FRIED FRANK

To Our Clients and Friends

Memorandum

March 27, 2020

Is COVID-19 a Force Majeure Event under English Law?

The worldwide spread of the COVID-19 virus presents significant challenges to the global economy. Over the last weeks, the position has intensified, with the World Health Organization declaring the novel coronavirus, COVID-19, to be a pandemic.[1] The virus and the implementation by governments of emergency legislation, travel restrictions, 'lockdowns' and quarantines have impacted supply chains in almost every sector. This has resulted in heightened legal risk for businesses. This memorandum focuses on one particular area of risk: Is COVID-19 a *force majeure* event under English law?

Parties may seek to rely on COVID-19 as a ground to declare *force majeure* such as to discharge or suspend the performance of their contractual obligations. If a counterparty elects to rely on a *force majeure* clause, this will have serious economic consequences on the parties' bargain. It is also likely to result in protracted litigation, causing significant economic and legal uncertainty. Importantly, it will have a consequential impact on other transactions with third parties because, for example, supplies may not be available, funding may be withdrawn or it may put a party in breach of certain financing covenants.

It is therefore essential for businesses to determine whether, for key contracts, there is any basis for a party to declare *force majeure* based on COVID-19 and the actions taken by governments in response.

***Force Majeure* under English Law**

The perhaps surprising starting point is that English law does not recognise *force majeure* as a legal concept. Unlike in civil law systems and in international conventions, the term '*force majeure*' is not a term of art and has no clear meaning.[2] Accordingly, the precise effect of a *force majeure* clause depends principally on the words chosen by the parties.[3]

A *force majeure* clause will be interpreted by reference to the usual principles of contractual interpretation under English law.[4] When interpreting a contract between sophisticated commercial parties, a court or tribunal should, first and foremost, focus on the words used by the parties and give them their ordinary

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1 Available at: https://www.who.int/docs/default-source/coronaviruse/transcripts/who-audio-emergencies-coronavirus-press-conference-full-and-final-11mar2020.pdf?sfvrsn=cb432bb3_2

2 *Thomas Borthwick (Glasgow) Ltd v Faure Fairclough Ltd* [1968] 1 Lloyd's Rep. 16 ("*the precise meaning of the term, if it has one, has eluded lawyers for years*").

3 Lewison, K., *The Interpretation of Contracts*, 6 ed., ¶ 13.01.

4 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896; *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50, [2011] 1 WLR 2900; *Arnold v Britton and Others* [2015] UKSC 36,[2015] AC 1619; *Wood v Capita Insurance Services Ltd* [2017] UKSC 24, [2017] AC 1173.

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and natural meaning. Nonetheless, the words do not exist in a vacuum, and the court or tribunal should have regard to other relevant provisions of the contract, the purpose of the clause, the admissible factual matrix and, to the extent that the words used in the *force majeure* clause are capable of more than one potential meaning, the commercial purpose.[5]

As every contract is different, is entered into against different factual backgrounds and the precise wording of *force majeure* clauses vary, one can only analyse the scope and effect of a clause by focusing in detail on the language used.

Nonetheless, helpful guidance can be derived from leading cases. A *force majeure* clause will often provide that a party is excused from performance of the contract, in whole or in part, or is entitled to suspend performance or claim an extension of time for performance, upon the happening of a specified event beyond its control.[6]

Force majeure clauses commonly used in international transactions governed by English law typically provide that a party is excused where it is prevented or hindered (or impeded) from performing its obligations due to an event or circumstance outside its reasonable control. The clause will often then list a series of events or circumstances, either exclusively or non-exclusively. The lists may extend to an 'act of God', war, riots, civil unrest, strikes, export prohibitions, changes in the law, acts of state authorities, the suspension of necessary licences, etc.

The party relying upon a *force majeure* clause similar to the one summarised above will be required to prove the following[7]:

1. the occurrence of the event or circumstance relied on;
2. that it has been prevented or hindered (as the case may be) from performing its obligations under the contract because of the event or circumstance relied on;
3. that its non-performance was due to circumstances beyond its (reasonable) control; and
4. that there were no reasonable steps that it could have taken to avoid or mitigate the event or circumstances or their consequences.

We consider whether COVID-19 may fall within the scope of a 'typical' *force majeure* clause by looking at each of these requirements.

1. *Is COVID-19 and/or related governmental actions an "event" or "circumstance" falling within the scope of the clause?*

We shall first consider the existence of COVID-19 pandemic itself before addressing governmental actions.

