



Focus

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COVID-19 Special Edition

COVID-19 - A Reason to Discharge Contractual Obligations?

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With the onset of the global public health emergency of coronavirus (COVID-19), supply chains continue to be disrupted and consumer spending has plummeted to unprecedented levels. As a result, businesses are looking at the possibility of having to deal with a cascade of defaults. Given such dire projections, a common question has been whether the current situation caused by the COVID-19 outbreak relieves parties from their contractual obligations.

How parties may discharge their contractual obligations

There is no case law directly on the operation of law in the context of pandemics. This may very well be the case since in recent history, Maldives has not had to grapple with a pandemic of such extent. However, some domestically decided cases

and English common law provide guidance on how businesses may discharge their contractual obligations in pandemic situations.

Parties seeking to discharge their contractual obligations as a result of the COVID-19 outbreak may do so by mainly two ways. That is either by invoking a force majeure clause or by relying on the doctrine of frustration.

What is force majeure?

There is no precise judicially accepted definition of the term 'force majeure'. Broadly speaking, force majeure events are unexpected events occurring beyond the contracting parties' reasonable control that prevents, hinders or delays the performance of their contractual obligations by reason of occurrence of that event.

Following in the footsteps of other common law jurisdictions, under Maldivian law it is likely that force majeure will not be regarded a standalone principle that relieves parties from their contractual obligations. In practice this means that parties can rely on force majeure as a defense only if a force majeure clause is expressly provided for in their contracts. Thus, care must be taken when defining the circumstances that constitute a force majeure.

Is COVID-19 outbreak a force majeure event?

It is likely that COVID-19's classification as a "pandemic" by the WHO¹, COVID-19 outbreak will constitute a force majeure event under contracts where it expressly accounts for "pandemics" as a force majeure event. Where a force majeure clause does not expressly refer to "pandemics", whether the outbreak of COVID-19 and its consequences can be regarded as a force majeure event depends on the wording of the relevant clause in the contract.

In response to COVID-19, both foreign and local governmental authorities have imposed various containment measures. Foreign governments are imposing travel restrictions and as a result it has forced several resorts and guesthouses to suspend their operations. Domestically, the government of the Maldives has placed several resorts under quarantine, suspended all dine-in, imposed travel bans and ordered closure of spas on local islands. Such government-enforced measures intended to slow the spread of the COVID-19 are expected to have a trickle-down effect on businesses' ability to fulfil their contractual obligations.

In the coming months, one major issue likely to be confronted by businesses may be shortages in the workforce as employees become unable to work due to sickness or as a result of placing themselves in quarantine. Apart from workforce shortages, businesses are already facing the difficulties of paying rent of their properties, issues with fulfilling loan obligations, and last-minute cancellations as consumer spending continues to fall. Businesses facing such ramifications as a result of the COVID-19 outbreak, therefore, may successfully invoke force majeure clauses.

What needs to be established to rely on force majeure clause?

The first step for any businesses seeking to rely on a force majeure clause is to determine whether your contracts have made provisions for force majeure clause and consider the wording of the clause to see whether COVID-19 outbreak is a force majeure event under the clause.

Even where COVID-19 outbreak constitutes a force majeure event under your contract, it does not automatically mean that the clause will be triggered by the impact of coronavirus. The party seeking to rely on the clause must establish the facts that bring the clause into play. This may require some level of legal interpretation and drawing similarities from case law. Engaging legal counsel at this stage may be crucial to put forward the best possible arguments.

