IS THE CORONAVIRUS THE END OF ALL CONTRACTS?

I INTRODUCTION

The coronavirus, or Covid-19, has been properly classified as a pandemic in Australia and around the world. Nations have gone into lockdown, some have slowly recovered while others are still struggling to contain the pandemic. Its impact on all industries will be long term and wide ranging. Within the legal profession, barristers have reported a substantial decrease in briefs,[1] while commercial law firms have had to undertake job cuts to cope with the fall in revenue, which was in turn a result of businesses collapsing.[2]

There is no doubt that this pandemic brings with it serious consequences for parties to commercial contracts. Not only does it put a halt on the economy with the suspension of the sale of goods and provision of services, it makes it impossible for parties to go about their business activities due to the lockdown of premises and the closure of international and state borders.

This paper focuses on the impact of this pandemic on pre-existing contractual obligations, in particular commercial contracts. The short point is that if a party to a contract is unable to perform their obligations under that contract due to the coronavirus, it will need to seek to be released from the contract without attracting damages or penalties. This paper argues that there are primarily two mechanisms by which that can be achieved: *force majeure* clause and the common law doctrine of frustration.

If the contract in question contains a *force majeure* clause, the primary issue is the scope of that *force majeure* clause. The task for the court is essentially one of interpreting a contractual provision. If the contract in question does not contain a *force majeure* clause, the common law doctrine of frustration may be relied on. The task for the court in that situation is to interpret and apply existing authorities pertaining to frustration.

The paper will be divided into two parts, the first focusing on *force majeure* clause and what businesses need to rely on such a clause in the context of the pandemic. The first part will place a heavy emphasis on English authorities as Kiefel J[3] observed that Australian courts have not traditionally endorsed the common law doctrine of *force majeure*.[4] The second part focuses on frustration and how the court may apply it to the factual circumstances of each case in the context of the pandemic.

II THE CONCEPT OF *FORCE MAJEURE* AND ITS ELEMENTS

Litigations centred around a *force majeure* clause typically involve four main questions:

- Is the event said to give rise to a failure to perform contractual obligations a *force majeure* event?

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1 Chip Le Grand, 'Barristers turn to other jobs, chambers empty, as pandemic hits legal profession', *The Age* (online, 5 July 2020) https://www.theage.com.au/national/victoria/barristers-turn-to-other-jobs-chambers-empty-as-pandemic-hits-legal-profession-20200703-p558vz.html.

2 Ann Davies, 'Deloitte cuts 700 jobs in Australia as coronavirus takes its toll on professional services', *The Guardian* (online, 22 June 2020) https://www.theguardian.com/australia-news/2020/jun/22/coronavirus-job-losses-hit-law-firms-accountants-and-other-professionals

3 As her Honour then was.

4 *Hyundai Merchant Marine Co Ltd v Dartbrook Coal (Sales) Pty Ltd* [2006] FCA 1324, [61] ('*Hyundai MM*').

- Did the *force majeure* event prevent or hinder the performance of contractual obligations?
- Was the event reasonably foreseeable at the time the contract was entered into?
- Did the party wishing to rely on the *force majeure* clause exercise reasonable skill and care?

A *What Is A Force Majeure Event?*

Force majeure literally translates to 'an act of God'. It is a common clause in commercial contracts which operates to release both parties from contractual obligations, which performance was prevented or made impossible by an event out of the parties' control. Whether or not parties to commercial contracts can rely on this type of clause to escape liability is a question of fact and is highly dependent on the wording of the clause itself.

The event the topic of this discussion is the outbreak of the coronavirus, more commonly referred to as Covid-19, or 'the pandemic'.

An issue that has no doubt arisen with many *force majeure* clauses in a standard commercial contract is that it rarely refers specifically to a pandemic of the nature of Covid-19. Most *force majeure* clauses refer to war, strike, obligation under the laws, natural disasters such as flood, storm or fire. While it may be easy to prove that the pandemic has resulted in stoppage of work, reduction in working hours due to government restrictions and lockdowns, it is the extra steps in the legal analysis which create uncertainties and obstacles that need to be overcome.

The parties may have stipulated the particular events which would trigger the clause itself, such as fire, flood, storm, liquidation of one party, death of one party etc. The application of a *force majeure* clause in that case is unambiguous. For instance, if the *force majeure* clause stipulates that a pandemic or epidemic is a *force majeure* event, then clearly the outbreak of the coronavirus would trigger that clause in a contract, one would be hard pressed to argue otherwise.

Even if the *force majeure* clause in question does not expressly provide for pandemic or epidemic, but instead has a catchall provision which states that 'and any other event outside the control of the parties', it is fairly obvious that no one could have prevented or control the spread of the coronavirus. In that sense, this pandemic can be said to resemble a natural disaster which occurrence cannot be predicted even with modern technology and human interference. This means that parties to contracts will not have much difficulty satisfying the court that the outbreak is a *force majeure* event.

B *Impact on performance*

The next issue is whether or not the pandemic can be said to prevent or hinder a party's performance of its contractual obligations.

