Haavind

HANDLING THE CORONAVIRUS AND COVID-19 PANDEMIC IN CONTRACTS

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1. Introduction

On 30 January 2020, the World Health Organization (the "WHO") declared the outbreak of the novel coronavirus (Covid-19) a Public Health Emergency of International Concern ("PHEIC"), and 11 March 2020, it defined the situation as a pandemic. The outbreak and the subsequent measures imposed by local and national governments in many countries severely effected by the outbreak, is causing disruption to delivery of goods and services and other commercial relationships. The adverse effects include prevention of following-up contracts (e.g. performance of site-visits), prevention from access to sites (due to travel restrictions and quarantine requirements) and delayed delivery of goods from vendors and subcontractors and delayed performance of services (due to i.a. lack of personnel caused by travel restrictions, quarantine requirements, sick-leave and the need for parents to be home with children due to closure of schools and kindergartens).

Parties who are or may be unable to perform their obligations as a result of the pandemic may find a means of suspending their performance or exiting a contract, or a defence from liability via force majeure clauses in their contracts or under statutory provisions.

Considering the current situation in Norway, the outbreak of the coronavirus will generally be considered a force majeure event. The same will apply to associated measures implemented by governments, municipals and other officials. However, note that the assessment of what constitutes a force majeure situation may be different under various jurisdictions (countries).

Some general principles will apply:

Notification: Most contracts include strict notification requirements that must be complied with to preserve rights under force majeure provisions.

Documentation: It is of utmost importance to make sure to gather relevant documentation and keep a detailed time line as the party invoking force majeure under a contract bears the burden of proof of being prevented by a force majeure event and the actual impacts of the hindrance.

Cessation of force majeure: The relevant contract provisions related to cessation of a force majeure event must be reviewed. Most contracts impose obligations to notify the other party of any claims for schedule impact or other remedies when the force majeure event ceases.

Norwegian law, and several other civil law jurisdictions (e.g. most of the European countries, except for UK), recognizes force majeure both as a statutory provision and as a contract term concerning relief from contractual obligations. Under most common law systems (e.g. under English law), the courts will not imply a force majeure clause unless such a clause is included in the contract. However, certain other common law doctrines may provide access to defences against liability for the failure to perform under a contract.

Force majeure is traditionally defined as an occurrence that prevents fulfilment of a contractual obligation. The occurrence must be beyond the control of the affected party. Further, under most contracts and civil law systems it is required that the party could not reasonably have foreseen the occurrence when entering into the contract and could not reasonably have avoided or overcome it and its consequences. Traditional examples of force majeure events include war, insurrection, riots, invasions, blockades, earthquakes, extreme weather, fires, strikes, lock-outs and similar serious intervening events that are outside the control of the contracting parties.

Whether or not an event is considered a force majeure event, will ultimately depend on the interpretation of the relevant contract clause if such is included. Concerning statutory force majeure, the conditions that must be fulfilled are defined in statutory law, e.g. in the Norwegian Sale of Goods Act of 1988 if the contract is subject for Norwegian law, which again follows the provisions of CISG (United Nations Convention on Contracts for the International Sale of Goods) closely.

The Norwegian Sale of Goods Act of 1988, especially in the sections 27, 40 and 57, introduces the concept of "control liability". This is in effect a strict liability for a party's fulfilment of those contractual obligations that lie within the "control" of the party. Force majeure occurs when the fulfilment of a contractual obligation is prevented by circumstances outside the control of the party.

For contracts that include force majeure provisions, the contract determines both what constitutes a force majeure event, the effects of the force majeure event, and the parties' obligations in relation to the event. It is therefore always important to examine the relevant contract.

For an event to be considered as force majeure it is relevant under both Norwegian background law and most contracts, if and to what extent the impacts of the event could reasonably be expected to be overcome or mitigated. Under the current situation, it is not always easy to find efficient and reasonable measures. However, the parties should always consider its options and possibilities. It may inter alia be a reasonable measure to reduce activity (e.g. to limit the risk of further transmission of the virus and thereby avoid being forced to implement quarantine restrictions) at an early stage to prevent that the work under the contract stops completely. It may also be reasonable to consider different rotation schemes etc. to solve a manning risk or a problem caused by restrictions on mobilisation. Another possibly reasonable alternative may be to look for possible changes in the planned sequence of activities or other ways of doing things to keep some progress under the contract, although this may not be the most cost-efficient solution.

It will always be a question of where the limit for what a party is obliged to offer or implement. The guideline will be that it is not reasonable to expect measure that is disproportionate expensive or burdensome to implement compared with the likely effect achieved (losses saved) or with the agreed risk distribution in the contract.

