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International construction business, COVID-19 and reasons to excuse performance or not

by Simon Tolson

It is not often disease impacts construction in a macroeconomic way.

The global presence of the China / PRC in the construction space is unparalleled. According to the Nikkei Asian Review, Chinese contractors took in nearly a quarter of international construction revenue in 2018, so disease that paralyses China is inevitably going to have repercussions

Ebola virus disease was brought to the world's attention in March 2014 by the charity Médecins Sans Frontières when it announced 25,000 people infected and 10,000 of them killed by it - almost all in Guinea, Liberia and Sierra Leone. Panic arose obviously. But no impact on business or hits on construction activity.

So six years later as a result of the novel coronavirus (or COVID-19) outbreak as at 19 February 2020 there have been 75,200 confirmed cases and 2,012 reported deaths around the world and counting. It originated in Wuhan, China, many cities and regions across China have introduced near lockdown and announced travel restrictions and a supercharged version of a neighbourhood watch to keep hundreds of millions of people away from everyone but their closest kin.

As readers will know, The World Health Organisation declared[1] COVID-19 a public health emergency of international concern. For example, the Singapore Ministry of Health promptly announced that from 1 February 2020 all new visitors with recent travel history to mainland China within the last 14 days will not be allowed entry into Singapore, or to transit through Singapore. Then the Immigration and Checkpoints Authority suspended the issue of all forms of new visas to those with PRC passports. Things have spiralled.

My firm has seen two energy related arbitral cases listed in Singapore this month, both adjourned at the last minute due to COVID-19 travel restrictions affecting witnesses and tribunal alike. Business trips to China ended in January and vice versa, caution abounds.

This impact of such announcements and factory and office closures accompanied with other international government responses to COVID-19 is creating issues on business operations, particularly for construction, manufacturing facilities and supply chains.

China has already issued more over 1,600 force majeure slips to COVID-19 hit companies to shield them from damages liabilities[2]. The certificate[3] exonerates companies from not performing or partially performing contractual duties by certifying they are suffering from circumstances beyond their control.

1. 31 January 2020.
2. On 14 February 2020 The China Council for the Promotion of International Trade (CCPIT) has issued 1,615 certificates for companies involving over 30 sectors, covering a total contract value of $15.7 billion.
3. CCPIT's force majeure certificates are recognised by governments, customs, trade associations and enterprises of more than 200 countries.

Companies here now need to consider their obligations in response to government announcements, the level of business disturbance and other commercial risks[4], as well as the options under their contracts, including the common law doctrine of frustration and the operation of contractual "force majeure" clauses.

Further considerations may be relevant in the context of Engineering, Procurement and Construction (EPC) agreements and energy or mineral resources contracts which may be particularly affected along the Belt and Road.

But wait a minute, are we running ahead of ourselves? We might be regarding travel. The International Health Regulations (2005) (IHR)[5] governs how WHO and 196 countries collectively address the global spread of disease and avoid unnecessary interference with international traffic and trade. Article 43 of this legally binding instrument restricts the measures countries can implement when addressing public health risks to those measures that are supported by science, commensurate with the risks involved, and anchored in human rights. The intention of the IHR is that countries should not take needless measures that harm people or that disincentivise countries from reporting new risks to international public health authorities. In imposing travel restrictions against China during the current outbreak of COVID-19), many countries are violating the IHR!

Article 43.2 says countries cannot implement additional health measures exclusively as a precaution but must rather ground their decision making in "scientific principles", "scientific evidence", and "advice from WHO". Many of the travel restrictions being implemented during the COVID-19 outbreak are not it seems supported by science or WHO. Travel restrictions for these kinds of viruses have been challenged by some public health researchers. We will have to see how this develops.

Whilst the outbreak of an epidemic may not be seen as an unforeseeable event given the outbreaks of various strains of flu in recent years since SARS in 2003 and MERS in 2012. What is different this time is the unprecedented scale of the restrictions enforced together with their swift implementation. This could differentiate the coronavirus outbreak from other epidemics. The recognition by the WHO of the severity of the outbreak and separately, by the Chinese authorities that its implications constitute a force majeure event is likely to assist the party seeking relief to rely on the force majeure clause.

In most civil law countries, the doctrine of 'force majeure' will apply where exceptional and unforeseen events threaten excessively onerous loss to one of the parties. In those jurisdictions, the law may excuse that party from further performance or limit his losses.

Common law systems, such as the English legal system, adopt a different approach. "Force majeure" does not have a precise legal definition, but its meaning is more extensive than an "Act of God". Typically, a force majeure clause will list a number of events, the occurrence of which may excuse a party from its obligations under the contract. The word "epidemic" is listed as such an event in many commercial contracts. Therefore, in such circumstances and in light of the WHO's classification of COVID-19 as an epidemic, a party to a contract containing a force majeure clause should not have too much difficulty in asserting that the COVID-19 outbreak triggers the provisions of that clause.

There is no doctrine of force majeure as such but, instead, the common law relies wholly on its use as an express contractual term, and how the parties decide to regulate for unforeseen events in their contract. Hence, the inclusion of 'force majeure' clauses in nearly all construction contracts.

4. A week ago, at an emergency meeting of the OPEC's Joint Technical Committee, Russia refused to agree to the cartel's proposal to reduce production by an additional 600 000 barrels per day (bpd). Explaining Russia's position, Energy Minister Alexander Novak said that in order to make such a decision, it takes time to evaluate the effect of coronavirus on the oil market. It is really not yet clear how much the coronavirus will reduce global demand for crude oil. In February, amid the unfolding epidemic, OPEC lowered its demand growth forecast for 2020 by 230 000 bpd to 0.99 million bpd. The Oxford Institute for Energy Studies is more pessimistic: according to its estimates, in China alone, demand in Q1 2020 will decrease by at least 500 000 bpd.
5. WHO International Health Regulations, WHA 58.3, 2nd edn. World Health Organization, Geneva 2005.

