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Legal Practitioners and Arbitrators

COVID-19 PANDEMIC: A FORCE MAJEURE TO RECKON WITH IN BUSINESS TODAY

THE COVID-19 PANDEMIC

As at April 5, 2020 the World Health Organisation ("WHO") has reported over two hundred countries/territories/areas with confirmed cases of the COVID-19 pandemic with the Falkland Islands (Malvinas) joining the list of territories with confirmed cases in the past 24 hours. Nigeria has reported 230 cases and 6 deaths. The world has over 1,200,000 confirmed cases and counting and nearly 70, 000 deaths. It is widely believed that these statistics are not a true picture of the situation and the correct figures are likely to be much higher as many countries face various limitations in the number of per capita test rates.

WHO has canvassed various public health and social measures to be taken by individuals, institutions, communities, local and national governments and international bodies to slow or stop the spread of COVID-19. These measures amongst others include contact tracing and quarantine, social and physical distancing including banning of mass gatherings, closure of non-essential facilities and services, local or national movement restrictions and stay-at home orders as well as international travel restrictions.

There is therefore no doubt that the world is faced with a serious health challenge, the kind and magnitude of which has not been experienced in recent history. The effect cuts across the fabric of our economic, religious and social lives. The capital market is in a state of pandemonium, manufacturing and commercial activities are almost paralyzed and performance of contractual obligations are being delayed or put on hold leading to the possibility of claims of breach of contract or default. However, this might not be the case where the agreement between parties provides for a Force Majeure clause.

WHAT IS FORCE MAJEURE?

The term Force Majeure is actually a French phrase which means "irresistible compulsion or greater force" having its origin in the Latin term vis major meaning "an act of God or a superior force or an irresistible natural occurrence resulting in damage or disruption that cannot be prevented by humans". It is provided under the French Civil Code as a defence against liability for contractual non-performance due to the occurrence of certain events. However, under English law from which Nigeria derives its legal system, the term Force Majeure is not expressly recognized but is quite similar to the English common law principle of Frustration which will be discussed further below. The following elements are usually present in a general definition of Force Majeure contained in a contract: The circumstance must be such:

(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.

However, each contract is unique and would usually involve a variation of the above based on the industry and negotiation between contracting parties. The definition is usually accompanied by a list of Force Majeure events which upon their occurrence entitles a party to be excused for non-performance, partial or delayed performance as the case may be. To the inattentive lawyer or contractual parties, Force Majeure is one of those frequently overlooked boilerplate clauses that is either completely ignored or poorly drafted to address possible eventualities. However, with the present Covid-19 outbreak, it has become one legal terminology that is on the lips of business owners and stakeholders in various industries – from aviation to banking, oil and gas, power, information technology, manufacturing, maritime, hospitality, sports, and others.

TREATMENT OF FORCE MAJEURE UNDER NIGERIAN LAW

In our jurisdiction as in other common law jurisdictions, Force Majeure provision cannot be implied into a contract and must be specifically provided for in a contract for it to avail a party.

In the Court of Appeal case of Globe Spinning Mills Nigeria Plc vs. Reliance Textile Industries Ltd (2017) LPELR-41433 (CA) the parties' Sale and Purchase Agreement defined Force Majeure as follows:
Force Majeure:

28. The term force majeure means circumstances beyond the control of the party concerned and resulting in or causing a failure or delay by or hindrance to or interference with such party in the fulfillment wholly or in part of any of its obligations under this agreement which circumstances cannot be prevented or overcome by the exercise of due diligence by the party concerned and without prejudice to the generality of the foregoing shall be deemed to include (but not limited to) the following:

i. compliance with any law, regulation, policies, order or demand or any other act of any government or its agencies;
ii. strikes, boycotts, lockouts and other industrial disturbances;
iii. Acts of God, acts of the public enemy, wars, blockades, military action, insurrections, riots, epidemics, landslides, lightening, earthquakes, fires, explosions, storms, floods, civil disturbances and restraints of all governments which makes the operation of textile or spinning industry impossible.

