the contract includes the specific event that actually prevents performance. The contract defines a force majeure event as one outside the parties' control and including:

without limitation, any act of God or of a public enemy or terrorist act, labor troubles, strikes, lockouts, riots, nonavailability of machinery, embargoes, blockades or interventions or expropriations by government or governmental authorities, interference by civil or military authorities or other civil unrest, [or] failure or delay of manufacturers or suppliers to deliver machinery or equipment

Drummond argued that the environmental regulations constituted government interventions or interference by civil or military authorities. Kinder Morgan responded that where government regulations merely trigger a party's decision to act, rather than force or prohibit certain actions, a force majeure clause would not apply. Financial hardship was deemed to not constitute grounds for avoiding performance under a contract.

- Excused Performance. Drummond alleged it was excused from performing because in 2015 the Terminal was unable to handle the minimum volume of coal required under the contract. Kinder Morgan's Motion to Dismiss was denied. However, subsequently, Kinder Morgan's Motion for Summary Judgment was granted and the excused performance claim was rejected. Drummond was unable to demonstrate that Kinder Morgan was not ready, willing and able to perform its obligations under the contract. The Magistrate found that Kinder Morgan's performance was dependent upon Drummond actions that had not been taken.

A copy of the Opinion can be downloaded [here](#).