A force majeure clause (in contrast to the doctrine of frustration) enables the parties to a contract to allocate the risk of an unforeseen event adversely affecting one party's ability to perform its contractual obligations on time or at all. The provisions of a well-drafted force majeure clause can often be considerably more sophisticated than the automatic discharge of obligations that may result from the application of the doctrine of frustration. For example, the parties may provide for obligations to be merely suspended for a given period (after the expiry of which discharge may occur) and may also set out detailed provisions regarding who is to retain the benefit of monies paid or work done under the contract, after the occurrence of the force majeure event.

A contract will be frustrated when a contractual obligation becomes incapable of being performed as the result of an intervening event or circumstance which makes any further performance radically different from that contemplated by the parties; Non haec in foedeva veni, in other words, "it is not this that I promised to do".

If a contract is frustrated, both parties are automatically discharged from any further obligation as at the date of frustration. Obligations accrued up to the time of frustration, such as payment for previous work, remain valid.

The common law doctrine of frustration generally operates to discharge a contract where a supervening event occurs (without the default of the parties concerned and for which the contract does not make sufficient provision) which results in performance of the contract being physically or commercially impossible, or the obligations under the contract being radically different to those originally undertaken. The doctrine normally operates within relatively narrow confines. It cannot usually be invoked merely to relieve a party from an imprudent commercial bargain, nor where the parties have foreseen the relevant event and provided for it in the contract.

Frustration is notoriously difficult to establish. The fact that the works may be more difficult or costly to carry out or deliver is unlikely to be sufficient. However, frustration may arise where the contract becomes illegal to perform or where the subject matter of the works is destroyed, e.g. because the COVID-19 requires and infected building to be demolished, such as a hospital wing.

For example, the doctrine of frustration may possibly be relied upon where an exhibition or event is cancelled, as a result of COVID-19. The cancellation of the exhibition[6] or event may "frustrate" the contract, if it can be said to have destroyed the "commercial purpose" of the contract.

At common law, frustration usually results in the contract concerned being brought to an end forthwith (and both parties being released from any further obligations). Provision for the possible recovery of money paid under certain contracts is made by the Law Amendment and Reform (Consolidation) Ordinance (modelled on the Law Reform (Frustrated Contracts) Act 1943 in the UK).

Is impossibility an excuse?

Certain jurisdictions, such as states in the USA take a pragmatic view of impossibility and may excuse performance of a contract if a party is unable to perform its obligations in the manner in which it contracted to by reason of external circumstances for which he is not responsible.

Under English law, the doctrine of impossibility is much narrower. Only in very limited circumstances, will English law excuse a party from performing its obligations under a contract because the agreed method of performance has become 'truly' impossible

6. As happened this week when the world's biggest mobile technology fair, Mobile World Congress in Barcelona was cancelled due to COVID-19 fears.

(not just difficult) or because the consequence of continuing the contract in the face of an unforeseen event would result in a party suffering an especially severe and unreasonable loss.

In any event, due to the ambiguity of the word 'war' many force majeure clauses now provide that a force majeure event will include "war, hostilities (whether war be declared or not)". In the event of a force majeure event occurring, a contract may typically provide that the contractor may suspend performance of the works or be discharged from carrying out further obligations under the contract.

What to do if an epidemic has affected your business

If a party believes that its obligations under a contract have been affected by COVID-19, it should first consider whether the contract includes a force majeure clause. If the contract contains no such clause, or if COVID-19 does not fall within the scope of the clause, a party may seek to rely on the doctrine of frustration to discharge the contract. Such reliance is only likely to be successful if the effect of COVID-19 can be shown to render performance of the contract impossible, or only possible in a very different way from that originally contemplated. Mere inconvenience, or hardship, or financial loss in performing the contract, or delay which is within the commercial risk undertaken by the parties, will usually be insufficient to frustrate a particular contract. Given the relatively narrow confines of the doctrine of frustration (at common law), now is an apt time to review the force majeure clauses (if any) in contracts pursuant to which parties conduct their businesses. Otherwise, contractual parties may be storing up problems for the future and without the comfort of knowing how long COVID-19 will last and whether or not it is a one-off event. Therefore do:

- Before any decision can be taken on whether force majeure or whether frustration applies the applicable law to be determined at first;
- Review and evaluate contractual clauses and the allocation of risk in any on-going contracts, particularly in relation to the consequences of conflict or pandemics;
- Review insurance provisions, both personal and works insurance;
- Check the provisions of your contracts to identify the entitlements that may arise in terms of extensions of time, additional cost and possibly suspension of the works;
- Put in place systems for recording delay and additional cost to the works by reason of the direct (and possibly indirect) consequences of the conflict, evidence proving force majeure event and/or frustrating event needs to be gathered (e.g. certificates issued by competent authorities and/or institutions);
- Ensure that any necessary contractual notices are provided on time. Procedural red tape, e.g. notification on force majeure event / frustrating event and respective requests (e.g. suspension, modification, termination of contract etc.) to be strictly followed;
- Evidence proving causation between such event and failure to perform / frustration of purpose to be marshalled;
- As a fallback, initiating a lawsuit or arbitral proceedings to be considered.

Watch this space!