If a clause lists 'pandemics' as one of the events or circumstances, then it is clear that COVID-19 is capable of falling within the scope of the clause. The World Health Organisation is an international

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5 *Wood v Capita*, at [13].

6 *Chitty on Contracts*, 32 ed., ¶ 15-152.

7 *Channel Island Ferries Ltd v Sealink UK Ltd* [1988] 1 Lloyd's Rep. 323; *Tandrin Aviation Holdings Ltd v Aero Store LLC* [2010] EWHC 40 (Comm); 2 Lloyd's Rep. 668.

organisation established by treaty[8] and a specialised agency of the United Nations.[9] The declaration that COVID-19 is a pandemic is likely to be treated as authoritative.

What if the clause refers more generally to 'health emergencies'? Given that the World Health Organization has declared COVID-19 to be an emergency, as have many governments worldwide, COVID-19 is likely to fall within the scope of such a clause. Further, a pandemic is significant example of a health emergency.

What is the position if a *force majeure* clause does not refer to health at all? In these circumstances, a party may attempt to rely on more general language in the clause such as 'act of God'. The position here is far from clear.

The meaning of 'act of God' all depends upon the precise wording used by the parties in accordance with the usual principles of interpretation. Guidance can be sought from previous cases, but caution must be exercised because most of these concerned not *force majeure* clauses, but standard forms used in charterparties and contracts for common carriers. From these cases, it seems that an act of God must be (1) entirely of natural causes without human intervention; and (2) could not have been foreseen, or, if foreseen, could not have been resisted.[10]

Acts of God have been held to extend to, amongst others, earthquakes, a violet storm and fire caused by lightning.[11] It has been extended to illness, but only in the context of a contract for personal services.[12] It is challenging to argue that COVID-19 is entirely of natural causes since it requires human interaction. This is even more evident to the extent that a party attempted to rely on governmental actions in response to the virus as amounting to an act of God. Nonetheless, much will depend ultimately upon the precise words used in the clause under consideration.

Finally, might COVID-19 fall within the scope of a clause referring to '*force majeure*'? Assuming that such a clause were sufficiently certain as to be enforceable, the COVID-19 pandemic may well fall within its scope. This is because this term (while not a term of art) has been held to extend to a range of events broader than an 'act of God', and it goes beyond natural events.[13] In one case, the court said, *obiter*, that a "*flu pandemic*" would constitute *force majeure*.[14]

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8 Constitution of the World Health Organisation, done at New York, on 22 July 1946 (Off. Rec. Wld Hlth Org., 2, 100).

9 Convention on the Privileges and Immunities of the Specialized Agencies, done at New York on 13 February 1946, 1 U.N.T.S. 16.

10 *Nugent v Smith* (1876) CPD 423, 444

11 *Chitty on Contracts*, 32 ed., ¶ 15-161.

12 *Boast v Firth* (1868-69) L.R. 4 C.P. 1.

13 *Lebeaupin v Richard Crispin and Company* [1920] 2 K.B. 714, at 717: where Macardie J quoted from a French legal textbook and stated as follows: "This term is used with reference to all circumstances independent of the will of man, and which it is not in his power to control, and such force majeure is sufficient to justify the non-execution of a contract. Thus, war, inundations, and epidemics, are cases of force majeure; it has even been decided that a strike of workmen constitutes a case of force majeure.' *This is a wide definition, but I think that it usefully though loosely suggests not only the meaning of the phrase as used on the Continent, but also the meaning of the phrase as often employed in English contracts*." (emphasis added)

14 *Clifford Gardner v Clydesdale Bank Limited* [2013] EWHC 4356 (Ch), at [25]: "*absent some form of* force majeure*, for example a flu pandemic*."

Other events or circumstances listed in a *force majeure* clause, such as acts of governmental authorities, changes in the law and the suspension of licences, may well extend to the acts taken by governments in response to the COVID-19 pandemic. For example, on 25 March 2020, the Coronavirus Act 2020 became law in the United Kingdom. This Act grants wide-ranging powers to the government, including the powers, following a declaration made on certain grounds, to close ports and airports, to detain potentially infectious persons and to issue directions (including ordering closure) relating to "*events, gathering and premises*." The exercise of these powers may well fall within the scope of a 'typical' *force majeure* clause.