The Macquarie Dictionary defines 'prevent' as follows:

> 1. To keep from occurring; hinder.
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> 2. To hinder (a person, etc.), as from doing something…[5]

The plain meaning of the word 'prevent' suggests that in order to show that performance is prevented by the pandemic, a party will need to prove that performance could not occur, or was made impossible. Impossible in this sense must be understood as having zero probability of occurring, as opposed to impractical or unlikely. In the current context, impossibility means performance is legally or physically impossible.[6]

Blackburn J said in *Taylor v Caldwell*:

> …where, from the nature of the contract, it appears that the parties must from the beginning have known that it could not be fulfilled unless when the time for the fulfilment of the contract arrived some particular specified thing continued to exist, so that, when entering into the contract, they must have contemplated such continuing existence as the foundation of what was to be done; there, in the absence of any express or implied warranty that the thing shall exist, the contract is not to be construed as a positive contract, but as subject to an implied condition that the parties shall be excused in case, before breach, *performance becomes impossible from the perishing of the thing without default of the contractor*.[7]

Taylor v Caldwell was about a concert hall that was destroyed by fire at the fault of neither party. The Court held that as the hall the subject of the contract ceased to exist, that rendered performance by both parties impossible. They must be excused from further performance of the contract, the plaintiff to pay the rent and the defendant to make the concert hall available for the plaintiff's use.

During World War I, many cases come before the English courts pertaining to the question of whether or not the outbreak of the war could constitute a *force majeure*. One of them was *Dynamit Actien-Gesellschaft v Rio Tinto Co Ltd*.[8] This case concerned a contract to deliver iron ore between two parties respectively based in Britain and Germany. There was a *force majeure* clause in the contract which stipulated that if an event outside the parties' control prevented the delivery or receipt of the ore, the parties are effectively released from further performance of the contract. The case was principally resolved by the public policy in Britain at the time that all executory contracts which benefit an enemy of the kingdom (Germany) are illegal and void as there was a war between Britain and Germany.[9]

However, Lord Atkinson was of the view that it was necessary to say in *obita* what the resolution of the matter would have been without the existence of the public policy. The contract in question required ore to be shipped from a port in Spain to Germany. When the war broke out, all carriage by sea or otherwise was rendered illegal. This included all shipment via sea or train carriage on land. Lord Atkinson held that the carriage of goods via these means was the basis of the contract, when made illegal by the war, constituted a complete breakdown of the contract. The very subject of the contract ie. delivery of goods between Spain and Germany ceased to exist because it was forbidden by law. The House of Lords held that performance was impossible.

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5 *Macquarie Dictionary* (online at 15 August 2020) 'prevent'.
6 *Channel Island Ferries Limited v Sealink UK Limited* [1988] 1 Lloyd's Rep 323 ('*Channel Island Ferries*').
7 [1863] EWHC QB J1.
8 [1918] AC 260.
9 Ibid 277.

Let us then consider this principle's application to the delivery of goods. The context of the contract is of crucial important. Victoria is currently in Stage 4 lockdown restrictions, which involves no movement outside of one's home between 8pm and 5am; no travel outside the 5km perimeter outside one's home and no travel at all unless to shop for essentials or seek medical help. The delivery of essential goods and services is exempt from these restrictions so I will focus on other non-essential goods and services.

If a contract provides for the delivery of non-essential services such as gyms, clubs, shopping centres, sporting events and beauty treatments, the timing of such service is essential to a contract. If one has a contract with a shopping centre to open from 9am-10pm every day to provide one of these services, performance of that obligation is impossible because with Stage 4 restrictions currently in place in Victoria, all of these venues must be closed. To remain open for those hours is a contravention of the Premier's directive and liable for a fine. The basis for such contract has disappeared because it has been rendered illegal by the Stage 4 restrictions. Participants to such contract can rely on the *force majeure* clause in their contract to avoid liability for breach of contract.

Different considerations apply for delivery of services which timing is not of the essence. Take for example contracts for consultancy services or evaluative reports. The main input for such services is intellectual, as opposed to physical work. It has become apparent that human resource driven industries such as consultancy can be very effectively delivered from home. The legal service industry has become virtual over the last few months, with the Supreme Court of Victoria conducting hearings online and lawyers participating in those hearings remotely. Similarly, accountants, consultants and university lecturers have taken their services online with most organisations now making working from home mandatory. The upshot is that if a contract relates to a service which could be done online and does not require the physical presence of a thing or a person, it is very difficult to argue non-performance due to the pandemic.

It is important to note that even with the strictest lockdown restrictions, such as Stage 4 currently in place in Victoria, the context and subject matter of the contract itself will determine whether or not a party can rely on a *force majeure* clause. There is no blanket exemption for all businesses to avoid liabilities under a contract in the midst of the pandemic.

1 *Impossible or merely difficult?*

I have so far presented some scenarios in which performance is impossible or very close to it. The question is then what happens if performance is not impossible but merely difficult, ie. if performance is much more expensive than originally contemplated by the parties and to the commercial detriment of the party owing the obligation. The below cases demonstrate such scenario.

Tennants (Lancashire) Ltd v C S Wilson & Co Ltd was also in the context of World War I.[10] The parties contracted for the supply of magnesium chloride. The outbreak of the war caused a shortage of raw material which increased the price of magnesium chloride. The defendant ceased supply to the plaintiff on the ground that it did not have sufficient stock to deliver to the plaintiff. The defendant had at the time several other contracts for supply to other merchants, which the defendant had given notice of non-delivery. Every other merchant accepted this except for the plaintiff. As a result, the defendant was left with enough stock to supply to the

[10] [1917] AC 495 ('*C S Wilson*').

plaintiff, but at an increased price. The plaintiff brought an action contending that it should only have to pay the original price in the contract.

