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(Judicial Precedents on Pandemics and Force Majeure)

Judicial Precedents on Pandemics and Force Majeure: the common law perspectiveDato' Andri A Badri

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1) Background

It is undoubted that the circumstances that had been brought about by COVID-19 (1) is unprecedented in terms of its global scale of the pandemic as well as the governmental actions being involved to mitigate the spread of the virus. The steps taken to mitigate are taken by governments as it involves the safety and well being of its people as well as to those of others countries as well. This include the restriction of movement of people both travelling within the country as well as international travel. As a consequence, the provision of many goods and services had been and continues to be impeded to the extent that many contractual obligations are unable to be satisfied. The discussion in this paper is concentrated on the legal effect on obligations of parties to a contract in relation to the pandemic of COVID-19 as a force majeure from the perspective of common law.

2) Common law (2) position on Force Majeure

Force majeure under the common law is not recognised as a principle on its own to have effect on contractual relationships unless it is stipulated as a term of contract. As such contracts that are contemplated to be affected by events beyond the control of the contracting parties will typically include a force majeure clause. As it is a clause to be agreed between the parties, there is no standard force majeure clause and indeed the term “force

(1) Corona Virus Disease 2019

Common law for the purposes of this paper refers to the common law as applied in England and to countries that had accepted the same as part of the national law, for example Malaysia subject to postulations as provided in statutes.

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majeure" does not have any fixed meaning in common law as it is a term to be construed from the clause it is used [3]

(a) Is the COVID19 pandemic a force majeure event?

As force majeure is contractual, the question as to whether the COVID-19 pandemic is an event that triggers a force majeure type clause is a question of construct of the terms agreed by the parties. Such clause may have used the term force majeure itself but has defined it to only specified types of events and some contracts may not even define the term. There are contracts that do not use the term force majeure, but instead the term "exceptional events" is used. Where disputed the courts will determine the definition and the judicial method is one of construing the specific clauses where it appears [4].

Where it is expressly provided as a clause in a contract, the interpretation on the applicability of a force majeure clause will first involve the question of ascertaining as to whether COVID-19 falls as one of the agreed circumstances to trigger the force majeure clause.

We shall look at some contractual precedents to examine the operation of such force majeure clauses. An example of force majeure clause that may be found in a sukuk programme agreement (*illus. 1*):

illus. 1.

"If prior to the issuance of the Sukuk in the opinion of the Joint Lead Arrangers there has been such a change in national or international monetary, financial, political or economic conditions or currency exchange rates or exchange controls has an adverse effect on the marketability of the sukuk upon issuance, it is hereby agreed that the parties will enter

(3) Lebeaupin v Crispin [1920] 2 KB 714, Ambatielos v Anton Jurgens Margarine Works [1923] AC 175

(4) Matsoukis v Priestman Co [1915] 1 KB 681

into discussions with a view to arriving at a mutually acceptable solution. Pending such a mutually acceptable solution being agreed, no issuance of Sukuk shall take place."

For circumstances that arises from COVID-19, such a force majeure clause will have to be examined if it is within the ambit of the circumstances coming under the clause. Where the force majeure clause include expressly the term "pandemic" or similar wordings as one of the circumstances, the application of such force majeure clause is less arguable. In particular with the fact that World Health Organisation (5) has classified COVID-19 as such and the recognition of COVID-19 as a pandemic in many countries is very persuasive that COVID-19 does come into the category of a pandemic in a contractual stipulation.

In relation to a force majeure clause that does not expressly stipulate pandemic or infectious diseases as one of the expressly recognised circumstances, a pandemic such as COVID-19 will have to be interpreted as being part of the other circumstances or events having the effects as expressly provided in the force majeure clause, failing which it is arguable that such a force majeure clause will not apply. In the force majeure clause as set out in *illus. 1* above, since no express mention of pandemic is made, the interpretation of the effects of COVID-19 will then have to be such that arising from COVID-19 there is a change in the national or international monetary, financial, political or economic conditions or currency exchange rates or exchange controls that has resulted in an adverse effect on the marketability of the sukuk.

