



COVID-19 AND FORCE MAJEURE CLAUSES

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The novel Coronavirus (COVID-19) was first reported in Wuhan, China, on December 31, 2019, and has been rapidly spreading since. Now the outbreak has been declared a pandemic by the World Health Organization (W.H.O). The extent to which specific events relating to COVID-19 trigger a particular force majeure clause is a matter of contractual interpretation, and will turn on the precise language of the clause and the factual circumstances of each case.

Generally, parties which are in default or are considering potential default under the provisions of a contract due to COVID-19 must consider the following:

1. Does COVID-19 qualify as a force majeure event in the party's particular situation under the force majeure clause?
2. Has COVID-19 impacted the party's ability to perform its obligations under the contract?
3. What effect does the force majeure clause have on the parties' contractual obligations?

What is Force Majeure?

At common law, contracting parties are required to perform their agreed-upon obligations. Excuses for non-performance exist; however, they are narrowly interpreted and applied. Contracts commonly include an express force majeure provision, which allocates the risk of non-performance or delayed performance. The terms of the force majeure clause read in their entire context are determinative, as there is no force majeure provision implied by common law.

The Supreme Court of Canada in *Atlantic Paper Stock* describes a force majeure clause as "generally [operating] to discharge a contracting party when a supervening, sometimes supernatural event, beyond control of either party, makes performance impossible. The common threat is that of the unexpected, something beyond reasonable human foresight and skill."^[1]

There are three main factors to consider when determining the applicability of a force majeure clause to COVID-19. First, it must be shown that COVID-19 and the events that have transpired in relation to it fall within the force majeure terms of the relevant contract. Second, it must be demonstrated that the force majeure event directly caused the non-performance or delay in execution of the contract. This includes considerations such as whether the product or resource is one that is currently manufactured in an area on lockdown, if there are suitable competing suppliers or replacement goods from other regions of the world, or whether the supplier has an obligation to seek supply elsewhere if supply out of a particular area is blocked. Lastly, understanding the extent of the relief granted from contractual obligations must be considered, and whether failure or delay is permitted of the underperforming supplier before the contract can be cancelled or damages begin to accrue.

Analysis of the Clause

A party that is seeking to rely on a force majeure clause for relief from contractual obligations needs to demonstrate that there are no reasonable alternative means to perform its obligation under the contract. Canadian courts have typically set a high threshold for application of a force majeure clause, often requiring a supervening or supernatural event *beyond the control* of either party, rendering performance *impossible*.

Determining whether the events that have occurred as a result of COVID-19 can fall within a force majeure provision is largely dependent upon the language of the clause. The following are phrases commonly used in a force majeure clause, and are analyzed as they relate to the current COVID-19 pandemic[2]:

“Public health emergency or communicable disease outbreak”

On January 30, 2020, W.H.O declared COVID-19 a public health emergency. Further, COVID-19 is a communicable disease. While COVID-19 preliminarily falls within this language, it still leaves the issue of causation and notice as it relates to the relevant contract.

“Pandemics or Epidemics”

COVID-19 has now been declared a pandemic by W.H.O. Again, fitting into a specified force majeure event is only the first step in the analysis, as causation and notice must be proven. Where “epidemic” or “pandemic” is not included in a force majeure clause, force majeure *may still apply* to COVID-19 if the definition includes open-ended or catch-all language, as discussed below.

“Quarantines”

The *Concise Oxford Dictionary*, 10th ed. defines “quarantine” as “a state, period or place of isolation for people or animals that have arrived from elsewhere or been exposed to contagious disease.” While many individuals affected by COVID-19 have and will be quarantined, the virus may not affect the supplier specifically and could affect the applicability of this clause to the current pandemic.

“Government or administrative action, such as a decision or order preventing or hindering performance; or changes in laws or regulations”

COVID-19 may trigger this language in a force majeure clause, especially if there is a state-imposed lockdown or government action where certain services can no longer be performed. Parties must confirm, however, whether the basis for non-performance is due to the virus itself, or whether the government action was imposed to *limit* the *impact* of the virus (i.e., limitations on transportation, quarantines, closures of premises).

“Failure of upstream suppliers”

COVID-19 may cause disruption in the upstream supply chain, and if the force majeure clause provides for upstream supplier defaults or delays, the impacted party may have an excuse for delayed performance while it finds another supplier.