Additionally, it must also be proven that performance has been prevented², hindered³ or delayed by reason of the outbreak.⁴ Case law

¹ Dr Tedros Adhanom Ghebreyesus, WHO Director-General, 'WHO Director-General's opening remarks at the media briefing on COVID-19' (WHO Director-General Speeches, WHO, 11 March 2020) <<https://www.who.int/dg/speeches/detail/who-director-general-s-opening-remarks-at-the-media-briefing-on-covid-19---11-march-2020>> accessed 22 March 2020

² *Thames Valley Power v Total Gas & Power* [2005] EWHC 2208 (Comm), [2005] All ER (D)

³ *Reardon Smith Line v Ministry of Agriculture, Fisheries and Food* [1961] 2 All ER 577

⁴ *Seadrill Ghana v Tullow Ghana* [2018] EWHC 1640 (Comm), [2019] 1 All ER (Comm) 34

suggests that this may mean that, even where the COVID-19 outbreak is found to be a force majeure event within the definition used in a clause, the party seeking to rely on the clause have to establish that the COVID-19 outbreak is the sole operative cause impacting the performance – rather than being a concurrent cause.⁵ Therefore, even where the COVID-19 outbreak falls within the definition of force majeure event used in a contract, it is important to check what triggered the clause.

When invoking force majeure clauses, a business must also ensure that, they have complied with the procedural requirements under the contract. This may include having to give notice to the other party of their intention to rely on the force majeure clause. If such procedural requirements are conditions precedents, a party may not be able to discharge their obligations unless the requirements are complied with.

No force majeure clause?

As aforementioned, to rely on force majeure, the contract must explicitly provide for force majeure clause. If there is no force majeure clause, affected parties must look for other provisions of the contract to consider whether there are any other potentially relevant alternative contractual provisions to a force majeure clause. For instance, it is common for contracts to expressly provide that exercise of statutory power by a government or a change in law entitles the contracting parties to certain reliefs, including additional time and/or termination.

Should there be no possibility of relying on any such contractual provisions, it may be possible for parties

to rely on the doctrine of frustration. Frustration of a contract takes place when upon the occurrence of a supervening unforeseeable event, performance as initially contemplated by the parties is impossible or has become a thing radically different from what was initially promised. Section 22 of the Law of Contract (Law Number 4/91) specifically provides for the doctrine of frustration.⁶

However, it is difficult to establish frustration. It is generally accepted that the doctrine of frustration is typically narrow in practice and interpreted strictly. Frustration cannot be invoked simply because performance has become difficult or expensive.⁷ Businesses in the catering industry and hospitality industry such as restaurants, hotels, guesthouses and resorts may, however, successfully argue that government-enforced lockdowns of their businesses, that were imposed to contain the outbreak were unforeseeable and owing to such lockdowns, performance of their contractual obligations have become impossible. In practice, therefore, some businesses may be able to discharge their contractual obligations by establishing frustration as a result of the COVID-19 pandemic.

Key Takeaways

As of yet, the situation continues to unfold and how courts will apply force majeure clauses and the doctrine of frustration to the current circumstances is up for question. What the COVID-19 outbreak has shown us is that potential business disruptions from a pandemic must not be underestimated. In order to prepare for the inevitable legal issues as a result of the COVID-19 outbreak, we recommend businesses to be proactive and move fast.

⁵ ibid

⁶ See also *Mohammed Waheed v Almaak Maldives Pvt Ltd* [2007/HC-A/183]

⁷ Law of Contract (Law Number 4/91), s 22(b), *Island Transport Private Limited v Hussain Aashir* [2006/HC-A/32], [f]

In that regard we suggest businesses to consider the following practical steps:

1. Carefully review all your existing contracts to determine whether provisions are made for force majeure clauses and whether any such clause expressly provides for 'pandemics' and/or 'epidemics'.
2. If a force majeure clause is incorporated into the contract but does not expressly provide for pandemics or epidemics, consider whether COVID-19 outbreak and its consequence constitute as a force majeure event under the general language of the clause.
3. Consider your reason for triggering the force majeure clause and whether the inability to perform is because the COVID-19 outbreak or its consequences prevented, hindered or delayed your performance.
4. Consider whether there are any notice provisions that must be complied with before invoking a force majeure clause and serve any such notices prior to invoking the clause.
5. Keep track of all documentary records, in particular, documents evidencing how performance was prevented, hindered, delayed or made impossible as a result of the COVID-19 outbreak.
6. Explore alternative routes either through, your insurance policies, the existing terms or by negotiation variations to existing terms to include a force majeure clause.

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