



## **FRUSTRATED? IF YOUR FORCE MAJEURE CLAUSE DOES NOT COVER COVID-19 ISSUES – CONSIDER THE ENGLISH LAW DOCTRINE OF FRUSTRATION**

**During these unprecedented times we are receiving numerous queries from clients as to whether the force majeure (FM) clauses in their contracts will protect them from any issues caused by delays and/or defaults arising from COVID-19.**

Many of the FM clauses we see, particularly in commodities contracts, are well drafted and will cover COVID-19 events under the “epidemics” and/or “pandemics” wording in the list of potential FM events. Some even provide for “quarantine restrictions” as a FM event. Clients may also be able to rely on widely drafted FM clauses that just provide for events “beyond the parties’ reasonable control”.

However, we are also asked to advise upon FM clauses which are not as sophisticated and contain narrow lists of what might constitute a FM event. In these instances, it is unlikely that any issues arising from COVID-19 would be covered.

To overcome this issue, one possible option open to parties may be to rely on the English law doctrine of frustration.

### What is Frustration?

The English law doctrine of frustration provides a remedy for a party to be excused from all future contractual obligations where the following applies (this is an objective test<sup>1</sup>):

1. an event has occurred which was not considered by the parties when they decided to enter into the contract;
2. that event is important enough to be considered as affecting an obligation which is at the heart of the contract;
3. it has become illegal or impossible for the parties to perform that obligation (or if the parties were to perform it then it would be profoundly different from what was contracted for); and
4. the inability to perform the obligation is through no fault of either of the parties.

### Any Restrictions to Claiming Frustration?

#### Contractual obligation must be more than merely difficult to perform

Frustration cannot be claimed merely because the contract has become more difficult, more onerous to perform, or in circumstances where the contract has become economically unviable. In one claim, a shipper attempted to claim that the contract was frustrated in respect of a consignment to be shipped from Sudan to Hamburg on the grounds

that the Suez Canal was closed. The court rejected this argument, as an alternative route via the Cape of Good Hope was possible even though that would incur significant delay and additional cost<sup>2</sup>.

The key factor is whether it is *possible* for the contract to be performed. This is a question which will ultimately turn on the specific construction of the contract and the facts. Where a contract specifies that a party is obliged to load certain goods but does not specify the load port, a claim that the contract has been frustrated will be more difficult if an alternative port is workable, no matter if loading from that alternative port becomes more expensive<sup>3</sup>. If, however, the contract specifies a specific load port and it has become impossible to load because of COVID-19 related restrictions (e.g. port closure or government restrictions), then a claim of frustration will have more probability of succeeding<sup>4</sup>.

It is important to note that whether a contract can be performed is a question that will be considered on a contract by contract basis. That is to say, a contract cannot be said to be frustrated because performance under another contract in the chain would render performance more difficult, e.g. a third party supplier has failed to supply the goods in question.

#### Foreseeability of the event leading to frustration

A party will be unlikely to successfully claim that a contract was frustrated where it was aware of that frustrating event at the time the contract was made<sup>5</sup>, even where it did not make any provision for that event in its contract. So if parties enter into a contract when the issues arising from COVID-19 were known, they are unlikely to be able to claim frustration.

However, if the contract was entered into at a time when COVID-19 was merely foreseeable (and not actually

foreseen), then a claim of frustration is less likely to be rejected by the courts.

The courts have set a relatively high benchmark in regard to foreseeability, and so unless the contract was entered at a time when the scale and impact of the present outbreak was fully appreciated, it is unlikely the courts would prima facie exclude a claim of frustration.