On appeal to the House of Lords, the question was whether the war prevented or hindered the delivery of magnesium chloride to the plaintiff. The House of Lords held that a mere increase in price ie. unprofitability could not amount to 'hindering' delivery of the product. The mere fact that a party can escape performance of a contract because it has become uncommercial is not a sound legal principle.[11] Lord Loreburn was of the opinion that 'hindering' meant that the war must have presented obstacles which would be really difficult to overcome.[12] In order to demonstrate that delivery was hindered, it must be shown that it was impossible to fulfil the contract without completely dissolving the business of the party.[13] Lord Atkinson agreed and held that it was an accepted fact that if all other merchants had elected to enforce delivery from the defendant, it would have been impossible for the defendant to source enough magnesium chloride to fulfil all of those contracts. All those other merchants, by acquiescing to non-delivery, cannot be in a worse position than the plaintiff.[14] The shortage of magnesium chloride therefore made it very difficult, albeit impossible, for the defendant to fulfil its contractual obligations to all of its customers. Delivery to the plaintiff was in effect hindered by the shortage created by the war.[15]

In the above case, the House of Lords seemed to equate the notion of 'very difficult to perform' with 'impossible to perform', which is not helpful when the court is faced with situations where performance is not quite impossible but nevertheless very difficult. What is helpful is the principle that mere uncommerciality of performance of a contract does not excuse a party from breach. This notion has been adopted and applied in several Australian authorities.

In *Yara Nipro Pty Ltd v Interfert Australia Pty Ltd*,[16] Interfert contracted to supply fertilisers to Nipro at particular times of the year. Due to a failure by a third party to supply fertilisers to it, Interfert defaulted on its obligation under the contract to Nipro. Interfert relied on the *force majeure* clause in the contract, contending that the third party's failure to supply fertilisers to it constituted a *force majeure* within the meaning of the contract as it was beyond the control of Interfert and made delivery to Nipro impossible. This argument was rejected by the Queensland Court of Appeal as Interfert did not adduce any evidence to show that it could not source fertilisers from another party, in time or otherwise for the delivery to Nipro, nor did it seek to show that an alternative source of fertilisers would have increased the price it would have to charge Nipro. The Court held that in order for the third party's failure to perform its contract with Interfert to constitute a *force majeure*, the *force majeure* clause in the contract would have had to state with sufficient certainty that is the intention of the parties. The relevant clause could have stated, at the very least, the identity of the third party supplier, the maximum price at which the third party could charge Interfert in order for Interfert to in turn honour its obligation with Nipro, and contingencies should the particular third party fail to supply (as in this case).[17] It did not make business sense that Nipro would be willing to bear such a risk without inserting in the *force majeure* clause such details.

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11 Ibid 510.
12 Ibid.
13 Ibid.
14 Ibid 520.
15 Ibid 520 (Lord Dunedin agreeing at 516, Viscount Haldane agreeing at 512, Lord Shaw agreeing at 523, Lord Wrenbury agreeing at 526).
16 [2010] QCA 128 ('*Nipro*').
17 Ibid [31].

Hyundai MM concerns a maritime contract to charter coal between Australia and the Philippines.[18] At the same time that the defendants entered into the charter contract with the plaintiff, they were also negotiating the price at which they will sell coal to a prospective buyer. Negotiations broke down and no sale contract was entered into with a buyer. The defendants gave notice that it would not proceed with the charter contract as it could not find a buyer, which would accept the coal when it is delivered. The plaintiff alleged that the defendants wrongfully repudiated the charter contract, while the defendants contended that the charter contract was conditional upon a contract being entered into between the defendants and a buyer. The plaintiff sought damages and the defendants countered that the failure to find a buyer was a *force majeure* event within the meaning of that clause in the charter contract. Kiefel J held that that did not constitute a *force majeure* event because the defendants had a choice as to whether or not they could proceed with the charter contract, a choice that they chose not to take because it was not to their economic advantage.[19]

Analogous situations to this case are numerous in commercial litigation. Considering a contract which provides for the supply of a particular goods, the provider has always sourced this type of goods from overseas countries in which manufacturing and labour is cheap. The price stipulated in the contract reflects the low cost of the supplier's source. When Covid-19 necessitated the suspension of international flights, it is inevitable that low-cost goods can no longer be imported into Australia. There are two possible scenarios.

If the goods can be sourced from a domestic manufacturer, albeit at a much higher price, then performance of the contract is not impossible. It may be argued that it is difficult because performance of the contract will result in a loss to the party supplying the goods. Consistent with *Nipro*[20] and *Hyundai MM*[21], that argument is unlikely to sustain judicial scrutiny. The principle stated in *C S Wilson*[22] and cited in *Nipro*[23] and *Hyundai MM*[24], is that a party cannot resile from its contractual obligations merely because it can no longer derive the level of profit previously contemplated upon signing the contract.

On the other hand, if the goods cannot be sourced domestically and the only place from which the goods can be made has shut its border, it is arguable that performance has been made impossible by the outbreak.

A majority of Australian online retailers have been relying on Australia Post as its primary carrier. When most states and territories in Australia entered Stage 3 lockdown, Australia Post announced a number of changes to its operation. Apart from severe delay in service, it also temporarily suspended deliveries to many international destinations until further notice.[25] If a contract provides for the delivery of a particular goods to those destinations in which Australia Post no longer services, a party may argue that performance of such contract is impossible. A problem with this argument is that Australia Post, while a popular and cost-effective carrier in Australia, is not the only provider of postal service from Australia to overseas. DHL, Fedex and a number of international carriers are still servicing those destinations, albeit at a much higher price. The question is then of commerciality and the difficulty remains that absent other

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18 *Hyundai MM* (n 4).
19 Ibid [62].
20 n 16.
21 n 4.
22 n 10.
23 n16.
24 n 4.
25 The list can be found at https://auspost.com.au/about-us/news-media/important- updates/coronavirus/coronavirus-international-updates#international (accessed 11 August 2020).

factors, it is unlikely that the court will excuse a party from breach merely because it would be uncommercial for it to fulfill its obligations under the contract.