It is noted that many typical financing contracts as between a financier and a customer do not contain a force majeure event. The interpretation

(5) https://www.who.int/dg/speeches/detail/who-director-general-s-opening-remarks-at-the-media-briefing-on-covid-19---11-march-2020

of such absence can be construed as an intentional acceptance of risk on the respective party's obligations under the contract, whereby the obligations are intended to be unchanged in the event of a force majeure, in particular the obligation to pay the debt of a financing. The seemingly unfair position has led for the national authorities to intercede for example in Malaysia where a 6 months' moratorium on payment of financing is directed by the central bank of Malaysia (6) to be given by the financiers as a result of the COVID-19 pandemic. Short of such intercession by authorities or by law, where the financing contract does not cater for force majeure then there is none that may be implied and parties are very much left with what is agreed within the four corners of the contract.

However, in the more sophisticated financing transactions, for example such as those involving swaps and derivatives, contractual provisions are found to cater for force majeure. In the ISDA/IIFM Tahawwut Master Agreement ("TMA") which is based on the ISDA 2002 Master Agreement, force majeure is an event that is recognised that entitles the affected transactions to be terminated. It is to be noted however the term "force majeure" itself is not defined in the TMA and the meaning will therefore have to be construed on the actual circumstances in which it is to be used. In the TMA the effect of the force majeure event is emphasised whereby the relevant clause qualifies that such an event must be paramount in creating the prevention, impossibility or impracticability to perform. This qualifier is stated at the end of Clause 5(b)(ii) of the TMA (*illus. 2*):

illus. 2

"..so long as the force majeure or act of state is beyond the control of such Office, such party or such Credit Support Provider, as appropriate, and such Office, party or Credit

(6) https://www.bnm.gov.my/index.php?ch=en_press&pg=en_press&ac=5018&lang=en

Support Provider could not, after using all reasonable efforts (which will not require such party or Credit Support Provider to incur a loss, other than immaterial, incidental expenses), overcome such prevention, impossibility or impracticability; "

Likewise, as may be found in standard forms of construction contracts, events that are beyond the control of the parties are typically included. For example under FIDIC version as revised in 2017 ("FIDIC Template") the term "force majeure" was previously used. This term is now called "Exceptional Event" and is defined as (*illus. 3)*:

illus. 3

".. an exceptional event or circumstance:

(a) which is beyond a Party's control;

(b) which such Party could not reasonably have provided against before entering into the Contract;

(c) which, having arisen, such Party could not reasonably have avoided or overcome, and

(d) which is not substantially attributable to the other Party."

Instead of providing an exhaustive list of what can constitute a force majeure or "Exceptional Event", the FIDIC Template lists the following as being recognised (*illus. 4*):

illus. 4

"(i) war, hostilities (whether war be declared or not), invasion, act of foreign enemies,

(ii) rebellion, terrorism, revolution, insurrection, military or usurped power, or civil war,

(iii) riot, commotion, disorder, strike or lockout by persons other than the Contractor's Personnel and other employees of the Contractor and Subcontractors,

(iv) munitions of war, explosive materials, ionising radiation or contamination by radio-activity, except as may be attributable to the Contractor's use of such munitions, explosives, radiation or radio-activity, and

(v) natural catastrophes such as earthquake, hurricane, typhoon or volcanic activity."

It can be seen that COVID-19 or "pandemic" does not on its own come under an express classification of the circumstances as set out in *illus. 4* above. However, as the list as set out in *illus. 4* above is intended as a non-exhaustive list, COVID-19 may still be applicable subject to the qualifier tests as set out in *illus. 3* above are satisfied.

In essence, the typical qualifier for a force majeure clause is that it has to be exceptional and that the exceptional circumstances had made the contracted performance impossible. Where the contractual terms do not provide an express interpretation as to the meaning, the English cases have interpreted "force majeure" to include circumstances that can be attributed to those beyond control of man[7]and the event must be a physical or legal bar and not merely an economic event [8]. Such interpretation in the author's view will include pandemics such as COVID-19.

