

Contractual Issues During Covid-19 Force Majeure and Frustration

By David Nicholson

The COVID-19 global pandemic continues to significantly disrupt business operations around the world and is making some contractual obligations increasingly more difficult (and in many cases impossible) to perform by contracting parties. These circumstances have led to parties more readily invoking force majeure clauses in their contracts to avoid incurring liability for, and any additional costs associated with, the failure to perform their contractual obligations.

The application of a force majeure clause will depend on the particular terms in which it is drafted. The definition of a force majeure event will normally include an “act of God”.^[1] This article will consider whether the COVID-19 global pandemic is an “act of God” under Australian law for the purposes of force majeure clauses. The article will also consider the application of the common law doctrine of frustration, which may similarly have the effect of discharging the parties’ obligation to perform their contractual duties under a contract.

Force Majeure clauses and ‘Acts of God’

Force majeure clauses aim to protect contracting parties from liability for the non-performance of a contract because of circumstances not reasonably foreseeable and beyond the control of the affected party (*Ambatielos v Anton Jurgens Margarine Works* [1923] AC 1705, 182). In Australia, force majeure is not generally recognised as a common law doctrine but rather as a contractual concept, which means that it is open to contracting parties to agree (at their own discretion) on whether the occurrence of a particular event will excuse a party from an obligation to perform (*Hyundai Merchant Marine Co Ltd v Dartbrook Coal (Sales) Pty Ltd* (2006) 236 ALR 115, [61]). Whether a force majeure clause captures an event like the COVID-19 pandemic is largely a question of construction. Accordingly, local governments must closely examine the specific wording of a force majeure clause in their contract to determine whether it may shield them from implications arising from the COVID-19 pandemic.

If a force majeure clause does not expressly include terminology such as “infectious disease”, “epidemic” or “pandemic”, or alternatively, “government action” or “national emergency”, then it may not capture an event like COVID-19. In spite of this, most contracts also include an unqualified “act of God” clause, which is ordinarily designed to capture certain events that are not already specified in a force majeure definition.

Is COVID-19 an “Act of God”?

As force majeure is not a common law concept, there are very few cases (particularly in Australia) that have considered the meaning of “act of God”. Cases that have considered the meaning of the term appear primarily in 19th century English law, in the context of shipping law and negligence. Regardless, the English law offers some guidance as to what Australian courts might determine when faced with this or a similar issue in the future.

The prevailing case in English law is *Nugent v Smith* [1876] 1 CPD 423, where “act of God” is broadly defined (by James LJ) as follows:

1. be exclusively the consequences of natural causes;
2. be of an extraordinary nature;
3. it would not be anticipated or provided against by the party seeking to rely on it. [444]

Exclusively the consequences of natural causes

James LJ defined “natural cause” to mean “elementary forces of nature unconnected with the agency of man or other cause” ([444]). In English law, this has been interpreted to include storms, flooding, lightening and heavy snowfall (see, eg, *Briddon v Great Northern Rly Co* (1858) 28 LJ Ex 51; *Cushing v Peter Walker & Son Ltd* [1941] 2 All ER 693).

It could be argued that Covid-19 is not “exclusively the consequences of natural causes”, because it involves some form of human agency to the extent that the pandemic itself necessarily involves the spread of illness from person to person. Additionally, it could be argued that COVID-19 is not exclusively the consequences of natural causes because, although the disease itself may have derived from animals, the human pandemic (that is, the worldwide spread of the disease) is likely to be attributable to human acts in relation to the consumption of animals.

Nonetheless, if “human agency” is more narrowly defined as intentional action, this element is arguably lacking given that the pandemic is not the result of intentional human action. This interpretation is consistent with later English cases in support of the proposition that illness or disease may indeed constitute “acts of God”. In *Boast v Firth* [1868]-69] LR 4 CP 1 and *Hall v Wright* (1859) 120 ER 695, it was held that illnesses not the fault of the person in question (e.g. cancer, heart attack) may be considered acts of God in the context of negligence claims.

Of an extraordinary nature

James LJ defined “extraordinary nature” to mean “overwhelming” or “unprecedented” ([444]). Examples of “extraordinary” events in English law include “extraordinary” high tides, “extraordinary” flooding and snowfall and “unprecedented” rainfall (see, eg, *Nicholas v Marsland* [1976] 2 Ex D 1; *Briddon v Greater Northern Rly Co* [1858] 28 LJ Ex 51). There is little doubt that a pandemic of the scale and impact of COVID-19 would meet this requirement.

Not anticipated or provided against

James LJ defined this to mean that an event must be unable to be “prevented by any amount of foresight and pains and care reasonably to be expected by the party relying on it” ([444]). Again, given the degree to which the disease has impacted communities and economies around the world, it is relatively clear that it is not an event that could have been prevented by any amount of foresight and care reasonably to be expected.

COVID-19 likely to constitute “act of God”

On balance, whilst there is an absence of judicial authority specifically on point, it appears likely that the COVID-19 pandemic would constitute an “act of God” for the purposes of a force majeure clause as it is exclusively the consequences of natural causes, of an extraordinary nature and could not reasonably have been anticipated or provided against.

Additionally, some force majeure clauses may specifically include government directives or changes in law in the definition of a force majeure event, which may be another basis on which a force majeure clause may be invoked.

Frustration

If a contract does not include an operative force majeure clause, then an affected party may alternatively seek to invoke the common law doctrine of frustration, which will have the effect of discharging both parties from the obligation to perform their contractual duties. Frustration occurs whenever the law recognises that, without default of either party, a contractual obligation has become 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 (*Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696, 729).

While there is no strict rule as to what constitutes a frustrating event, frustration will generally occur in circumstances where it is impossible for a party to perform a contractual obligation like, for instance, where performance becomes unlawful by virtue of government action. In some contexts, it is possible that the COVID-19 pandemic could constitute a frustrating event. For example, frustration will likely be established where a catering company contracts with a concert promoter to provide food and drinks, but due to government restrictions on indoor public gatherings, the concert is cancelled and cannot take place. By contrast, in less serious circumstances, such as where a contracting party is forced to delay performance by two weeks by reason of a reduced work force, it is unlikely that frustration will be established.

It is important for local governments to note the following points before asserting frustration. Firstly, a contract will be not discharged for frustration if its terms provide for the occurrence of the event in question. Ordinarily, a contract will only be frustrated if, on a proper construction of the contract, it shows a presumed intention of the parties not be bound in the situation that has ensued (*British Movietonews Ltd v London and District Cinemas Ltd* [1952] AC 166). Secondly, once frustration is established, losses will lie where they fall, meaning that all expenses incurred by a party (such as expenses incurred in preparation for the performance of a contractual obligation prior to frustration) will not be recoverable.

Conclusion

If a contracting party's ability to perform its contractual duties is affected by the COVID-19 global pandemic, then that party should initially look to any specific force majeure provision in their contract to protect it from liability associated with non-performance. A force majeure provision may potentially apply either on the basis of an "act of God" or alternatively on the basis of government directive or a change in laws, depending upon the wording of the clause and the definition of a force majeure event.

Alternatively, a party may seek to invoke the common law doctrine of frustration, which will have the effect of discharging the parties' contractual obligations if their performance is frustrated. However, frustration will only ever be upheld in circumstances where it is impossible for a party to perform a contractual obligation, not where performance is merely delayed. It is also important to note that parties must be careful when invoking frustration, as the absolute termination of a contract may have serious repercussions for either contracting party.

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[1] Definition of a Force Majeure event may also include government directives or a change in law, which could also be relied upon in the current circumstances where the COVID-19 has led to a declared state of emergency and various government directives restricting business activities.