COVID-19: PRESSURE POINTS: FORCE MAJEURE CONSIDERATIONS IN A POTENTIAL "SECOND WAVE" OF COVID-19 (UK)

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Legal Briefings – By **Emma Schaafsma, Sarah Pollock, Maura McIntosh and Julie Farley**

As many countries contemplate an easing of COVID-19 lockdown restrictions following a downturn in cases, scientists and politicians are warning of the possibility of a "second wave" of COVID-19 cases which would then require a re-imposition of restrictions. We are already seeing this in certain Asian countries.

The prospect of a second wave will have important implications for contracting parties who are currently affected by a force majeure event related to the COVID-19 pandemic. At the same time as dealing with the current impacts on their contracts, parties should be looking forward and preparing not only for the end of the current relief due to force majeure, but also a possible second claim for force majeure relief should restrictions be re-imposed as a result of a second wave of the pandemic.

What this means in practice will very much depend on the situation affecting each individual contract:

- in some cases, parties will be able to resume full contractual performance as restrictions are lifted so that the initial period of force majeure relief ends, but then find that the re-imposition of restrictions affects their contractual performance in a different manner and to a different extent;

- in other cases, parties may not be able to resume performance before any new restrictions come into force, in which case they will need to assess whether they need to notify of a new force majeure event;

- others may not yet have sought force majeure relief but may find that the second round of restrictions affects their performance so they will be seeking force majeure relief for the first time.

Whatever the situation, it is essential for parties to consider now how their situation may evolve in light of any potential easing and re-imposition of restrictions, and what they need to be doing at each stage to ensure that they obtain the best contractual protection available.

THE LAW

Although many jurisdictions have statutory requirements in relation to force majeure, this article considers the position where force majeure is solely a contractual concept, as is the case in the UK and other common law jurisdictions. In those jurisdictions, in broad terms and subject always to the actual wording used, force majeure provisions will typically excuse one or more parties from performing their contractual obligations if they are prevented from doing so by circumstances outside their control. The following requirements must generally be met in order to gain relief from performance:

- The occurrence of an event beyond the parties' reasonable control that falls within the term "force majeure" in the contract. The term is often defined by reference to a list of categories of events, which may include an epidemic or pandemic, a change of law or regulation, or an act of government. It could be a closed list, contain sweep-up wording to cover other similar events, or otherwise be a non-exhaustive list.

- The event has affected the party's ability to perform the contract. The relevant test will be set out in the contract, but will typically require that the force majeure event has prevented, or perhaps hindered or delayed, performance of "any" (often referred to as "partial force majeure") or sometimes "all" of their obligations under the contract.

- The party could not have avoided the impact of the event itself or its consequences by taking reasonable steps.

- The party claiming relief has satisfied any notification requirements in the contract.

- Often there will be express obligations on parties to take reasonable steps (sometimes phrased as a "best endeavours" or "reasonable endeavours" obligation) to mitigate the impact of the force majeure event (eg by resequencing work, implementing business continuity plans, making adjustments within the supply chain, etc).

DEALING WITH CURRENT FORCE MAJEURE RELIEF WHEN INITIAL RESTRICTIONS ARE LIFTED

The wording of the contract is key in assessing when force majeure relief ends. Commonly the contract will provide that force majeure relief will continue only for so long as performance of the contract is prevented (or hindered or delayed).

There will inevitably be a difference of views as to when the impact has ended and, in the case of partial force majeure relief, at what point individual obligations were no longer affected. Parties currently benefitting from force majeure relief should be constantly monitoring the impact that the force majeure event has on their ability to perform the contract so that they can be ready to resume performance as soon as that impact ceases. A failure to do so could result in a party being in breach of contract for failure to perform once the period of force majeure relief ends.

Parties who are close to a situation where they, or their counterparty, are entitled to terminate the contract for prolonged force majeure should take particular care in light of government indications that restrictions are being, or will soon be, lifted. Such termination rights are commonly tied to the length of time that a party is prevented, hindered or delayed in performing its obligations under the contract, so again the focus would be on when the affected party was no longer affected by the COVID-19 pandemic. Termination due to long-term force majeure close to the point at which the impact ended, eg the lifting of the government restrictions, is likely to be challenged (and, indeed, could give rise to a claim of repudiatory breach of contract entitling the other party to seek damages for wrongful termination). The party terminating in those circumstances should ensure that it gathers strong contemporaneous evidence justifying its actions.