Although COVID-19 may qualify as a type of force majeure event contemplated to be covered by a force majeure clause, it must be proven that COVID-19 is the cause for the impossibility of performance. This factual causation is a prerequisite to the operation of a force majeure clause. In a case [9]where charterers that had entered into a long term

(7) See note ii above at 719.

(8) Yrazu v Astral Shipping Company (1904) 20 TLR 153, 155.

(9) Classic Maritime Inc v Limbungan Makmur Sdn Bhd [2019] EWCA Civ 1102

contract with the ship owner for the transportation of iron ore from Brazil to Malaysia, the charterer had sought to rely on an event of a burst dam as a force majeure event that prevented it from the shipment of the ore. They failed in being able to rely on force majeure as the court held that the charterers would not have been able to perform their obligations anyway even if the dam had not burst and as such the failure to perform was not caused by the force majeure event.

(b) The effect of a Force Majeure clause

Being a contractual term, the parties are free to agree on the effect of a force majeure event in so far as the allocation of risks are concerned. Where it has been established that a force majeure clause in a contract exists and is applicable, the effect of the clause is one of interpretation as to what is expressly provided for.

In general, the allocation of risks in a force majeure type clause include:

(i) the right to have a suspension of the obligations of all parties;

(ii) the right to have an extension of time to perform the obligation contracted without penalty;

(iii) the right to terminate the contract.

As may be seen in the wordings set out in *illus. 1* in a contract for the arrangement of a sukuk issuance, the parties had agreed to a specific course of action in that the obligation to arrange for the issuance of sukuk is suspended. It did not provide for a termination of the agreement and thus the clause cannot be used to justify a termination.

In relation to construction where the standard form of FIDIC Template is used, the effect of force majeure can result in either an extension of time provided or a termination depending on the agreed effect that the force majeure clause will have under the terms of the contract. For example in

relation to a contractor, the occurrence of a recognised force majeure event will entitle the contractor to an extension of time to complete the work and also to costs if it falls within the named type of force majeure in the country the project is executed.

Clause 19.4 of the FIDIC Template provides (*illus. 5*):

illus.5

"If the Contractor is prevented from performing any of his obligations under the Contract by Force Majeure of which notice has been given under Sub-clause 19.2, and suffers delay and/or incurs Cost by reason of such Force Majeure, the Contractor shall be entitled subject to Sub-clause 20.1 to:

(a) an extension of time for any such delay, if completion is or will be delayed, under Sub-clause 8.4, and

(b) *if the event or circumstance is of the kind described in sub-paragraphs (i) to (iv) of Sub-clause 19.1 and, in the case of subparagraphs (ii) to (iv), occurs in the Country, payment of any such Cost…."*

It is to be noted that COVID-19 or "pandemic" is not a type of force majeure event that is listed specifically and as such although the contractor may be entitled to an extension of time he may not be entitled to claim for costs as the clause expressly stipulate that only if the force majeure event is of the types expressly listed can the contractor be entitled to costs.

Force majeure clauses may also give rise to a right to terminate the contract. For example, in the FIDIC Template either the contractor or the employer may terminate the contract if the execution of substantially all the agreed works in progress is prevented for a continuous period of 84

days or 140 days in total by reason of Force Majeure of which notice has been given [10] . In such event the period which is provided for is one that the parties have agreed at the beginning of the contract. The consequence of such termination is also dealt with in the contract including the agreed method of payment and as to how such computation is determined. In the context of the COVID-19 especially where lock-downs have been enforced the 84 days continuous period that gives rise to a right to terminate may be a likely possible scenario.

(c) Where a specific force majeure clause is absent

Where a specific force majeure clause is absent and the performance of the parties are affected, the principle of *frustration* under the common law may be applicable. As was held by Lord Radcliffe in his judgment [11] (*illus. 6*):

illus.6

"..that frustration occurs whenever the law recognises that, without the default of either party, a contractual obligation has become incapable of being performed because the circumstance in which performance is called for would render it a thing radically different from that which was undertaken by the contract. Non haec in foedera veni. It was not this that I promised to do."

The common law position sets out three main elements that need to be considered in construing as to whether an event of frustration applies to a contract:

(i) performance becomes impossible;

(ii) performance becomes illegal [12];

(10) See Clause 19.6 of the FIDIC Template.