2. *Has COVID-19 and/or related governmental actions prevented or hindered (as the case may be) a party from performing its obligations under the contract because of the event or circumstance relied on?*

This second limb is key and it is likely to be the main battleground in disputes about whether an exercise of *force majeure* is valid or not. It is one thing to say that COVID-19 and/or governmental actions fall within the scope of the clause in general. It is another to say that they caused the failure of performance.[15] The party relying on the clause has to prove the causal link. We shall consider the two most commonly encountered degrees of impairment in turn.

(a) *Prevented*

A party is only 'prevented' from performing its obligations under a contract if it has become physically or legally impossible to do so, not merely more difficult or unprofitable.[16]

It is not enough for a seller to show that it is unable to obtain the goods or services needed from its intended supplier if it can obtain the goods or services from another supplier, even if at a higher price. Much will depend on the relevant terms in issue though and the bargain as a whole, as a party may be able to rely on such a clause where it is able to show that it was prevented by a government embargo from shipping the goods, even though they could have attempted to purchase substitute goods afloat, on the ground that such an attempt would, in the circumstances of that contract and market, have been impractical and commercially unreasonable.[17]

One could well imagine a business in the hospitality sector claiming that it was 'prevented' from performing a contract because of governmental action requiring closure of hotels and restaurants in response to COVID-19.

Similarly, a business may not be able to perform certain obligations because of governmental action prohibiting non-'key workers' from leaving home to travel to work. Here though, the party would need to show that it was truly prevented from performing its obligations, as it may have been able to perform its obligations by establishing home-working and/or other solutions.

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15 In *Seadrill Ghana Operations Ltd v Tullow Ghana Ltd* [2018] EWHC 1640 (Comm); [2019] 1 All ER (Comm) 34, Teare J held that the triggering event must be the sole cause of the failure to perform, but noted that is ultimately a matter of interpretation of the particular clause.

16 *Tennants (Lancashire) Ltd v CS Wilson & Co* [1917] AC 495.

17 *Tradax Export SA v André et Cie* [1976] 1 Lloyd's Rep. 416, 423; *Bremer Handelsgesellschaft mbH v Vanden-Avenne Izegem PVBA* [1978] 2 Lloyd's Rep. 109, 115.

While much would depend on the nature and duration of the ordered closure vis-à-vis the overall length of the contract, such an argument is certainly plausible.

Similarly, if a contract requires supplies from a country currently subject to a shutdown with restrictions on the export of certain goods, this may well be sufficient to establish that performance has been prevented.

By contrast, a party would be unlikely to succeed in arguing that an economic downturn as a result of COVID-19 'prevented' performance of a contract.

(b) *Hindered*

A clause that requires a party to show that the event or circumstance 'hindered' or 'impeded' its performance is a lower bar than one that requires a party to show that it prevented performance. The leading appellate decision on the issue is *Tennants (Lancashire) Ltd v CS Wilson & Co*.[18] In that case, a clause in a contract for the sale of magnesium chloride gave the sellers the right to suspend performance in the event of contingencies beyond their control, "*such as fire … war strikes or the like preventing or hindering the manufacture or delivery of the article*." Following the outbreak of the First World War, they were cut off from their principal source of supply in Germany, even though a small English source remained available from which they could have satisfied the buyers. The House of Lords held that these events had "*hindered delivery*", even though they might not have prevented it. It is important to note, however, that, the main ground why the sellers were able to rely on the clause 'hindering delivery' was that, because of the events that occurred, they were unable to deliver unless they breached their contracts with other customers.[19]

It is clear, however, that an increase in price, costs of performance or economic grounds will not be sufficient. As the House of Lords stated in *Tennants*:

"*The argument that a man can be excused from performance of his contract when it becomes 'commercially impossible' seems to me to be a dangerous contention which ought not to be admitted unless the parties plainly contracted to that effect*."[20]

Similarly, in *Thames Valley Power Ltd v Total Gas and Power Ltd*, a case concerning a 15-year fixed price gas supply contract, the Commercial Court held that a party was not entitled to rely on a *force majeure* clause due to a substantial increased cost in supplying the gas. The court held as follows:

> "This conclusion [that Total not be permitted to rely on the force majeure clause] is consistent with a line of cases, both on force majeure clauses and on frustration […] to the effect that the fact that a contract has become expensive to perform, even

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18 *Tennants (Lancashire) Ltd v CS Wilson & Co* [1917] AC 495.

19 This is part of the principle from the doctrine of frustration that a party may be permitted to 'allocate' the impact of the *force majeure* event in a rational and reasonable way: *Chitty on Contracts*, 32 ed., ¶ 15-166.