PREPARING FOR AND DEALING WITH A SECOND WAVE OF RESTRICTIONS

Second force majeure event: Parties will need to consider now how to prepare for the risk of a second round of restrictions. They need to consider afresh what it is that might prevent them from performing their contractual obligations and whether that event falls within the scope of force majeure relief in their contract. The existence, and specific terms, of any right to terminate for long-term force majeure should also be considered, as some termination rights arise when there are multiple periods of prevention of performance due to the same notified force majeure (see further below).

It will also be important to consider whether other provisions might apply, such as change of law, price reopeners or cost sharing. Obviously the application and operation of any such clauses will need to be carefully considered but, if relevant, they could provide an alternative source of relief including, in some cases, more generous relief than may be available under a force majeure clause.

Impact / causation: As noted above, contracts commonly specify how the force majeure event has to impact performance before relief can be claimed, often using one or a combination of “prevent”, “hinder” and “delay”.

Just as the trigger for a second period of force majeure relief may not be the same as the trigger for the initial period so the impact may not be the same in a subsequent period. For example, should the contract in question require that force majeure relief is only available if performance of "all" obligations are "prevented" by force majeure, if with the second wave only some obligations are affected, and possibly merely hindered, then force majeure relief would not be available the second time around. The affected party must consider these issues and reflect them correctly in any notification of a second force majeure period.

Most importantly, the failure to perform must be **caused** by the force majeure event in order to give rise to relief. In order to benefit from relief due to the impact of a potential second wave of COVID-19 infections and restrictions, the affected party will need to show that it could not reasonably have protected against the impact that a second wave and any related governmental restrictions might have on its performance under the contract.

Given that scientists are currently warning that a second wave is likely, it is essential that companies start planning now so that they can show they have taken reasonable steps to avoid any impact on their contractual performance. Merely relying on the same steps that were taken to avoid the impact of the first wave of COVID-19 pandemic is unlikely to be sufficient, and could lead to allegations that the cause of a party's inability to perform its contractual obligations is, in fact, its lack of preparation rather than the force majeure trigger.

The steps that a party should take will be highly dependent on what was reasonable in the circumstances, for example:

- What a party could reasonably achieve in light of any relaxation of existing government restrictions prior to any second wave, and the nature of any restrictions introduced in response to a second wave.
- The availability of materials etc necessary for performance of the contract during any period of relaxation of restrictions (how fast can factories ramp up, start producing, start shipping), and the ability to stockpile such materials in that time.
- For supply contracts, if the contract permits supply from any (rather than a particular) source, the extent to which a party may be able to identify and change to a source of supply that might be less vulnerable to a second wave.
- In the context of long-term operation and maintenance contracts for properties and facilities, the ability to reschedule outages and maintenance activities to undertake operation-critical maintenance before the second wave hits (noting the ability to reschedule in the context of other activities, the ability to ramp up staffing levels etc).
- The ability of the affected party to change operating practices, train more staff, adjust working conditions to facilitate social distancing, etc.

Notification: Parties impacted as a result of a second wave of COVID-19 cases and associated restrictions need to ensure that they continue to comply with the notice provisions in the contract, which are commonly drafted as conditions precedent to obtaining relief. Note that some notice provisions require notice to be given within a number of days following the occurrence of the force majeure event, rather than from when performance is affected by the event.

Even where a party has not been able to resume performance before new restrictions are imposed as a result of a second wave of infections and restrictions, it will still need to re-assess its notification obligations. It may well be that the prudent course of action is to issue a new notice to reflect the fact that it is being prevented by additional or other matters, even if in practice the impact is the same.

Notifying parties should also consider whether, from a practical point of view, they should serve notice in a number of ways. For example, the contract notice provisions may require notice to be sent to an office address, but in reality it is unlikely that anyone will be there to receive it because of the local lockdown measures in place. In such circumstances, as well as sending the notice to the stated address in order to comply with the contractual requirement, parties should take practical steps to bring the notice to the attention of their counterparty, for example by sending an email copy to key personnel.

Mitigation: As noted above, even if it is not possible to avoid the force majeure event having the relevant impact on performance, the affected party will typically be under an ongoing obligation to take reasonable steps to mitigate that impact. Again, what is reasonable will be considered against the circumstances at the time. An obvious response might be that the affected party would be expected to take the same or similar mitigation measures as with the first wave (which might indeed have been none in some circumstances). However, the following should be borne in mind:

- Given that this is a second wave, the circumstances might be such that the affected party is (or should be) able to implement mitigation measures faster and more effectively than with the first wave.

