Covid-19 and its effect on contractual obligations

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The simple effect of the Covid-19 lockdown announced on 23 March 2020 was that life, and business, changed for everyone. People and organisations could no longer do things they had planned or intended to do, and in many instances, difficult decisions had to be made, and some were made hastily, without thinking through the ramifications. As time goes on, many will be faced with the question of whether steps they took, or didn't take, mean that they are in breach of a contractual obligation; on the other side of the coin, others will be wondering whether they have a remedy for not having received goods or services they expected to on time, or at all.

Where there is a written agreement, the starting point will of course be the provisions set out there, including whether there is a force majeure clause, and other terms governing performance and discharge of obligations. Even without express clauses, the common law doctrine of frustration may be applicable, including questions of supervening illegality.

Force majeure

The literal translation of 'force majeure' is "superior force"; it is an expression which originally arose in French rather than English law. It only arises as an express contractual term, although to be effective, the term does not need to be specifically titled in that way; it is a question of form and whether it adequately protects the non-performing party from being in breach and its liability for delay or complete failure to perform. The term itself will define its extent, subject to the usual rules of contractual interpretation, although possibly with some ambiguity in the Covid-19 context, unless it expressly includes "epidemic or pandemic", which clearly potentially hits the spot. Absent such express provision, it will be necessary to construe other cited examples to see if they are likely to bite, bearing in mind that force majeure clauses are construed restrictively. Terminology which is often used and is potentially applicable is "acts of God" and "acts of government".

Whether the defendant can avail itself of the term will be fact specific as to why it was unable to perform, and then whether the factual matrix falls within the language of the express agreement between the parties. The defendant has the burden of showing the scope of the clause, and that the facts fall within it. The Health Protection (Coronavirus, Restrictions) (England) Regulations 2020 ("the Regulations") as enacted did not go so far as to order all businesses to cease operation. Those which

were required to do so were set out in Schedule 2, but otherwise, Regulation 6, dealing with restrictions on movement), expressly permitted people to leave their homes "*to travel for the purposes of work … where it is not reasonably possible for that person to work from the place where they are living*". Accordingly, businesses listed in Schedule 2 would potentially be able to avail themselves of an "act of government" term, whereas those which were not, but, for example, unable to perform because of staff absences caused by sickness are more likely to have to look at "acts of

God" arguments. There may well be issues where steps were taken voluntarily by businesses, rather than them being forced to do so by reason of the emergency legislation, particularly as, depending on the wording of the relevant contractual provision, there is likely to need to be a causal connection between the failure to perform and the force majeure event.

It is imperative for the defaulting party to remind itself of the wording of the relevant terms; if performance is at stake, many contracts require notice to be given to the innocent party within a certain timescale. There may also a requirement to mitigate the effect of the force majeure event. Furthermore, the contract will itself set out the effect of such an event: it may not provide for an automatic discharge of the contract, but merely for suspension. Being fully informed can ensure the correct steps are taken to avoid or limit liability to a disappointed customer, or, conversely, can help a disappointed customer understand their rights and ensure they are protected and enforceable.

Frustration

Frustration is a long-standing principle, arising first in the 19th century case of *Taylor v Caldwell* (1863) 3 B&S 826. That concerned an agreement for the hire of The Surrey Gardens and Music Hall in Newington (now part of South London) in the summer of 1861 for "*giving a series of four grand concerts and day and night fêtes*". After the parties entered into their agreement, the music hall was destroyed by an accidental fire six days before the first of the planned events. The Court of King's Bench concluded that since neither party was at fault, both parties were "*excused*" from their obligations under the agreement: the plaintiffs from hiring the venue and paying the sum agreed for doing so, and the defendants from providing the venue for hire.

The principle has developed since then, and is viewed as one which should not be "lightly invoked" since it brings the contract to an end (as per Bingham J in *J Lauritzen AS v Wijsmuller BV, The "Super Servant Two"* [1990] 1 Lloyd's LR 1 at 8). It may also difficult to rely on the common law principle where there is a detailed written agreement between the parties with clauses covering force majeure, intervening events and so on, on the basis that the parties have entered into their own bargain in that respect. However, the clauses must give "full and complete provision" in relation to the event in question for frustration to be ousted (*Bank Line Ltd v Arthur Capel & Co* [1919] AC 435).

