Article Information

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Service: Corporate & Commercial, Projects & Construction
Sector: Infrastructure

COVID-19 pandemic, force majeure and contract relief: a guide

On 11 March 2019, the World Health Organisation (WHO) declared COVID-19 a global pandemic. The WHO Director-General called on countries to "activate and scale up emergency response mechanisms". Worldwide, government actions to limit contagion have escalated dramatically, and include lockdowns, travel restrictions, employee isolation and transport closures. Following our recent discussion on legal responses to supply chain disruption we discuss the broader issues as they affect contract obligations.

Despite the emerging consensus that steps must be taken to curtail the spread of COVID-19, the response is by no means global and there is much to indicate that in the developed world, the worst is yet to come. Preventative measures implemented by countries (and businesses) differ wildly. China and Italy, have gone into lockdown, implementing significant travel and other restrictions. On 12 March 2020, the US announced a 30 day travel ban to Europe.[1] Some countries have enforced school and university closures.

Australia has imposed restrictions on travel from mainland China, Iran, South Korea and Italy. Numerous businesses and schools have been closed. Working from home is expected to be widely implemented and the Victorian government is contemplating enforce a state of emergency.[2]

Each action of local, state, national and overseas governments is capable of triggering "change in law" provisions in commercial contracts, however, whether relief applies will require careful consideration of the terms agreed. Government actions on their own are unlikely to affect the rights and obligations of the parties to a contract. The effects that such actions have will depend on what the parties have agreed and how that agreement is expressed.

FORCE MAJEURE ENLIVENED?

Our previous article discussed force majeure provisions in detail.

The WHO's recent declaration of a pandemic will enliven many force majeure provisions which reference such declaration as the trigger to a force majeure event. Notwithstanding that such triggering may have occurred, it is also important to consider other limiting language in a clause. For example, many construction contracts contain terms which confine the meaning of a force majeure event to things which affect the ability of a party to access the site site. In such circumstances, a declared pandemic may seriously delay or prevent the shipment of goods without triggering any contractual relief merely because access to site remains unaffected.

The effect of such limiting language denying relief will no doubt provide cause for parties to more closely consider force majeure clauses next time a contract is signed.

CHANGES IN LAW

"Change in law" clauses are also common. Typically, they contemplate situations where an unforeseen legal requirement affects the ability of a party to do what it has contracted to do. A change in law provision will provide relief for such a change, including such things as suspension rights, extensions of time or recovery of additional costs.

Again, the breadth of events triggering relief and the extent of relief available will depend on the wording of the clause. Depending on how broadly it is drafted, change in law provisions may not be limited to a change in Local, State or Commonwealth law. In rare cases, it may apply to a change in overseas law. A declared state of emergency, where

governments impose restrictions on the public,[3] will more commonly attract change in law relief.

Clauses will commonly seek to narrow the scope of relief to exclude certain changes in law (e.g. changes to the interpretation of an Act or laws enacted by foreign countries), or limit their effects in terms of location or parties (leaving effects on the broader supply chain outside of those things capable of attracting relief). If a change in law clause does not capture changes in law which apply to contractors or suppliers (as opposed to the parties to the contract), the contracted parties may still be left exposed, despite the fact of changes in law affecting performance in their supply chain.

DOCTRINE OF FRUSTRATION

Unlike force majeure (or change in law clauses), the doctrine of frustration will apply regardless of whether or not the contract expressly provides for its application.

A contract may become 'frustrated' when an event outside the control of the parties makes a contractual obligation *"incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract."*[4]

Determining whether a contract has been frustrated requires consideration of both the contract and the "frustrating" event (in terms of the effect it has on contract performance). An event merely making performance more difficult or costly will not render the contract frustrated.[5] Similarly, minor temporary concerns are also unlikely to frustrate.[6] Consideration of whether this doctrine applies requires assessment of the magnitude of the impact on the party's ability to meet its contractual obligations. Different contracts will be frustrated by different events and each event and contract must be assessed on an individual basis.

If a party believes a contract has become frustrated due to excessive delay or potential future excessive delay, it is relevant to take into account both the probable length of delay and the estimated time remaining on the contract (prior to it being completed) in order to determine whether or not the delay has frustrated the contract.[7]

Parties are not required to wait for an effect to happen but, as may be the case with COVID-19, they may rely on the fair assumption that a particular event will give rise to a particular impact on the performance of their obligations.[8] The determination of the length and effect of the delay is to be made at the time of the interruption, without the benefit of hindsight.[9]

MANAGING CONTRACTUAL IMPACTS OF COVID-19

Managing these issues requires consideration of the following:

1. **Ability to comply with obligations**
   Consider how the pandemic may impact your obligations and those of downstream contractors and suppliers.
2. **Notice requirements**
   Where delay (or worse) is anticipated, consider contract notice obligations. Typically, construction contracts require notice as soon as a delay is anticipated as well as regular updates as to the impacts of the delay. Rights to relief may be "time-barred" where timely notice is not given.
3. **Early engagement and "stand-still" arrangements**
   Onerous contract administration requirements can get in the way of parties' abilities to manage crisis situations effectively. Where this is a problem, parties may consider entering formal "standstill" arrangements which suspend administrative obligations and risk in order to promote cooperation in solving problems rather than arguing as to whose risk they are.
4. **Available remedies and relief**
   Review your contracts to assess risks, reliefs and remedies in both up and downstream arrangements.

[1] Anne Barrowclough, The Australia, *Trump announces Europe Travel ban* (12 March 2020).

[2] ABC News, *Coronavirus case closes Melbourne school as Victoria activates State Control Centre to respond to COVID-19* (11 March 2020).

[3] See *Disaster Management Act 2003* (Qld) s 69; *State Emergency and Rescue Management Act 1989* (NSW) s 33; *Emergency Management Act 1968* (Vic) s 23; *Emergency Management Act 2004* (SA) s 24.

[4] *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.

[5] *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696.

[6] *FA Tamplin Steamship Co Ltd v Anglo-exican Petrleum Products & Co td* [1916] 2 NSWLR 540, 557.

[7] DW Greig and JLR Davis, *Law of Contract*, Law Book Co, Sydney, 1987, 1310 – 11.

[8] *Embiricos v Sydney Reid & Co* [1914] 3 KB 45.

[9] *Court Line v Dant & Russell* (1939) 64 LI LR 212.