(11) Davis Contractors Ltd v Fareham Urban District Council [1956] AC 696, 728-9

(12) Denny, Mott & Dickson Ltd v James B Fraser & Co Ltd [1944] AC 265

(iii) it is radically different from what the parties originally contemplate that the carrying out the obligation will be unjust.

The courts have construed the doctrine strictly and the findings very much revolve around the specific circumstances of the case. In the current circumstances of COVID-19, the onus is to prove that the effect arising from COVID-19 has satisfied the conditions for a frustration to apply to a contract. A hypothetical example may be that a delivery of a particular goods is to be made on a date where a lockdown has been imposed by law. The lockdown was not one that was contemplated by the parties when the contract was entered into and making the delivery will be illegal. Such a contract qualifies as one that is frustrated.

The fact that a contract becomes more difficult or more expensive to perform does not qualify a contract to be frustrated (13). The frustration event must be one that is significant enough. The District Court in Hong Kong (14)for example had held that an isolation order imposed for 10 days during the SARS outbreak in 2002-2003 did not constitute a frustration event after taking into account the 10 days duration was not significant enough in the context of a 2 years tenancy. The English case of *Canary Wharf (BP4) T1 Ltd v European Medicines Agency (EMA)* (15) *exemplified the high degree of threshold to be met in considering as to whether a contract is radically different from that originally contemplated.* In this case the tenancy of an office by EMA being an EU body is able to rely on frustration to terminate the tenancy of its headquarters office in London

(13) See note vii above; Tsakiroglou & Co Ltd v Noblee Thorl GmbH [1962] AC 93

(14) Li Ching Wing v Xuan Yi Xiong [2004] 1 HKLRD 754

(15) [2019] EWHC 335

for it to be relocated within the EU in view of BREXIT. The Court decided BREXIT is not a frustration event in the context of an office lease by EMA.

It is to be noted however that the effect of a frustrated contract is that the parties are released As such for example, from all their obligations under the contract. It does not render the contract void from the beginning. It releases future obligations.

As a principle that rests very much on the facts of each particular case, it is possible that contractual terms may deny the application of the frustration principle (16). In other words, parties may stipulate a clause that regardless of any event, the obligations still survive. Even the existence of a clause that caters for exceptional circumstances such as a force majeure clause or an exceptions clause had been taken by the courts as to the non-applicability of the principle of frustration to the contract(17)

Conclusion

COVID-19 is certainly an unexpected event in any measure of the term. Common law however has its limitations to deal on the various scenarios to which contractual recourse can be sought by parties to a contract. Even then, force majeure type of clauses only appears in certain types of contracts. Where force majeure event is not made as an express contractual term the parties are left with the obligations to be fulfilled to the strict letter of the contract, unless the principle of frustration applies.

(16) Jacobs v. Credit Lyonnaise (1884) 12 Q.B.D. 589 (C.A.).

(17) Jackson v The Union Marine Insurance Co Ltd (1874) LR 10 CP 125

Even then, the principle of frustration in most if not all cases will not be applicable due to the high threshold required to be satisfied apart from the fact that even if the event may qualify as frustration, the resulting consequence of termination may not be the outcome the parties may want.

A glaring example of a type of contract that can do with a force majeure type of clause is the financing contract. The allocation of risk to be shouldered wholly by the customer may appear inequitable in a force majeure event such as a pandemic like COVID-19. Financing contracts if not mitigated with goodwill on the part of the financier, can turn unduly onerous as a result of the effect. Under the financing contract the Customer has no express right to a deferment of payment or even an agreed avenue to discuss if as a result of a lockdown he is unable to meet scheduled payment arising from the temporary inability to conduct business. This is notwithstanding the reason of lockdown is undisputed and no party to the financing contract is at fault. But if nothing is provided in the contract to cater for an event such as the COVID-19, a breach of the contract appears inevitable.

With the new normal perhaps it is time all contracts be considered to provide expressly for unexpected eventualities such as for pandemics as much as possible to permit a more equitable possibility between the parties including an agreed framework for parties to be able to consult on payment schedules and temporary suspension of obligations.