C *Foreseeability*

Even when a business can bring itself within a *force majeure* clause, either because the particular clause specifically lists pandemic as a *force majeure* event, or performance of the contractual obligation is plainly impossible with all the restrictions associated with Covid-19, foreseeability of the pandemic at the time of signing the contract may still bar a party from relief.

Asia Pacific Resources Pty Ltd v Forestry Tasmania (No 2) concerns a contract in which the defendant agreed to construct a flitch recovery mill and to supply the plaintiff with flitch log material by a certain date in a certain amount.[26] The contract provided for contingencies, or milestone, failure to achieve such milestone would entitle the parties to terminate the contract. The milestones included, amongst other things, approval for a plan of subdivision for the land on which the mill was to be constructed and the licenses necessary for the production of flitch log. As to the issue of foreseeability, Underwood J examined the relevant authorities from the UK and said:

> …more recent authority is to the effect that circumstances existing at the time the agreement is made may be relied upon to bring a party within the scope of a force majeure clause; it all depends on the proper construction of the clause in each case…there is no settled rule of construction that prevents a party to a force majeure clause from relying on events in existence at the time the contract is entered into as events beyond that party's control.[27]

Underwood J cited the judgment of Kerr J in *Trade and Transport Inc v Iino Kaiun Kaisha Ltd*[28] and accepted as correct the principles stated in that decision. On the question of whether or not a party is entitled to rely on circumstances in existence at the time of execution of the contract to terminate the contract, Kerr J held that it is always a question of the proper construction of the *force majeure* clause in each case.[29] However his Honour went on to state that a party is not entitled to rely on pre-existing circumstances at the time of the contract if:

(a) it was inevitable that the *force majeure* event would come to pass after the contract comes into existence; and

(b) the facts with show that the *force majeure* event would eventuate were known to the party seeking to rely on the *force majeure* clause, or 'if the existence of such facts should reasonably have been known to the party seeking to rely upon them and would have been expected by the other party to the contract to be so known'.[30]

Timing is of crucial importance when it comes to the degree of foreseeability of the events surrounding the coronavirus. This is because a different layer of restrictions comes into effect at different times and there is not a single date on which the known effect of the pandemic becomes virtually certain. Depending on the facts which are relied upon by a party to argue that a *force majeure* event has occurred, the determination of foreseeability will vary.

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26 [1998] TASSC 50.
27 Ibid 13-4.
28 [1973] 1 WLR 210 ('*Trade and Transport Inc*').
29 Ibid 227.
30 Ibid.

Looking at the timeline of the virus in Australia, it is clear that Australia was slow to experience the effect of the pandemic compared to the rest of the world. While Wuhan recorded its first case of 'novel virus' in early December, the World Health Organisation (WHO) was not notified until the start of January.[31] At this stage the virus was virtually unknown in Australia, it can be argued that for contracts executed at that time in Australia, the facts giving rise to the pandemic were not known to the parties. It would not have been reasonable to expect any contracting party to know that Australia would eventually shut its border and limit people's movement. A party to such contract is likely to be able to pass the foreseeability test.

Australia recorded its first four cases on January 25th.[32] Arrivals from China were officially banned from February 1st. The Australian government was starting to take action, however lockdown restrictions were yet to be an option. If a contract was executed around this time, and performance of such contract was not reliant on international flights operating at the usual frequency between China and Australia, then it is probably not reasonable to expect any party to foreshadow that a *force majeure* event would arise a few weeks later (complete closure of border). Foreseeability is not going to be an issue for this group of contracts.

On the other hand, if a contract was executed in this timeframe and performance is dependent on the movement of goods or people between Australia and China, the facts giving rise to a *force majeure* event are known or ought to have reasonably been known by the contracting parties. Applying the principle in *Trade and Transport Inc*,[33] those contracting parties would not be able to rely on the *force majeure* event clause because it was foreseeable that circumstances existing at the time of signing the contract would give rise to a *force majeure* event. The relevant circumstance is the ban on international arrival from China, from then it would have been reasonably foreseeable that further restrictions involving movement from China would eventuate.

By mid-March, arrivals from South Korea and Italy were banned. On March 13th, the Prime Minister announced the requirement for all international visitors to Australia to self-isolate for 14 days and a precaution to Australians not to travel overseas.[34] This was precipitated by the rapidly increasing number of cases in Australia. Stricter restrictions were almost inevitable as the nation grapples to control the outspread of the virus. Businesses would have been keenly aware of what the stricter restrictions are and the impact that would have on their capacity to fulfil any contract. Parties who enter into contract at this time cannot reasonably argue that they could not have predicted the closure of Australia's border, restrictions to essential services and total shutdown of non-essential services. The fact that Australia did not officially close its border until March 19th is not to the point, neither is the fact that most states did not enter Stage 3 restrictions until late March. The point is that by mid-March, it should have been clear to all those contemplating a contract that business as usual would not last much longer.

D *Reasonable Endeavour to Mitigate*

The final hurdle to a party seeking to rely on a *force majeure* clause is to show that it has taken reasonable steps to prevent non-performance of the contract. The concept of mitigation in

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31 Caroline Kantis, Samantha Kiernan and Jason Socrates Bardi, 'Updated: Timeline of the Coronavirus', *Think Global Health* (online, 27 July 2020) https://www.thinkglobalhealth.org/article/updated-timeline-coronavirus.

32 Inga Ting and Alex Palmer, 'One hundred days of the coronavirus crisis', *ABC News* (online, 5 May 2020) https://www.abc.net.au/news/2020-05-04/charting-100-days-of-the-coronavirus-crisis-in-australia/12197884?nw=0.

33 n 28.