20 *Tennants (Lancashire) Ltd v CS Wilson & Co* [1917] AC 495, per Lord Loriburn at p.510; cf. the *obiter* statement in *Brauer & Co (Great Britain) Ltd v James Clark (Brush Materials) Ltd* [1952] 2 All ER 497: "*If it was one hundred times as much as the contract price, that would be 'a fundamentally different situation' which had unexpectedly emerged, and they would not be bound to pay it*" *per* Denning L.J., at 501G-H.

> dramatically more expensive, is not a ground to relieve a party on the grounds of force majeure or frustration."[21]

Applying these principles to the COVID-19 pandemic, in certain sectors and depending on establishing causation, a party may be able to show that lockdowns, travel restrictions and other governmental actions had 'hindered' its ability to perform certain contracts, particularly where to perform would require real difficulty and involve breaching contracts to other customers, similar to the position in *Tennants*. This may be the case where, for example, the state closes a factory on health grounds or prohibits exports of certain materials needed.

Again, much will depend on the counterfactual as to what whether there were, in fact, other methods of performance available; economic grounds alone are unlikely to be accepted by a court or tribunal.

3. *Is the claiming party's failure of performance due to circumstances beyond its (reasonable) control?*

A *force majeure* clause will usually be interpreted as applicable only where the specified triggering event is beyond the control of the party in question, and cannot be overcome.[22] This is not, however, an invariable rule, and it depends upon the precise wording of the clause in issue.

It emphasises that a party claiming *force majeure* because of COVID-19 will need to establish that its failure of performance was due to the events or circumstances relied on and that these were not due to events within its control. For example, a party is unlikely to succeed in a claim for *force majeure* if the event was caused by its own breach of contract or if there were other reasonable courses of action open to it to perform its obligations, such as obtaining supplies from elsewhere or taking other steps to perform.[23]

4. *Duty to Mitigate*

A 'typical' *force majeure* clause will require a party claiming *force majeure* to take reasonable steps to mitigate the consequences of the *force majeure*. This may extend, depending on the wording and circumstances, to requiring a party to take steps to bring the *force majeure* to an end, and may include seeking supplies elsewhere or other means of performance.

Other Issues

There are a number of other issues that need to be taken into account. The most important of these are addressed below.

Notice

Force Majeure clauses usually have detailed notice provisions which the party claiming *force majeure* ought to fulfil. Depending on the wording of the clause, the requirement to provide prompt notification may amount to a conditions precedent, the failure to comply with which would bar a claim for *force*

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21 [2005] EWHC 2208 (Comm) at para. [50].

22 Lewison, K., *The Interpretation of Contracts*, 6 ed., ¶ 13.04; *Okta Crude Oil Refinery AD v Mamidoil-Jetoil Greek Petroleum Co SA* [2003] 1 Lloyd's Rep. 1 at [53].

23 *Great Elephant Corp v Trafigura Beheer BV* [2013] EWCA Civ 905; [2013] All E.R. (Comm) 992; *Hoecheong Products Co Ltd v Cargill Hong Kong Ltd* [1995] 1 W.L.R. 404.

majeure.[24] Other clauses may, instead, be an intermediate term, the breach of which does not bar the claim for *force majeure,* but may expose the claiming party to a claim in damages for losses flowing from the failure to notify.[25]

It is therefore essential for any party considering claiming *force majeure* or a party who receives a claim to check the notification provisions and assess their legal effect.

Consequences

The consequences of a declaration of *force majeure* depend upon the terms of the contract. A valid declaration of *force ma*jeure may discharge the contract, excuse the claiming party from performance, suspend performance or delay performance until the event giving rise to *force majeure* has abated.[26] A prolonged *force majeure* may also entitle a party to terminate the contract.

The Doctrine of Frustration

It should also be noted that, in the absence of a *force majeure* clause, a party may seek to rely on the doctrine of frustration.[27] The doctrine of frustration allows a contract to be discharged automatically upon the occurrence of a frustrating event such that the parties are no longer bound to perform their future obligations. It cannot be "lightly invoked"[28], and claims of its application rarely succeed. The impact of the doctrine is not considered in detail in this memorandum, but we outline the broad contours of the principles.