29. On the occurrence of any of the events as listed in clause 28 (i-iii) the parties shall be relieved from liability under this agreement, except in relation to obligation to make outstanding payments on the due dates and in delivering to the Buyer the quantity of yarn already manufactured and any available excess which has not been committed to a third party before the occurrence of the force majeure.

30. A party seeking relief under this force majeure shall, within a period of forty-eight hours after the happening of the event causing the force majeure, notify the other of such event and shall with diligence furnish such relevant information as is available concerning the event and give an estimate of the period of time required to remedy the failure.

The Respondent in declaring Force Majeure as its reason for refusal to take delivery of the contracted quantity of yarn, stated in its notice letter to the Applicant, four major hindrances to its ability to fulfill its obligation under the agreement as:

1. Failure of government to curb illegal importation of textile fabrics banned by the federal government.
2. Permanent loss of market with no future anticipated turn around due to huge supply of low priced illegally imported fabrics.
3. Frequent and unpredictable interruptions in gas supply which is our only financially viable source of energy.
4. Mounting cash losses coupled with a large level of unsold stocks and high customer credit outstanding which have resulted in our liquidity crunch.

The Arbitral Tribunal in rejecting the plea of Force Majeure by the Respondent, examined what conditions the Respondent must show to bring its eventualities within the realm of Force Majeure in clauses 28-30 of the agreement, stating that:

"From the evidence given we were able to ascertain that there were alternative sources of energy which the respondent would use either in addition to or in substitution for gas at comparative cost. Mounting cash loss and unsold stock are normal vicissitude of business which can easily be anticipated by companies. We are therefore of the opinion that these circumstances are not beyond the control of the respondent resulting in or causing a delay to or hindrance to the fulfillment of the obligation of the respondent in the agreement which circumstances cannot be overcome by the exercise of due diligence on the part of the respondent. We therefore hold that force majeure based on the facts given by the respondent cannot be sustained."

Upon appeal of the decision of the High Court which upturned the decision of the Tribunal, Honourable Justice Uzo I.A Ndukwe-Anyanwu J.C.A (Delivering the Leading Judgment) upheld the decision of the Tribunal, stating further:

Force majeure is generally intended to include occurrences beyond the reasonable control of a party, and therefore would not cover:

1. Any result of the negligence or malfeasance of a party, which has a materially adverse effect on the ability of such party to perform its obligations.
2. Any result of the usual and natural consequences of external forces. To illuminate this distinction, take the example of an outdoor public event abruptly called off. If the cause for cancellation is ordinary predictable rain, this is most probably not force majeure. If the cause is a flash flood that damages the venue or makes the event hazardous to attend, then this almost certainly is force majeure. Some causes might be arguable borderline cases; these must be assessed in light of the circumstances. Any circumstances that are specifically contemplated (included) in the contract – for example, if the contract for the outdoor event specifically permits or requires cancellation in the event of rain.

This case buttresses a fundamental principle in interpreting Force Majeure clauses, which is that the event in particular must be expressly provided in the agreement or in the absence of an express provision, the event must be one which closely resembles the enumerated events or can be inferred from a catchall phrase which can be interpreted to include similar occurrences as those listed. Such as in the instant case of Globe Spinning Mills, the phrase "... and without prejudice to the generality of the foregoing shall be deemed to include (but not limited to) the following:" Even at that, these clauses are usually interpreted quite narrowly and the threshold for excusing non-performance is quite high.

COVID-19 A FORCE MAJEURE?

In a Covid-19 situation, how do you determine whether non-performance of your obligations under your contract is permitted or on the flip side, if you are the recipient of Force Majeure notice, how do you confirm that the other party is excused from non-performance or is permitted delayed or partial performance? Each contract will have to be thoroughly scrutinized and considered on a case by case basis. Many Force Majeure clauses may not include words such as plagues, epidemic or pandemic in the list of events constituting Force Majeure particularly in older contracts. In the absence of such express words, it would be necessary to consider the interpretation of certain words and phrases usually included in the list of events such as "compliance with any law, regulation, policies, order or demand or any other act of any government;
Acts of God.