#### Alternative contractual remedies

A party cannot claim frustration where a remedy or provision already exists in a contract which caters for the circumstances which have arisen<sup>6</sup>. Therefore, if there are clauses in the contract which potentially cover issues arising from COVID-19, e.g.:

- material adverse change clause;
- price adjustment/hardship clause; or
- change of law clause;

it is likely to lead to the conclusion that the parties have already provided a relevant remedy for any COVID-19 related impact upon their obligations (albeit ones which may not have been foreseen or foreseeable), irrespective of whether such a claim is successful. Any potential frustration claim is therefore likely to be negated by these clauses. However, the courts will construe such clauses narrowly and insist that the provision for the event be “full and complete”<sup>7</sup> before the conclusion is reached that frustration is excluded. The more catastrophic the event (and COVID-19 is undoubtedly a catastrophic event), the less likely it is that a clause will be held to cover the event which has occurred, unless particularly clear words are used.<sup>8</sup>

#### Self-induced frustration

Relief from contractual obligations by way of frustration will not be available where a party is at fault or has, in some way contributed to the circumstances leading to the

1 *Davis Contractors Ltd v Fareham U.D.C.* [1956] A.C. 696

2 *Tsakiroglou v Noble Thorl* [1962] A.C. 93

3 *The Furness Bridge* [1977] 2 Lloyd's Rep. 367.

4 *Re Badische Co Ltd* [1921] 2 Ch.331

5 *Tamplin S.S. Co Ltd v Anglo Mexican Petroleum Products Co* [1916] 2 A.C. 397, 426

6 *Jackson v Union Marine Insurance Co Ltd* [1874-75] L.R. 10 C.P. 125

7 *Bank Line Ltd v Arthur Capel & Co* [1919] A.C. 435, 455;

8 *Metropolitan Water Board v Dick Kerr & Co Ltd* [1918] A.C. 119

contractual failure<sup>9</sup>. The courts have not provided a definitive test to establish when such an exclusion would apply, but a party failing to take adequate precautions and follow government advice in relation to a COVID-19 outbreak could fall within this exception.

### Effect of Claiming Frustration

A successful claim of frustration differs from one of FM in that the contract will be automatically discharged and the parties excused from any future obligations. However, any obligations incurred prior to the discharge of the contract will survive.

Whether a party can recover payments made prior to the frustrating event will depend on whether the contract is subject to the Law Reform (Frustrated Contracts) Act 1943 (**LRA**). If the contract is one to which the LRA does not apply, then the parties must rely on the common law rules, which provide that any money paid will only be recoverable where there has been a total failure of consideration. If the failure is only partial, then no recovery will be possible<sup>10</sup>.

If the LRA does apply (it applies to many commercial contracts with the exception of certain shipping/insurance/and contracts for specific goods that have perished), it provides that:

- Money paid before the frustrating event can be recovered and that money due before the frustrating event, but not in fact paid, ceases to be payable.
- A party who has incurred expenses is permitted to retain an amount out of any money they have been paid by the other party before frustration (up to the value of the expenses paid).
- The court may require a party who has gained a valuable benefit under the contract before the frustrating event occurred to pay a “just” sum for it.

### Summary

Frustration may be able to assist parties whose contracts have been affected by COVID-19 but who are not protected by a properly drafted FM clause.

However, if a party wishes to claim under the doctrine of frustration for any contract affected by COVID-19 it must prove that the frustrating event has made performance impossible – not merely difficult.

### Take Action

If neither FM nor frustration is available, parties should consider mediation/ADR to try and resolve any potential disputes. Alternatively, parties may wish to review any insurance policies they have in place, which may assist. Here is a link to an article from HFW's Insurance team on Business Interruption claims:

<https://www.hfw.com/COVID-19-Briefing-on-Business-Interruption-issues>

The current situation with COVID-19 is fast moving and the global business world is changing day by day. We recommend clients take action promptly, whether declaring FM, claiming frustration or seeking advice.

For further information, please contact the authors of this briefing:



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<sup>9</sup> *J. Lauritzen A.S. v Wijsmuller B.V. (The Super Servant Two)* [1990] 1 Lloyd's Rep. 1, 8

<sup>10</sup> *Chandler v Webster* [1904] 1 K.B. 493

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