34 Ibid.

relation to negligence has warranted significant judicial attention in Australia. However in this essay I wish to be more precise and focus on the concept as it pertains to a *force majeure* clause.

Channel Island Ferries concerns a cargo contract between two shipping companies operating in the same ports.[35] Both operations were apparently loss making. The contract was entered into with the intention to combine the vessels owned by each company in order to cut costs. This led to redundancy across the two companies. Upon signing the contract and announcement to the union, a strike ensued which resulted in unavailability of a number of vessels for service, two of them the subject of the proceeding. The question on appeal was whether or not the defendant had taken reasonable steps to secure alternative vessels in order to perform its obligation under an existing charter. It pleaded that the strike was a *force majeure* event, which resulted in workers staying on the vessels and stopping them from being used by the company. Ralph Gibson LJ, with whom Parker LJ agreed, stated the principle as follows:

> …in order to establish a force majeure situation it was incumbent on [the defendant] to prove:
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> (i) that the non-fulfilment of the obligation to bareboat charter the two first choice vessels was due to circumstances beyond [the defendant]'s control; and
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> (ii) that [the defendant] had to show that *there were no reasonable steps they could have taken* to avoid or mitigate the strike and its consequences.[36]

It was common ground at the trial that the defendant did not consider itself obligated to source alternative vessel and therefore did not take any steps to secure vessels from elsewhere in order to fulfil its obligation under the charter. The Court held that as the defendant failed to take reasonable steps to secure performance of its contractual obligations, it could not rely on the *force majeure* clause.

This principle was accepted as correct by the Court in *Seadrill Ghana Operations Ltd v Tullow Ghana Ltd*.[37] *Seadrill Ghana* concerns a contract to hire a drilling equipment which was needed for a number of oil wells off the Coast of Ghana. Under the contract, the defendant was to pay a daily hiring fee for the use of the equipment, which had been paid up until the Ghana government was involved in a United Nations dispute with another country, which necessitated the suspension of some wells. The defendant stopped paying the daily hiring fee on the ground that the intervention by the Ghana government was a *force majeure* event.

Teare J held that the government intervention could not constitute a *force majeure* event and found in the plaintiff's favour. However his Honour went on to consider the reasonable endeavour issue and stated that once a *force majeure* event has occurred, there is an obligation on both parties to use reasonable endeavours to 'ensure that the *force majeure* does not prevent them from performing their obligations under the contract or, if it does, to ensure that the effect of the *force majeure* is mitigated'.[38] His Honour further said:

> As a matter of language 'reasonable endeavours' is a phrase which enables account to be taken of all matters which bear upon the question whether it is reasonable to expect a party to take certain steps to avoid or circumvent a force majeure. There is no reason to exclude the absence of a business case or Tullow's commercial interests from those matters which may be taken into account. However, the extent

35 n 6.
36 Emphasis added.
37 [2018] 2 CLC 191 ('*Seadrill Ghana*').
38 Ibid 214.

> to which such matters may be taken into account and whether they are determinative will depend upon the contractual context in which the phrase is used.[39]

Teare J then applied the test stated by Rose J in *Minerva (Wandsworth) Ltd v Greenland Ram (London) Limited:*

> The question to be asked is what would a reasonable and prudent person acting properly in their own commercial interest and applying their minds to their contractual obligation have done to try to obtain the planning permission. In considering what steps were reasonable, the court has also to consider *whether any steps would have been successful*. If the party can show that it would have been *useless* for it to have taken those steps because they would not have been sufficient to achieve success.[40]

I now turn to the example stated earlier about a seller who is unable to supply a type of goods because those goods can only be manufactured in China and due to restrictions to international flights between China and Australia, cannot import those goods in order to fulfil its obligations under the supply contract. Assuming that it was able to satisfy the court that the closure of Australia's border was a *force majeure* event, importing the goods was impossible and the contract was entered into before the first case was reported in China, it would still have to show that there were no reasonable steps it would have taken to import the goods from China to Australia or to ensure that its customer would receive the goods from elsewhere.

Teare J was of the opinion that the party's commercial interest can be taken into consideration, but the extent to which it can be taken into account depends on each case on its own facts. For instance if the seller was able to source the goods from a domestic source but at a slightly higher price such that it would still be able to make a profit, then the seller is obligated to take such step and source the goods from elsewhere in Australia and deliver it to its buyer. If it had refused to source the goods elsewhere and purported to terminate the supply contract, it is likely that the court would not find in its favour because it had not taken reasonable endeavour to minimise the effect of the pandemic. If, on the other hand, sourcing the goods domestically would have cost the seller significantly more than the value of the contract, it may be argued that it is not reasonable to expect the seller to source the goods domestically so that it can deliver the goods to the buyer.

Rose J in *Minerva* posed the hypothetical question of whether or not such step would have been sufficient to mitigate the loss resulting from the *force majeure* event. Applying this to the situation where a contract provides for the delivery of goods to an international destination within a specified time frame, lockdown restrictions and social distancing measures would result in slower processing time by Australia Post and delayed delivery. As time is of the essence to such contract, using Australia Post would result in a breach. A party purporting to rely on the *force majeure* clause to terminate the contract would be required to show that even if it had used another provider, such as DHL or Fedex, it would still miss the delivery timeframe set out in the contract. If lockdown restrictions are such that no other carrier could have achieved the delivery timeframe in the contract, then any attempt to find another carrier would have been futile. Non-performance of the contract would occur in either scenario.

III FRUSTRATION

I have so far only considered contracts which expressly provide for what would happen in the event that performance becomes impossible. *Force majeure* is a commercial construct, meaning that if the contract in question does not have a *force majeure* clause, the court will not

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[39] Ibid.

