



Business Contracts

The impact of Coronavirus

Aisha Dickson, Consultant to our Corporate and Commercial department, has been advising on the impact of the Covid-19 virus on commercial contracts since the virus began its silent attack in late January. Here, she sets out the key Q&As encountered:

What happens if I can't perform my contractual obligations?

The general rule under contract law is that if you fail to perform your contractual obligations, you will be in breach of contract. This means that you are potentially liable to the other party for damages, and the other party might also have a right to terminate.

Surely I can rely on "force majeure" to get out of having to perform my obligations?

This is a common assumption to make, but unfortunately, it's not always correct.

The first step to take is to look at your contract to see what it says. There could be a clause headed "force majeure" or there may be an unlabelled clause which provides what is to happen if specific events or types of events occur. If there's nothing in the contract which deals with "force majeure", then you need to consider the position outside of contract.

My contract includes a force majeure clause. Is Covid-19 a force majeure event?

The term "force majeure" has no definition in law. It is simply used as a label to refer to events which might excuse one party from performing their contractual obligations where that performance is significantly affected by events outside of their control.

So whether Covid-19 is a force majeure event depends entirely on the drafting of the force majeure provision. Many force majeure clauses include a list of specific events which the parties have agreed will amount to force majeure, and this might include express reference to "pandemic" or "epidemic". If it doesn't, there might be some "catch all" wording referring for example, to "events of a similar nature to those listed".

Whether Covid-19 will be of a similar nature to those listed will be a question of fact based on the surrounding wording of the contract. For example, if the surrounding wording refers to "fires and floods" then Covid-19 is not similar; if it refers to "pandemics" but you sought to rely on force majeure before Covid-19 was declared a pandemic, then Covid-19 is similar, and more likely to fall within the definition.

What about the lockdown imposed by the Government?

Again, this will depend on what the contract says.

It is quite common for force majeure clauses to refer expressly to “any action taken by a government” or similar wording. Travel restrictions or a lockdown such as the one currently imposed, if they prevent or restrict your performance, are likely to fall into this category of force majeure event.

In addition, if your performance of your contractual obligations result in an outcome which goes against these government imposed restrictions, you might be able to rely on “illegality” to excuse non-performance (although the bar is set high to prove that performance of a contract is illegal).

My contract refers specifically to a pandemic as a force majeure event. Does this mean force majeure automatically applies?

Not necessarily. Force majeure clauses are construed restrictively, and as the party seeking to rely on the clause, you will bear the burden of proof to demonstrate the scope of the clause and that the facts in question fall within that scope.

You should check the provisions of your force majeure clause as there is likely to be a number of conditions that you must fulfil before you can rely on force majeure to alleviate your liability.

Common conditions include requirements to notify the other party of the occurrence of the event and its impact (time limits are often imposed), an obligation to show that the event has actually prevented, delayed or hindered your performance, and also an obligation to take steps to mitigate (or reduce) the effects the event is having. If the obligation to mitigate is not express, it will usually be implied.

I can rely on force majeure – what happens to the contract and what will my liability be?

If you are able to trigger force majeure, its precise operation will again depend on how the clause is drafted. Typically however, it operates to allow one or both parties to be “excused” from performance, or to “suspend” performance of some or all of their obligations.

Whether you can exclude all of your liability under the clause (including, for example, retaining fees received for services which you will not now render) will involve close scrutiny of its wording. A force majeure clause is effectively an exclusion clause and in most cases, subject to a test of reasonableness. If it is drafted too heavily in your favour, it could (if challenged) be held invalid.

I could still perform the contract, it will just be more difficult, and I just don't think it's profitable enough...

Unfortunately, changes in economic or market conditions which affect the profitability of your contract or the ease with which you can perform it, are not relevant, and do not themselves constitute force majeure events.

Your performance needs to have been prevented, delayed or hindered (depending on the wording of the clause) by the force majeure event, so for example, if the cost of performance has increased because you have to pay your staff more, but you are otherwise able to perform, then you cannot rely on force majeure.

It is worthwhile however checking the other provisions of your contract to see if, for example, you have a general right of termination.

I've looked at my contract but there's no force majeure provision. What shall I do?

You might be able to rely on “frustration”, which is a doctrine which applies outside of contract law. It can apply if, as a result of Covid-19, contractual performance has become legally or physically impossible through no fault of the parties.

A frustrated contract ends automatically and immediately, without any action by the parties (who then only have limited rights of redress). During World War II, many contracts were frustrated when it became legally impossible to trade with the enemy. It is unusual now to see a contract frustrated and the bar for this applying is very high.

Am I covered by insurance?

It is sensible to check what insurance policies you have in place and have early conversations with your insurers or brokers.

You may have policies that potentially cover losses suffered as a result of Covid-19, but as with all other contracts, the question of whether cover will be provided will depend on the particular policy wording and any specified exclusions. It is advisable to check the notification requirements in your policy as these might include notification of potential claims within a specified time.

Make sure you keep records of events occurring and conversations you have with your insurers and follow these up in writing.

We're all in the same boat. What can I do practically that will help?

The situation is unprecedented and rapidly changing, and there will no doubt be a wave of disputes which arise as a result of this pandemic as to which party bears the risks of non-performance.

The optimum solution, to the extent possible, may well be for you to seek to keep your contracts on track and avoid bringing potentially expensive claims against each other. Speak with your counterparties and discuss any exit plan.

If you do agree to vary or renegotiate the terms of your contract, then you should ensure that you comply with any relevant contractual requirements such as recording the variation in writing.

Don't rush into the situation and consider carefully whether changing one aspect of your arrangement has a knock-on effect on other provisions or future contracts, and whether there are any other long term impacts.

This has been a learning curve. What shall I think about for new contracts?

Unfortunately, it doesn't look like Covid-19 will be retreating any time soon, or that it will be the last pandemic we experience in our lifetimes.

Going forward, you should think about how to precisely define a force majeure event, based on your commercial experiences and case-law, the consequences arising, and how to allocate the risks that result. It's time to pay attention to clauses which have previously had a tendency to be overlooked.

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