- The range of options that need to be explored could well be different from those in the first wave, depending on the extent of the restrictions imposed and the circumstances of the affected party – both of which could differ significantly from the first wave.

Termination for multiple periods of force majeure: Some contracts provide for termination in the event of multiple periods of force majeure preventing performance for an aggregate number of days. Careful consideration of the wording used will inform whether this right is available for any number of different force majeure events, or if it only applies for multiple periods of prevention due to the "same notified force majeure". If the latter, while the overarching cause could be seen as the COVID-19 pandemic, there may be scope for debate as to whether a second period of force majeure relief is in fact due to the same force majeure event as initially claimed, and therefore counts towards the termination trigger.

Any party in such a position should consider its options carefully and take legal advice before exercising the termination right. As previously noted, if the right is not exercised properly, or if it is later found that the force majeure clause did not apply, the purported termination could be considered a repudiatory breach of contract (under English law) which could entitle the innocent party to either affirm or terminate the contract and seek damages.

WHAT SHOULD COMPANIES DO NOW TO PREPARE FOR A SECOND FORCE MAJEURE EVENT?

Contract audit: As force majeure is a contractual concept, being fully aware of the provisions contained in the relevant contracts is critical. In all likelihood, parties have already conducted an audit of their contracts as part of their initial response to COVID-19 and the related restrictions. If not, now is the time to do it. Parties should consider each contract individually and bear in mind that the provisions may vary from contract to contract, in terms of the trigger events, the extent of the impact required before relief can be claimed, the notification requirements and specific provisions around mitigation, termination rights and the ending of force majeure relief.

Preparation: Planning for any second wave is essential and, as noted above, a failure to do so could result in force majeure relief being unavailable. Parties should therefore consider what steps they can take (both now and as and when a second wave occurs) to increase the resilience of their operations and implement work-arounds to deal with any restrictions that may be imposed.

Collaboration: Depending on the circumstances, including the nature of the relationship that a contracting party has with its counterparty, it may be worth taking a collaborative approach to the prospect of a second wave of restrictions and having discussions around alternative ways of performing the contract and what mitigation can be put in place – while considering carefully before waiving any contractual rights.

(Note added 19 May 2020: The UK Government has published non-statutory guidance encouraging all contracting parties to act responsibly and fairly in the national interest in performing and enforcing their contracts, to support the response to COVID-19 and to protect jobs and the economy.)

Documenting steps taken: It may be that, in reality, there is a limited range of options available to avoid the impact of a second wave or mitigate the effects. Nonetheless, it will be important to document what steps are being explored and, if they are dismissed, why – as well as the steps taken. This will be vital evidence to demonstrate that a party has taken the necessary steps to avoid a force majeure event having an impact on its performance and, if such an impact cannot be avoided, that it has satisfied the mitigation requirements.

Maximising privilege protection: At the same time, parties should take care in avoiding any unhelpful documents being created which may have to be disclosed in any subsequent legal proceedings. To the extent that parties are seeking legal advice on their position or preparing for any litigation or arbitration that may be contemplated, appropriate steps should be taken to maximise the protection of legal professional privilege.

Dealing with claims for relief: Counterparties who are receiving claims for force majeure relief in the current circumstances should carefully consider them in light of the above considerations. Where there is an existing agreement as to how to address the current circumstances, consider whether it can and indeed should be extended to cover a second wave. It may be that the second wave situation necessitates a different arrangement.

New contracts: Any contract entered into now should deal expressly with the possibility of COVID-19 related restrictions having an impact on performance. Parties should not rely on a force majeure clause to protect them in the event of a second wave, given that a second wave of restrictions is currently anticipated and therefore may be unlikely to fall within many force majeure clauses.

More on COVID-19

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

SARAH POLLOCK
PARTNER, LONDON

+44 20 7466 2786
sarah.pollock@hsf.com

MAURA MCINTOSH
PROFESSIONAL SUPPORT CONSULTANT, LONDON

JULIE FARLEY
PROFESSIONAL SUPPORT LAWYER, LONDON
+44 20 7466 2109

+44 20 7466 2608 Julie.Farley@hsf.com
Maura.McIntosh@hsf.com

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