[40] [2017] EWHC 1457 (Ch), [255] ('*Minerva*') (emphasis added).

imply it. In such cases, the common law doctrine of frustration may be of assistance to contracting parties.

It is strictly not correct to say that the doctrine of frustration can be used as a fallback argument should the *force majeure* argument fail. The doctrine of frustration can rarely be used as an alternative in a contract that contains a *force majeure* clause. The genesis of a frustration argument is that something has occurred which has rendered performance of the contract something the parties did not foresee and therefore did not provide for in the contract. The very fact that the contract has a *force majeure* clause means that the parties did in fact foresee the event which is now said to affect performance and have provided for what to happen in such situation. If the party fails to bring itself within the *force majeure* clause, it is unlikely that it can rely on the doctrine of frustration.

It is also important to note another key difference between the two concepts. A *force majeure* clause excuses a party from further performance of the contract and sets out what would happen in that situation. It governs the risk between the parties if the contract cannot be fulfilled. A frustrated contract terminates the contract at the time of the frustrating event. A frustrated contract is not void *ab initio*, only *in futuro*, which means that only future obligations are excused, obligations which were due before the frustrating event are still binding on the parties. In a frustrated contract, the risk lies where it falls. This is why some states have enacted legislation to mitigate the harshness of such consequences.[41]

The leading authority on the doctrine of frustration is *Codelfa Construction Pty Ltd v State Rail Authority (NSW)*.[42] Codelfa Construction entered into a contract with the State Rail Authority ('SRA') to construct a railway. Due to the noise violation and the resulting court injunction, Codelfa Construction had to adjust its working hours and incurred additional costs. Before the High Court, it maintained that the contract had been frustrated by the requirement for it to work different hours to those contemplated by the contract. Mason J[43] stated the question as 'whether the performance of the contract in the new situation was fundamentally different from performance in the situation contemplated by the contract'.[44] His Honour, with whom Stephen, Aickin and Wilson JJ agreed, held that the restriction imposed by the injunction, from three shifts a day over six days a week to two shifts a day, was radically different from that contemplated by the contract.

This test has subsequently been applied on numerous occasions; indeed its correctness is not in doubt. However, as Nettle JA[45] said:

> …frustration is a 'flexible doctrine', unconstricted by 'arbitrary formula' which is 'apt to vindicate justice wherever owing to relevant supervening circumstances the enforcement of any contractual arrangement in its literal terms would produce injustice' and 'to give effect to the demands of justice, to achieve what is reasonable and fair and as an expedient to escape from injustice…'[46]

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41 See for example the *Frustrated Contracts Act 1978* (NSW); *Frustrated Contracts Act 1988* (SA); *Frustrated Contracts Act 1959* (Vic) (repealed).

42 (1982) 149 CLR 337 ('*Codelfa*').

43 As his Honour then was.

44 *Codelfa* (n 42) 362.

45 As his Honour then was.

46 *Ooh! Media Roadside Pty Ltd (formerly Power Panels Pty Ltd) v Diamond Wheels Pty Ltd* [2011] VSCA 116, [65] ('*Ooh Media*'), citing *Cricklewood Property and Investment Trust Ltd v Leighton's Investment Trust Ltd* [1945] AC 221, 241 (Lord Wright); *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675, 700 (Lord Simon of Glaisdale); *Edwinton Commercial Corporation & Anor v Tsavliris Russ (Worldwide Salvage & Towage Ltd*

His Honour went on to say:

> One difficulty with general conceptions of that kind is that they do not provide much guidance as to the degree or extent an event must overturn expectations, or affect the foundation upon which the parties contracted, or how unjust and unreasonable a result must follow, or how radically different from that originally undertaken must a contract become, before the contract is taken to be frustrated.[47]

Nettle JA then instilled the following elements which his Honour considered consistent with Mason J's statements in *Codelfa*:

> …a contract is not frustrated unless a supervening event:
>
> a) confounds a mistaken common assumption that some particular thing or state of affairs essential to the performance of the contract will continue to exist or be available, neither party undertaking responsibility in that regard; and
>
> b) in so doing has the effect that, without default of either party, a contractual obligation becomes incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract.[48]

In considering the doctrine of frustration, it is clear that in every case the court will look to the contract in question, the underlying goods or services that the parties have bargained for and how performance has been affected by the frustrating event. The following analysis seeks to address the criteria that will need to be satisfied if frustration is to be made out.

A *Foreseeability*

Ooh Media concerns a licencing agreement in which the licensee paid for the use of the licensor's building for displaying promotional material in a corner of the Melbourne CBD. A year down the track, the construction for a residential building began which substantially obstructed the licensee's display, resulting in a reduction in the licensee's revenue. The licensee purported to repudiate the licencing agreement. One of the issues on appeal was whether the contract was frustrated by the construction of the new building.

On this issue, Nettle JA made the distinction between 'foreseeable' and 'foreseen'. His Honour was of the opinion that if an event was not only foreseeable but actually foreseen at the time of contract, it would be very difficult for one of the parties to now contend that it had entered into the contract under the assumption that that event could not occur for the duration of the contract.[49] If, however, an event was foreseen at the time of the contract but the degree of foreseeability is not very high, then the case for frustration is stronger. Similarly, the parties may have foreseen the event now said to frustrate the contract, but not the nature or extent of such event.

The Court ultimately found that the construction of the building which obstructed the line of visual to the display was foreseeable with a high degree of certainty at the time of the contract, or at the very least it was a 'real possibility'.[50] There was undisputed evidence that the skyline in that part of the CBD had changed significantly over a very short time span when the licensing

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(The 'Sea Angel') [2007] 2 Lloyd's Rep 517, 532 [86]; *J Lauritzen AS v Wijsmuller BV (The Super Servant Two)* [1990] 1 Loyd's Rep 1, 8 (Bingham LJ).