In a leading case, the House of Lords held that:

> "Frustration of a contract takes place when there supervenes an event (without default of either party and for which the contract makes no sufficient provision) which so significantly changes the nature (not merely the expense or onerousness) of the outstanding contractual rights and/or obligations from what the parties could reasonably have contemplated at the time of its execution that it would be unjust to hold them to the literal sense of its stipulations in the new circumstances; in such case the law declares both parties to be discharged from further performance."[29]

The application of the doctrine depends upon the interpretation of the obligation in the contract in light of the circumstances that have now arisen. Accordingly, past cases can only be a guide, albeit a helpful

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[24] Lord Wilberforce held in *Bremer Handelgesellschaft v Vanden Avenne-Izegem PVBA* [1978] 2 Lloyd's Rep. 109, 113 that "*Whether this clause is a condition precedent or a contractual term of some other character must depend on (i) the form of the clause itself, (ii) the relation of the clause to the contract as a whole, (iii) general considerations of law*."

[25] *Great Elephant Corp v Trafigura Beheer BV* [2013] EWCA Civ 905; [2013] All E.R. (Comm) 992.

[26] *Chitty on Contracts*, 32 ed., ¶ 15-152.

[27] Frustration may still apply even where there is a *force majeure* clause, depending upon whether the *force majeure* clause covers fully and completely what would otherwise be a frustrating event: Lewison, K., *The Interpretation of Contracts*, 6 ed., ¶ 13.11. The law in this area is complex and is outside the scope of this memorandum: See the decision of the Court of Appeal in *Edwinton Commercial Corp v Tsavliris Russ (Worldwide Salvage & Towage) Ltd* [2007] 2 Lloyd's Rep. 517.

[28] *Lauritzen AS v Wijsmuller BV (The Super Servant Two*) [1990] 1 Lloyd's Rep. 1., *per* Bingham L.J.

[29] *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675, 700 *per* Lord Simon.

one. The courts have held contracts to be frustrated because of changes in the law (including exercise of statutory power), supervening illegality, outbreak of war, cancellation of an expected event and abnormal delay outside what the parties could have reasonably contemplated at the time of contracting.[30]

It is therefore possible to envisage COVID-19 and consequent governmental actions as potentially falling within one or more of these categories. In particular, where time is of the essence to the performance of the contract, the temporary unavailability of stocks or staff may arguably give rise to a frustrating event. Similarly, governmental restrictions in response to COVID-19 may render the performance of certain obligations illegal. This may potentially give rise to a claim of supervening illegality.

One thing is clear: English law does not recognise frustration based on so-called economic impracticality based on increased costs or general economic conditions that may be caused by COVID-19.[31]

Even if the impact of COVID-19 (and more particularly, governmental actions in response) may constitute a potentially frustrating event, this alone is insufficient. Much depends upon whether the risk of the event occurring was foreseen, yet not provided for in the allocation of risk in the contract, or whether it was foreseeable but not foreseen.[32] There are also complex statutory provisions addressing unjust enrichment as a result of a frustrated contract, including the recovery of advance payments.[33] These issues are not addressed in this memorandum, which focuses on whether COVID-19 might give rise to a declaration of *force majeure*.

Conclusion

In conclusion, COVID-19 has created significant economic and legal uncertainty. It is essential that businesses review their key contracts and identify risks of a counterparty seeking to rely on a *force majeure* clause or the doctrine of frustration. Equally, parties should consider whether the current circumstances truly do give rise to a *force majeure* event which could be used in discussions to achieve a commercial outcome.

It is, however, vital to note that the risks of wrongly declaring *force majeure* are high. If a party declares *force majeure* but is not, in fact, entitled to do so, this is likely to expose it to a claim for damages and for repudiatory breach of contract.

Sophisticated commercial clients in many industries are reluctant to declare *force majeure* for good reason. Nonetheless, given the dynamic nature of responses to the COVID-19 pandemic, it is inevitable that there will be an increase in declarations, and businesses should review key contracts now to seek to minimise that risk.

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30 *Chitty on Contracts*, 32 ed., ¶ 23-020 - 23-036.

31 *Tennants (Lancashire) Ltd v CS Wilson & Co* [1917] AC 495.

32 G.H. Treitel, *Frustration and Force Majeure*, 4 ed., Ch 13 generally.

33 Law Reform (Frustrated Contracts) Act 1943; see *B.P. Exploration Co (Libya) v Hunt (No. 2)* [1979] 1 WLR 783.

We continue to monitor the ongoing developments in response to the COVID-19 pandemic. If you have any specific questions, please reach out to your usual Fried Frank contact or the Coronavirus Task Force (CoronavirusTaskForce@friedfrank.com).

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its contents. If you have any questions about the contents of this memorandum, please call your regular Fried Frank contact or an attorney listed below:

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