“Other events beyond the reasonable control of a party”

Whether this broad catch-all language applies depends upon the language in the rest of the clause and the contract generally. Factors to consider are whether COVID-19 prevents, hinders, or delays performance, whether COVID-19 was foreseeable, and whether the contract was concluded before or after the first outbreak of COVID-19.

“Act of God”

Generally, an Act of God tends to refer to events that occur due to natural causes without any human intervention or an uncontrollable act of nature. Some sources are advising that the phrase (or other catch-all provisions) may cover outbreaks such as COVID-19; however, this determination is ultimately a question of fact depending upon the nature and context of the particular contract, language used in the relevant force majeure clause, and general provisions of the contract.

Even if the language of the force majeure clause applies, parties must further evaluate whether the clause protects both parties, or only one party is temporarily excused of its obligations. This issue is common in commercial leases, where the lessor is frequently protected by a force majeure clause, while the lessee is still obligated to pay rent. The lessee is then left with the common law defence of frustration, and the consequence is that the remedy is to void the contract rather than simply delay performance or payment of rent.

Impact Required

If a party establishes that COVID-19 falls within the contractual definition of the force majeure clause, it must also show that this force majeure event has impacted its ability to perform contractual obligations. In doing so, there are two factors to be considered: (1) what is the degree of impact on the party; and (2) was the force majeure event and its impact the definite cause of the party's failure to perform its contractual obligations? Further, notice of the triggering force majeure event must be provided.

Degree of Impact

In ***Atlantic Paper Stock***, the Supreme Court of Canada established that the event triggering a force majeure clause must strike at the root of the contract.[3] If the party, through the exercise of reasonable skill, can find trade markets or suppliers elsewhere, the event does not affect the contract with the

degree of impact required. In other words, the impact of the COVID-19 virus on the party must be so great that the commercial purpose of the contract is frustrated.

Cause of Failure to Perform

The force majeure event must be the event that is preventing a party from performing its obligations. A force majeure clause will generally require the impacted party to establish that COVID-19 has affected its performance to the extent required by the language of the contract, which usually entails that performance is either prevented, hindered, or delayed. If the impact claimed from COVID-19 involves inconveniences that the party would encounter in day to day business, such as temporary disruptions of consumer and supplier activities, it will be difficult for the party to invoke COVID-19 as a force majeure event.

Notice

Force majeure clauses typically contain written notice provisions to ensure certainty if a party wishes to invoke its right to rely on force majeure for non-performance or delayed performance. Failure to provide notice within the contractually specified time period may result in voidance of the party's force majeure rights.

Effect of Invoking Force Majeure

The effect of invoking the force majeure clause of a contract is negotiated prior to entering into the contract and typically requires that both parties follow certain procedure and establishes rights and obligations each party has upon invocation of the clause. These rights and obligations may include contract price changes, relief from performance of contractual obligations, partial excuse, or extension of time for obligations to achieve milestone dates.

Mitigation

Any party invoking force majeure has a duty to mitigate against the effect of the force majeure event itself, as well as the effect of the force majeure on the counterparty.[4] In other words, the party must do what is commercially reasonable and feasible to help limit the losses suffered by the other party to the contract. Although there may be additional costs arising from the force majeure event, this does not permit the supplier to pass the incremental costs onto its customer. As the British Columbia Supreme Court stated in *Domtar Inc v Univar Canada Ltd*, a force majeure provision is not a price escalation clause.[5]

Conclusion

To conclude, the enforceability of a force majeure clause as a result of COVID-19 is largely fact-dependent and contract-specific. Parties must consider any contracts which are potentially affected by this pandemic and have legal counsel review and analyze the relevant provisions and circumstances to determine whether non-performance or delay may be excused. The specific language of the force majeure clause, along with the related impact, notice and mitigation requirements, will all play important roles in triggering a force majeure provision.

[1] *Atlantic Paper Stock Ltd v St Anne-Nackawic Pulp & Paper Co*, [1976] 1 SCR 580 [*Atlantic Paper Stock*].

[2] Practical Law, *Commercial and Contract Law Implications of the COVID-19 Pandemic*, [https://ca.practicallaw.thomsonreuters.com/w-024-2932?transitionType=Default&contextData=\(sc.Default\)&firstPage=true&bhcp=1](https://ca.practicallaw.thomsonreuters.com/w-024-2932?transitionType=Default&contextData=(sc.Default)&firstPage=true&bhcp=1)

[3] *Ibid*, at para 4.

[4] 1996 CarswellAlta 642, [1996] 6 WWR 274.

[5] 2012 BCSC 510.

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