A consideration of the definition which usually includes the phase: "circumstances beyond the control of the party concerned" may also be necessary. The questions would be whether the direct effect of Covid-19 itself such as for example confirmed cases of contagion or sickness amongst key employees required to perform the contract, or the resultant effect of the pandemic such as government lockdown and inter-state transportation restrictions preventing access to relevant production materials (which are definitely circumstances beyond anyone's control) has rendered performance under the contract impossible. Where circumstances beyond the party's control have been established, it would still be necessary to prove other key elements required to claim Force Majeure viz:

- The event must be such as makes performance of contractual obligations impossible;
- The event was unforeseeable and steps to mitigate have been taken.

For instance, under the inter-state transportation restrictions scenario, is it possible to source alternative materials within the party's factory location albeit at a significantly higher price? Generally, economic hardship would not be considered as constituting Force Majeure and the fact that it is impracticable or difficult to carry out performance of the obligations is not sufficient. In the scenario of confirmed cases and sickness amongst key employees, unless it is a contract of which time is of the essence, is it possible to mitigate by identifying and providing ad hoc training to other employees who may be guided to work remotely to deliver on the contract albeit resulting in delayed or part performance? In Nigeria for instance, President Muhammadu Buhari on 30 March 2020 declared a complete lockdown of residents and businesses in Abuja, Lagos and Ogun State, for an initial period of 14 days exempting only businesses engaged in essential services like healthcare services, manufacturing and distribution, food processing, petroleum distribution and retail entities from the directive. It would therefore be more difficult for essential services providers to claim Force Majeure under COVID-19 for inability to fulfill their contractual obligations. This is because although it might be quite difficult to fulfill some obligations due to third party considerations, it may not be considered impossible as they are still allowed to carry on business despite the pandemic and the resultant government action. Each situation would need to be determined on its own merits.

Where a party is able to show that its inability to perform its obligations is really due to a Covid-19 event and that it was it was ready, willing and capable of performing its obligations but for the effects of the pandemic, the clause might have the following effects depending on the provisions of the agreement:

- Immediate termination of the contract
- Suspension of contractual obligations
- Termination of the agreement if the event isn't resolved within a specified number of days
- Non-liability for failure to perform its obligations
- Extension of time to fulfill obligations
- Renegotiation of terms
- Obligation to mitigate losses

Most clauses would also include provisions requiring certain steps to be taken in order to effectively rely on Force Majeure. These would usually include written notice to the other party (ies) within a specified period after the occurrence of the event with particulars of the occurrence and how it prevents performance; obligation to keep the other party (ies) informed of developments; mitigation steps taken if any and estimated time frame for remedying the situation particularly where the clause includes a duty to overcome. It is important to ensure compliance with these steps in claiming Force Majeure and likewise for a recipient party to consider whether the party claiming Force Majeure has done so in the specified manner. Sometimes these obligations are affected by third party obligations of contractors and sub-contractors down the value chain and must be meticulously tracked and managed.

Another issue to be considered is how parties are brought to a state of equilibrium particularly with regard to payment obligations upon the occurrence of a Force Majeure event especially in situations where a Force Majeure event which continues for a specified prolonged period of time entitles parties to terminate the contract altogether. We consider below how this is treated under oil and gas contracts.

INDUSTRY PRACTICE: A LOOK AT OIL & GAS CONTRACTS

The Association of International Petroleum Negotiators ("AIPN") Model Joint Operating Agreement ("JOA") defines Force Majeure as (i) "those circumstances beyond the reasonable control of the Party concerned", or alternatively, (ii) "those circumstances that could not have been avoided or mitigated by foresight, planning, and implementation consistent with generally accepted practices of the international petroleum industry, including strikes, lockouts, and other industrial disturbances even if they were not beyond the reasonable control of the Party." Some JOA definition clauses are often incorporated into other industry agreements particularly those connected to the JOA parties. In the second option, a party claiming Force Majeure may not be required to prove that the circumstances were beyond its reasonable control, but it would need to establish for instance that actions of mitigation employed are consistent with generally accepted practices of the international petroleum industry.

