

Contractual risks amid the COVID-19 outbreak

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The novel coronavirus (COVID-19) outbreak is causing widespread social and economic uncertainty. Amongst other commercial effects, it has led to travel restrictions, workplace disruptions and global supply chain issues. The reality of unexpected events, such as the spread of COVID-19, raises questions as to the operation of force majeure clauses. As the Supreme Court of Canada has explained,¹ force majeure or “act of God” clauses generally operate to discharge a contracting party when a supervening, sometimes supernatural, event beyond the control of either party makes performance impossible. The common thread is that of the unexpected—something beyond reasonable human foresight and skill.

The extent to which specific events relating to COVID-19 trigger a particular force majeure clause will depend on the wording of the provision and on the factual circumstances. However, this article provides an overview of the law relating to force majeure clauses and their role in allocating the risk of the unexpected.

Force majeure clauses and triggering events

A force majeure clause will typically include a list of specified “triggering events,” usually of an exceptional nature (such as earthquakes, floods or war), and may include a catch-all phrase designed to cover events not listed specifically in the clause. The listed “triggering events” generally reflect standard form drafting, but parties are at liberty to amend or supplement the standardized language to suit business needs.

Invoking force majeure

In order for a force majeure clause to be effective, the “triggering event” must fall within the scope of the provision. In addition, other considerations often direct the proper operation of force majeure clauses. For example, the party seeking to rely upon the provision generally bears the burden of showing that the event has significantly affected its ability to perform its contractual obligations. Further, force majeure clauses generally pre-suppose and require that the “triggering event” not be caused by, or otherwise be within the control of, the party seeking to be excused from performance.

It may be more difficult for a party to invoke force majeure if the impact involves an inconvenience one would encounter in the ordinary course of business, such as higher

operating costs or a recessionary market. Whether or not an event has affected the party's ability to perform a contractual obligation as a force majeure will be a fact-dependent analysis, with consideration of (amongst other things) the nature of the contract and the extent to which the "triggering event" has affected the locality of the invoking party. Any party attempting to invoke a force majeure clause should also strictly adhere to any required procedural steps set out in the relevant provision.

Effect of the clause

Upon the occurrence of a "triggering event," the force majeure provision would operate according to its terms. This may include the temporary or permanent release of the parties from some or all of the contractual obligations that parties would otherwise be required to perform. In certain cases, parties may invoke force majeure clauses to prioritize certain obligations over others. Parties invoking such a clause have a duty to mitigate the costs flowing from the suspension of the obligations (again, subject to or in line with the specific drafting of the relevant clause), or do what is commercially reasonable and feasible to help limit the losses suffered by the other party to the contract.

No force majeure clause

If a contract is silent on force majeure, impacted parties may nevertheless consider whether they can seek relief under the common law or applicable statutes. For example, the legal doctrine of frustration may serve as a viable solution in cases where there is no applicable force majeure clause. The principles of frustration require, amongst other things, that a supervening event be unforeseeable and render the contract "radically different" from what was originally undertaken. The concepts and consequences of the doctrine of frustration may also be captured in statutes, such as the Ontario Frustrated Contracts Act. The question of whether frustration is actually applicable to a given scenario is fact-dependent.

Conclusion

Many countries around the world are facing the public health, social and economic challenges associated with responding to the COVID-19 outbreak. Many parties to contracts may be considering whether the unfolding issues constitute force majeure, as articulated within the terms of their contracts. While this question will continue to evolve according to individual circumstances, businesses should proactively assess their risk profile, and, at the same time, evaluate the extent to which future contracts should address force majeure events, what those events may be, and which party should bear the risk.

¹ Atlantic Paper Stock Ltd. v. St. Anne-Nackawic Pulp and Paper Company Limited [1976] 1 SCR 580.

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