



Force majeure clauses - sword or shield?

▲ **Trying times** companies in many sectors will be forced to review the terms of existing contracts to determine their legal responsibilities amid Covid-19

The Covid-19 pandemic situation is currently evolving and ensuing, and its far-reaching effects are not yet assessed fully

THE ONGOING CRISIS following the Covid-19 pandemic has given rise to unprecedented circumstances and there is no denying that businesses have slowed down.

Businesses and transactions have been able to run, nonetheless, putting to use the available technological alternatives. As a result, physical meetings have

been replaced with video conferencing, and homes are filling in as offices. However, this serves its purpose in sectors where providing the product and/or service is unaffected by

3%

Contraction of the global economy as a result of Covid-19, according to the IMF

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measures taken in respect thereof may not be uniformly applicable to every sector.

Frustrated

In cases where restrictions imposed by the governments have rendered performance of obligations impossible, it may be said that the contract has been frustrated. When a contract is frustrated, the parties may invoke the force majeure clause to determine the fate of the contract.

The force majeure clause in a contract holds great significance in the prevailing times of the Covid pandemic and lockdown. Such clauses usually describe the applicable force majeure events, like natural calamities, government sanctions, and war, and set forth the consequential terms for when performance becomes difficult or impossible during such times.

Interpreted literally, a typical force majeure clause may not effectively cover all events causing impediments on the performance of obligations, and therefore may not be able to shield the interests of the obligors – who may still be required to perform despite the situation, or

the government's restrictive measures. Other sectors are not left with many options, except for the contracting parties to review terms of their underlying contracts and check the scope and extent of the applicability of force majeure clauses.

The Covid-19 pandemic and the preventive

compensate the other party. An incomplete clause therefore makes positions lopsided with a weak shield for the obligor and a heavy sword for the creditor.

Courts

On the other hand, the absence of such a clause, or such clause submitting to the prevailing laws, may give parties the option to determine the fate of the contract in accordance with the prevailing laws. However, this may also be marred by its time and cost impact due to the involvement of courts or dispute resolution forums.

Eventually it may rest on the contracting parties to consider the applicable force majeure clause and apply the same in a way so as not to make it too onerous on any one party to the contract.

For effective application, force majeure clauses may be drafted with the widest possible inclusions like “any pandemic”, “virus/ biotech disasters”, “leakage or spillage of nuclear/ hazardous items”, “biological warfare” and cover situations like “lockdowns”, “restrictions on public/ cargo movement” and so on. Further, parties may also consider incorporating a limitation of liability clause to deal with a force majeure event.

The Covid-19 pandemic situation is currently evolving and ensuing, and its far-reaching effects are not yet fully assessed. For the time being, it is for the contracting parties to assess their obligations in view of the existing circumstances,

with special reference to force majeure clauses, if any.

Defence

For the defence of force majeure, it is essential for the obligor to notify the creditor regarding the former's inability to perform its obligations. Inasmuch as the Covid-19 pandemic has taken the entire world, within its grip, contracting parties even in different jurisdictions would be able to appreciate the impact thereof. It is therefore essential for the parties to keep communicating about their respective positions, to determine and agree upon terms suited to the best interests of both.

The exact financial implications of frustration of contracts or application of force majeure clauses following the Covid-19 pandemic may be assessed in view of the implications following either the full rescinding of a contract or the extinguishment of a part of the obligations rendered impossible due to circumstances following the pandemic situation.

However, the implications will also depend on the period that the pandemic continues to exist, and how soon an effective cure is devised. It may be perceived that the existence of the pandemic for continued periods will likely invite the imposition of greater restrictions, which may have negative multiplier effects on sectors otherwise unaffected by the pandemic situation. Under such circumstances, the financial implications would be far reaching. ■