Some industry contracts expressly exclude inability to fulfill payment obligations as a reason to declare Force Majeure. Such inability cannot therefore be excused and would result in breach or default. This is particularly so with oil and gas contracts such as the JOA where cash call payments are central to the continued operations of the asset. The AIPN model JOA for instance provides that "If as a result of Force Majeure any Party is rendered unable, wholly or in part, to carry out its obligations under this Agreement, other than the obligation to pay any amounts due or to furnish Security, then the obligations of the Party giving such notice, so far as and to the extent that the obligations are affected by such Force Majeure, shall be suspended during the continuance of any inability so caused ..."
On bringing parties to a state of equilibrium, a Seismic Processing Agreement we considered provides that "Save as otherwise expressly provided in the CONTRACT, no payments of whatever nature shall be made in respect of a force majeure occurrence." This basically ensures that where Force Majeure prevents performance, the other party is not obligated to make payment for unperformed obligations.

The situation is however not always as clear cut particularly where you have contracts requiring part or milestones payments prior to contract performance or delivery or where there has been part performance prior to payment obligation becoming due or payable. Examples of such are Engineering, Procurement and Construction ("EPC") contracts. We have seen such contracts include provisions which requires that upon termination due to a Force Majeure event, the contractor claiming Force Majeure shall be paid for work carried out for which a price is stated in the contract; and for any other liability which in the circumstances was reasonably incurred by the contractor in the expectation of completing the works. There may even be need for refund where the work done is not commensurate with the payment already made. Such provisions are rarer to find in a Force Majeure clause and other factors may need to be considered in determining quantum of refund such as the provisions of the law in that jurisdiction as well as common law doctrines.

THE ENGLISH LAW VARIATION OF FRUSTRATION OF CONTRACT

The general doctrine of sanctity of contract under English law stipulates that contracting parties are strictly bound by the provisions of their contract. They are therefore bound to make good whatever obligation they have covenanted to under their contract. The doctrine of Frustration of contract was however later developed in English law jurisprudence to permit an exception to the general rule thus permitting the discharge of a contract where certain circumstances arise after the formation of a contract which makes the performance of the contract impossible. In the words of Honourable Justice Rhodes-Vivour, J.C.A. (Delivering the Leading Judgment) in Diamond Bank Ltd vs Prince Alfred Amobi Ugochukwu (2007) LPELR-8093(CA) "Frustration would occur where it is established to the satisfaction of the court that due to a subsequent change in circumstances which was clearly not in the contemplation of the parties the contract has become impossible to perform." Therefore, for the doctrine of Frustration to apply, the performance of the contract must be radically different from what was intended by the parties. Frustration may be pleaded where a contract has no Force Majeure provisions. The doctrine is usually more restrictive in interpretation and once proven, results in automatic discharge or premature determination of the contract thus excusing further performance of the contract. Frustration events include:

(i) subsequent legal changes which make a contract impossible or illegal to perform;
(ii) outbreak of war;
(iii) destruction of the subject matter of the contract;
(iv) failure of the commercial purpose of the contract,
amongst others and such events must be due to no fault of
the contracting parties.

In the light of the above, can a party for instance plead subsequent legal changes such as travel restrictions or government lockdown as supervening Covid-19 events, which may frustrate a contract? Such a question would be left to the determination of the courts on a case by case basis.

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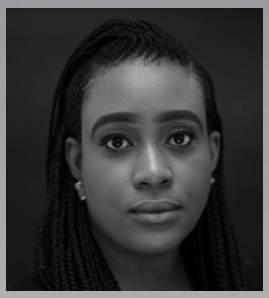

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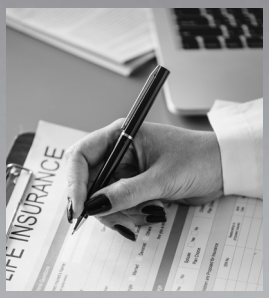

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