47 Ibid [66].

48 Ibid [70].

49 Ibid [72], citing *Maritime National Fish Ltd v Ocean Trawlers Ltd* [1935] AC 524, 529 (Lord Wright).

50 Ibid [80].

agreement was entered into.[51] It was common knowledge within the advertising industry that visibility of display panels within that part of the CBD would be impeded in a number of ways due to the speed at which buildings were being developed in that area.

Similar to the foreseeability analysis under *force majeure*, the degree of foreseeability of the pandemic will vary depending on when the contract was entered into. If the contract was entered into prior to 2020, it is arguable that the impact of the pandemic (lockdown restrictions etc) was not a 'real' or substantial possibility. However, if the contract was entered into around March of 2020, then it is likely the court may find that it is reasonably foreseeable that the pandemic would come to its full force in Australia and the resulting restrictions would have an impact on performance of contractual obligations.

B *Performance Which Has Become Radically Different from What The Contract Contemplated*

I now turn to the issue of whether or not performance of a contract can be considered 'radically different' from that which was provided for by the contract.

In *Ardee Pty Ltd v Collex Pty Ltd*, Palmer J considered the question of whether a deed of put and call options was frustrated by a series of events.[52] The deed entitled Ardee to a put option and Collex to a call option, which means upon satisfaction of certain conditions, Collex would buy a parcel of land owned by Ardee. Collex was a foreign owned entity and therefore needed approval from the Foreign Investment Review Board. The Board granted its approval on the condition that Collex would proceed with its proposal of a waste management facility. This waste management facility however needed a permit from the Minister for Urban Affairs and Planning, which permit was refused. Ardee instituted proceeding to enforce the put option. Collex contended that the deed had been frustrated by the Minister's refusal of the permit.

Adopting the test in *Codelfa*, Palmer J stated that the question was whether performance of the deed was radically different from that contemplated by the parties when signing the contract. His Honour held that it was, because if Collex were to exercise its call option, it would need to do something else with the land, other than a waste management facility. Collex would then contravene the conditional approval by the Board and be liable of an offence. This, Palmer J found, was radically different from that contemplated by the parties. There was ample evidence at the trial that the intention of the parties at all times was for Collex to conduct a waste management site on the land.

In coming to that conclusion, Palmer J made some helpful observations in relation to frustration of contract:

a) the fact that parties actually foreshadow the possibility of a particular frustrating event and make some provisions for it in the contract does not mean that the contract cannot be frustrated if the event occurs. The real question is whether or not the contract provided for what is to happen in the event that has actually occurred;[53]

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51 Ibid [76].
52 [2001] NSWSC 836.
53 Ibid [44].

b) discharge of a contract by frustration does not depend on the choice or election of the parties;[54]

c) an event prohibiting performance of some aspects of a contract does not necessarily frustrate the whole contract. The question of whether such event frustrates the whole contract depends on whether the event has defeated the main purpose of the contract;[55]

d) If the portion of the contract which has been frustrated is severable from the whole contract, then the rest of the contract (the part that is still performable) remains on foot;[56]

In *Veremu Ptd Ltd v Ezishop.Net Pty Ltd*, the New South Wales Court of Appeal considered the situation of shareholders who agreed to subscribe for shares in Ezishop which shortly afterwards went into liquidation.[57] Giles JA stated that:

> ...the task of the court is to determine on the true construction of the terms of the contract, read in the light of its nature and relevant surrounding circumstances, whether the contract is wide enough to apply to the new situation.[58]

Ezishop.Net Ptd Ltd was in financial difficulty and its existing shareholders resolved to inject more capital in exchange for the issuance of shares. After partial payment was received but before the shares were issued, Ezishop went into liquidation. On appeal, the buyers contended that they were not obligated to pay the remainder of the capital injection because the share agreement had been frustrated by the liquidation, that the value of their shares now after liquidation is drastically different from what they contemplated the value would be, had Ezishop not gone into liquidation. Ezishop argued that at all times it was ready and willing to issue the shares so it cannot be said that the contract had been frustrated.

Giles JA, with whom Handley and Santow JJA agreed, held that the share agreement had not been frustrated. His Honour stated that a share is a bundle of rights and obligations. The fact that Ezishop was in liquidation did not affect the rights and obligations attached to the shares the buyers were to obtain. If things had gone well, maybe the buyers would have received some dividend in due course, but the fact that they did not does not render the shares radically different to what the buyers contemplated.[59]

Ezishop is particularly relevant in the current context because due to the pandemic, many companies have run into financial strife and more are in administration or liquidation. *Ezishop* demonstrates the importance of determining precisely what goods or services underpin a contract. The contract in *Ezishop* was for shares, which represented 'a bundle of rights and obligations'. Similarly, if one was buying shares in a company with the hope of receiving some dividends, the fact that the pandemic rendered the company insolvent does not necessarily mean that one can avoid his/her future obligations under the share agreement.

The situation might be different if the contract relates to an investment fund, in which one party periodically contributes money in exchange for future returns. If the fund fails as a result of financial downturn due to the pandemic, the investor has two options. He/she can treat the

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54 Ibid [53].
55 Ibid [55].
56 Ibid.
57 [2003] NSWCA 317 ('*Ezishop*').
58 Ibid [3], citing *Davis Contractors Ltd v Fareham Urban District Council* (1956) AC 696.
59 Ibid [21].

fund's failure to generate returns as repudiation of the contract, terminate the contract and make a claim for damages. However, if the fund's manager insists on enforcing the rest of the contract, being future payments into the fund, the investor can argue that the contract has been frustrated by the fund's performance and the investor is freed of future obligations under the contract.