A frustrating event must not be due to the fault of either party, and a contracting party cannot therefore rely on self-induced frustration. This may be relevant in the Coronavirus context if the defaulting party's behaviour was as a result of a choice when faced with issues arising as a result of the virus, rather than being forced upon it by the relevant legislation or, for example, having insufficient labour.

The general test as to frustration has recently been reiterated by Marcus Smith J in *Canary Wharf (BP4) T1 Ltd & ors v European Medicines Agency* [2019] EWHC 335 (Ch), citing Lord Radcliffe in *Davis Contractors Ltd v Fareham UDC* [1956] 1 AC 696 at 729:

> "*…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. Non haec in foedera veni. It was not this that I promised to do.*"

As with a force majeure clause, the specific facts as to why performance did not occur will be closely scrutinised. In the aforementioned *Davis Contractors* case it was held that frustration did not arise simply because performance had become unprofitable as a result of a shortage of labour and bad weather which caused delay in building 78 houses for a fixed price: "*the job proved to be more onerous but it never became a job of a different kind from that contemplated in the contract*". Covid-19 has clearly caused issues with the supply of raw materials as supply chains are affected by staffing shortages and transport difficulties. Whilst that may give rise to frustration, it was made clear by the Court of Appeal in *CTI Group Inc v Transclear SA (The Mary Nour)* [2008] EWCA Civ 856 that not every supervening event which prevents performance of a contract results in its being frustrated. In that case, which concerned supplies of cement, it was held that the failure of the appellant's suppliers to deliver was a risk that the appellant had taken on and there was no frustration.

The well-known 'coronation' cases may prove to be applicable in disputes arising in the Covid-19 context given the number of events which have been cancelled as a result of it. They arose as a result of coronation events being cancelled due to King Edward VII's ill-health, and had opposing outcomes. In *Krell v Henry* [1903] 2 KB 740 a flat in Pall Mall was to be hired on specific days on which coronation processions were due to pass along the Mall. The agreement did not expressly reference the coronation, but it was held that it could be inferred from the surrounding circumstances that the taking place of the processions on the days in question formed the foundation of the contract, and it had been frustrated. *Herne Bay Steam Boat Company v Hutton* [1903] 2 KB 683 had been an agreement for the hire of a boat to watch the king conduct a naval review, and spend the day cruising around the naval fleet. Although the review did not take place, it was not the sole basis of the contract, and the cruising aspect was still possible. Courts will scrutinise what the parties had bargained for to see whether Coronavirus, including the restrictions and their knock on effects, have made the purpose of the contract different to that which was envisaged, or just slightly different, such as for there to be no frustration.

Of interest in the current climate is this observation in *Herne Bay Steam Boat Company*, from Vaughan Williams LJ:

> "*I see nothing that makes this contract differ from a case where, for instance, a person has engaged a brake* [car] *to take himself and a party to Epsom to see the races there, but for some reason or other, such as the spread of an infectious disease, the races are postponed. In such a case it could not be said that he could be relieved of his bargain*"

It can be seen therefore that there must be a direct link between the effects of Covid-19 and the contractual performance which has not been as expected. Had the driver of the 'brake' been self-employed and unable to provide his service because he was subject to compulsory quarantine himself, that may well have amounted to frustration on the basis of performance being impossible, but again, that would have been fact specific as to the way he ran his operation. Things would become more complex if the contract was not with him personally but with an employer or agency, and would have raised questions including as to whether he personally needed to be the driver, and if other drivers were available.

As already set out, the consequence of frustration is that the contract is discharged, and all rights and obligations fall away. In terms of remedies, there are both statutory claims under the Law Reform (Frustrated Contracts) Act 1943, including for money paid before discharge and recovery of non-money benefits, and common law claims in unjust enrichment.

Supervening Illegality

This is a doctrine which is likely to be engaged in at least some Covid-19 disputes, and is effectively a form of frustration. Where a contract is governed by English law, it is discharged if performance becomes illegal by English law. However, the illegality must entirely prevent performance, rather than, for example, simply making it inconvenient, so the same issues as set out above arise as to whether the defaulting party chose to take the steps it did in difficult operating circumstances, or was forced to, for example by being a business listed in Schedule 2 of the Regulations.

Concluding comments

As Covid-19 cases begin to litigate, case law will undoubtedly assist in at least some instances, for example in relation to the interpretation of boiler-plate force majeure clauses in this context. However, as should be clear from the above, the applicability of the various legal concepts will be fact specific, and defaulting parties should not assume that Covid-19 has discharged them of their obligations.

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