International Law Office

COVID-19: *force majeure* and contract frustration

AUTHOR

Dwight Glinton

01 October 2020 | Contributed by Lennox Paton

The COVID-19 pandemic has disrupted commercial activity on a global scale, challenging contracting parties' ability to fulfil their legal obligations. *Force majeure* clauses and frustration principles may provide some relief to those which may otherwise incur liability because of non-performance.

What is a *force majeure* clause?

A *force majeure* clause enables the parties to a contract to suspend or terminate their obligations where the occurrence of exceptional events or circumstances make the performance of the contract impossible or radically different from that which was undertaken by the contract.

There is no presumption of a *force majeure* event and parties that wish to include a *force majeure* clause in a contract should specifically define the kinds of supervening occurrence that would constitute a '*force majeure*' or 'superior force'. Parties could tailor the clause to include events that may be unique to their circumstances. Occurrences generally accepted as a *force majeure* include:

- riots;
- war;
- rebellion;
- government restrictions;
- earthquakes;
- floods;
- fires;
- strikes; and
- civil unrest.

Unforeseen events that could disrupt a contract are myriad, so the courts may have to interpret a *force majeure* clause to determine whether the particular occurrence is covered. Judges will construe a *force majeure* clause with close attention to the words in the clause and with regard to the general terms of the contract. The effect of the clause may vary with each instrument as certain events in a *force majeure* clause may not always be beyond a party's sphere of control.

Force majeure clauses sometimes include a catch-all phrase such as "or any other cause beyond the parties' control". While in some cases the courts have allowed parties to use this phrase for events not stated or unrelated to those in the *force majeure* clause,(1) in other cases they have rejected certain occurrences even where there was a catch-all phrase.(2)

Where a *force majeure* clause covers a particular event, a party relying on the clause may not be excused from the contact merely because the performance of the contractual obligation is more difficult or less profitable.(3) A defaulting party that wishes to rely on a *force majeure* clause will have the burden of proving that the serious event has made it impossible to perform or radically changed its ability to meet its contractual obligation.

Is COVID-19 a *force majeure*?

Whether the COVID-19 pandemic constitutes a *force majeure* will depend on a contract's wording. It may be covered under a *force majeure* clause if words such as 'pandemic', 'epidemic' or 'disease' are used.

'Act of God' is often used in *force majeure* clauses, and it is widely felt that the COVID-19 pandemic falls within the ambit of this term. 'Act of God' has been legally defined as:

> *such a direct and violent and sudden and irresistible act of nature as the defendant could not, by any amount of ability, foresee would happen, or, if he could foresee that it would happen, he could not by any amount of care and skill resist, so as to prevent its effect.*(4)

It has also been held to cover one-off events which "involved no human agency".(5) Acts of God have generally been confined to natural disasters such as floods and earthquakes.

While it could be argued that COVID-19 is a factor of nature, it seems unlikely that the courts would affirm that it is an act of God because it has historically been applied to geographic phenomena. Also, the nature of the pandemic may not be seen as sufficiently direct or violent so as to make persons unable to avoid its effects.

What is frustration?

Frustration is a common law doctrine that is similar in nature to *force majeure*, but somewhat narrower in scope. It recognises that an event may occur through no fault of the parties, which may make a party unable to carry out its obligations under a contract.

Even if there is no *force majeure* clause in a contract, a party may be relieved from its obligations if it can establish that a frustrating event has occurred. Whether a particular radical development is deemed sufficient to frustrate a contract will generally depend on past decisions of the courts. While there is no specific test to establish frustration, it may generally arise where:

- the frustrating event occurs after the contract is formed;
- the occurrence was beyond the parties' contemplation when the contract was formed;
- the occurrence renders performance impossible or radically different from what the parties originally intended; and
- neither party is at fault.

Hurricanes, earthquakes, strikes and civil unrest have been found to be sufficient to frustrate the performance of a contract.

In *Hepburn v Taylor*,(6) where a defendant sought to rely on the doctrine of frustration in his defence, the court stated that the circumstance rendering it impossible for a party to fulfil its contractual obligations must not be due to that party's fault, and that frustration must not be self-induced.

In *Millennium Telecommunications Limited v Bahamas Telecommunications Company Ltd*,(7) the court affirmed the principles that a frustrating event must be beyond the parties' contemplation when the contract is agreed. The court also stated that the impediment should not be the fault of either party, so circumstances caused by negligence or oversight will not constitute frustration.

Is COVID-19 a frustrating event?

There does not appear to be any clear case law precedent for COVID-19, so it is uncertain whether the pandemic will be deemed a frustrating event by the courts.

It may be found that the pandemic is a frustrating event because of the level of disruption that it has caused to the world's economy. It should be noted that parties which have entered into contracts since the spread of COVID-19 began may be unable to assert frustration because of foreseeability.

Even if the disease itself is not deemed to be enough to frustrate a contract, the consequences flowing from it – such as government curfews and shutdowns – will likely be seen as enough to render carrying out a contract impossible. Many commercial entities were forced to close pursuant to emergency power orders and so performance of commercial activity became impossible through no fault of their own.

Comment

The COVID-19 pandemic is expected to lead to a wave of legal disputes as to which party bears the risks of non-performance. The application of *force majeure* and frustration legal principles in court decisions in the near future will likely better define the rights of contracting parties affected by the pandemic.

In the wake of the pandemic, many companies and individuals have sought to place *force majeure* clauses in commercial contracts and have included the abovementioned words as protection in case they cannot perform their contractual obligations due to COVID-19 or other similar challenges.

Contractual terms, particularly those of great importance to a contracting party's business, should be checked to ensure that a *force majeure* clause is included. In order to protect the parties from difficulties that may arise from a pandemic, the *force majeure* clause should include such key words as 'pandemic', 'epidemic', 'disease', 'government restrictions' and 'state of emergency'.

For further information on this topic please contact Dwight Glinton at Lennox Paton by telephone (+1 242 502 5000) or email (dglinton@lennoxpaton.com). The Lennox Paton website can be accessed at www.lennoxpaton.com.

Endnotes

(1) *Chadris v Isbrandtsen-Moller Co Inc* [1951] 1 KB 240.

(2) *Tandrin Aviation Holdings Ltd v Aero Toy Sore LLC* [2010] 2 Lloyd's Rep 668.

(3) *Tennants (Lancashire) Ltd v G S Wilson & Co Ltd* [1917] AC 485.

(4) *Nugent v Smith* (1876) 1 CPD 423 at 426.

(5) *Transco plc v Stockport Metropolitan Borough Council* [2003] UKHL 61.

(6) [1997] BHS J No 90.

(7) [2017] 1 BHS J No 88.

The materials contained on this website are for general information purposes only and are subject to the disclaimer.