Ross & Anor v IceTV[60] also concerned a company in financial difficulty. After being made redundant, two of IceTV's senior directors operated another company in breach of the restraint of trade clause in their employment contract. At the time of signing the contract, the directors were given options and bonuses if the company went public. After a major legal dispute with Channel 9, IceTV became financially troubled and thus the public float was no longer possible. The directors argued that as the public float was no longer possible, the employment contract had been frustrated and so they were no longer bound by the non-competition clause.

After citing the principles as stated in *Codelfa* and *Ezishop*, Sackville AJA held that IceTV's failure of going public did not frustrate the employment contract. This is because each director continued to have rights and responsibilities above and beyond the event of IceTV's going public.[61] Furthermore, his Honour said, frustration could only occur if taken as a whole, the contract could not be said to be broad enough to apply to the event of the company not going public. The employment contract made the public float a condition for the directors' options and bonuses, which means that it clearly contemplated the very event which the directors now said amounted to frustration.[62]

Analogous situations to *IceTV* can arise in the context of the pandemic. If a contract provides for repeat delivery of goods and one delivery cannot occur because of lockdown restrictions, the subsequent deliveries, if not affected by the lockdown, will need to be performed. Consistent with the reasoning in *IceTV*, the delivery contract is not frustrated. The provision of periodic delivery, one after the other, clearly accounts for the subsequent deliveries to occur even if one fails. The deliveries can happen independently of one another.

C *The Importance of Identifying The Frustrating Event*

What has crystallised over time in the way that courts have applied the doctrine of frustration is the importance of identifying exactly what the frustrating event is. This is particularly relevant in the context of the pandemic. It is evident that in some cases simply saying the pandemic has frustrated the contract is not sufficient. The pandemic is associated with many circumstances, any one of which could be said to frustrate one type of contract but not another. Any of the following can be said to be the result of the pandemic:

- Prohibition of public gathering of more than 5 people
- Restriction in people movement ie. people can only leave their residence for essential services (getting food, medical care or work which cannot be performed at home)
- Closure of international/state border
- Reduction in flights to and from Australia

60 [2010] NSWCA 272.
61 Ibid [75].
62 Ibid [77].

The above circumstances can affect contracts directly or indirectly. If a contract provides for the holding of a public event such as a concert or a sporting event, the prohibition of public gathering of any size would no doubt frustrate the performance of any such contract, or at the very least render performance something very different from that which was envisaged by the parties. This is a direct consequence of the restrictions caused by the pandemic.

If however, the contract in question is a loan agreement in which a party has failed to make repayments, the analysis is not so simple. Situations can arise where a party whose business is the organisation of outdoor public events, which would no doubt experience liquidity problem if all public events are prohibited. If this business then fails to make repayments under a loan agreement, the argument that the loan agreement has been frustrated due to the pandemic may be difficult to sustain. The question which will be posed by the court is whether or not the event said to have frustrated the contract (the pandemic or ban on public gathering) has rendered the obligation to make repayments something which is fundamentally different from what was contemplated by the loan agreement. Can it really be said that failure to make a repayment due to the payer's financial difficulty is not contemplated by a typical loan agreement? The answer is in the negative. A standard loan agreement often provides for such situation by having penalty clauses which provide for a penalty interest rate or a late payment fee. In fact, liquidity problem on the part of the party obligated to make repayments is almost always contemplated by financiers, evidenced by penalty clauses in virtually all financing agreements. It is almost certain that a party failing to honour its repayment obligation would not be able to rely on the pandemic as a frustrating event, without some other vitiating factors.

Similar situations can arise if the closure of international border is said to be the frustrating event. If the contract in question pertains to the delivery of goods to or from Australia, the suspension of international flights would certainly qualify as a frustrating event as it is a direct consequence of the pandemic's restrictions. However, different considerations apply if the relationship between the underlying contract and the closure of international border is more remote. For example, a contract may provide for the manufacturing of a product. The product is comprised of many parts, one of which is sourced from outside Australia. In order to perform its part of the contract, the manufacturer would have to source the missing part domestically. The question is whether or not performance in this manner is so different from what the parties contemplated that the contract ought to have been frustrated. The answer again is in the negative. It is reasonable to expect a manufacturer of a product which is made up of many parts to encounter problem with finding one part or another. It would be prudent, if not necessary, to have a clause in the contract with provides for that situation.

IV CONCLUSION

This paper has considered the two legal pathways in which commercial parties can deal with existing contractual obligations in the wake of Covid-19.

If the contract in question has a *force majeure* clause, a party defaulting on its obligation can argue that the pandemic qualifies as a *force majeure* event and obtain relief provided in that clause, which was what the parties agreed upon when signing the contract.

If the contract does not have a *force majeure* clause, the defaulting party may rely on the common law doctrine of frustration in order to avoid the remainder of the contract.

It is important to note, as demonstrated by previous authorities on the elements of *force majeure* clause and the doctrine of frustration, that the court's analysis is always fact-based, which

means that each case is determined on its own factual circumstances. As extraordinary as the pandemic and its consequences have been, there is no certainty that every *force majeure* clause will be triggered and all commercial contracts will be frustrated. The same factual circumstances associated with one restriction may frustrate one type of contract but not others. A particular *force majeure* clause may operate to relieve the parties of one contract, but in a different contract the *force majeure* clause may not apply.

Businesses should always exercise due care and diligence in navigating their contractual obligations, especially in uncertain time such as one we are in.

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