When force majeure occurs, the main effect is normally that the party's obligations under the contract are suspended as long as performance is prevented by the force majeure event. I.e., a party might be entitled to claim relief from its responsibilities and liabilities under the contract to the extent its failure to perform is caused by force majeure (and could not have been overcome by reasonable measures). Under certain circumstances, e.g. in case of fulfilment being prevented by force majeure for a certain period of time, contracts may also provide basis for exiting the contract. However, it is uncommon that force majeure provisions provides for a direct and immediate exit right.

In the following, we address possible effects of the coronavirus outbreak under commercial contracts for the supply of goods or services, and recommendations on how to handle these issues, both towards customers and towards contractors or sub-contractors.

2. Does outbreak of the coronavirus constitute force majeure?

Whether the outbreak of the coronavirus constitutes a force majeure event must be determined based on a case-by-case interpretation of the relevant force majeure provisions in the contract. The interpretation may also be affected by the relevant background law. Generally, there are four conditions that must be fulfilled:

I. The event is beyond the control of the parties;

II. The event prevents fulfilment of contractual obligations;

III. The event could not reasonably have been foreseen at the time of entering into the contract; and

IV. The effects of the event cannot reasonably be overcome or mitigated.

If the definition of force majeure in the contract explicitly includes "pandemics" or similar listed events, it is obviously likely to be triggered by the outbreak of the coronavirus pandemic. Regardless of listed events, within the typical definition of force majeure, an event beyond the control of the parties, the outbreak of the coronavirus will also generally be considered force majeure, in particularly after the WHO declared Covid-19 as a pandemic on 11 March 2020.

Further support for such position is found in the WHO's designation of the coronavirus outbreak as a PHEIC, which is defined as "an extraordinary event which is determined...:

I. to constitute a public health risk to other States through the international spread of disease; and

II. to potentially require a coordinated international response" [1]

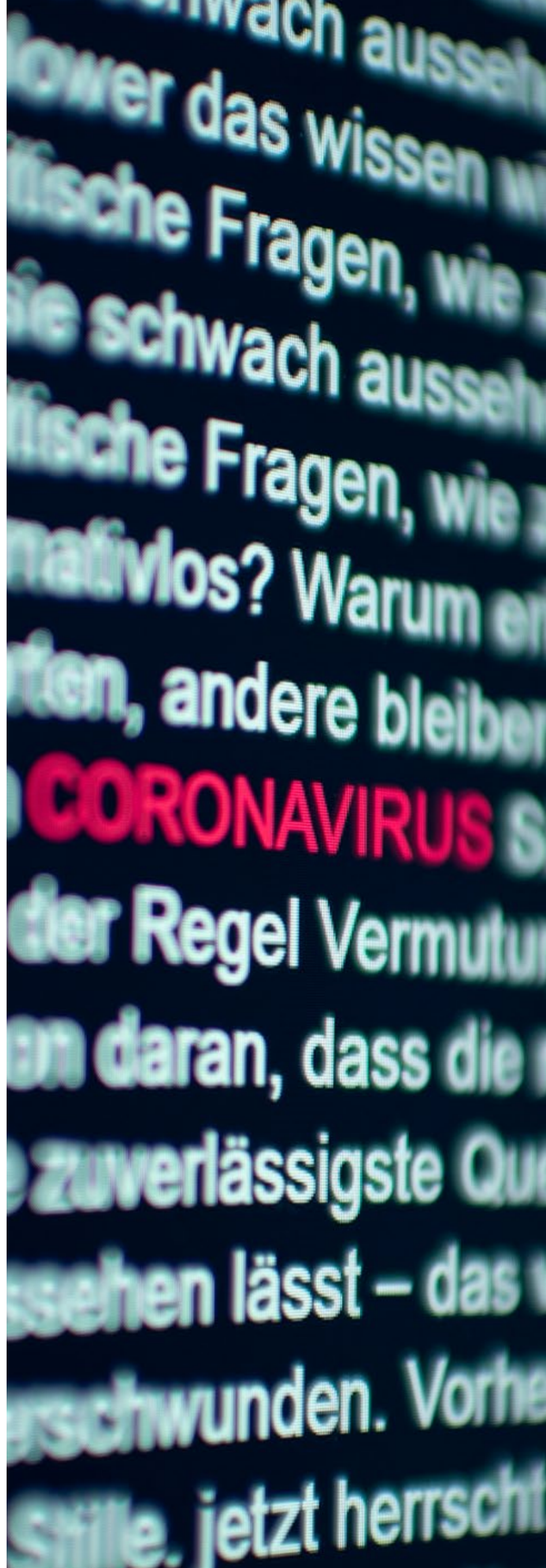
The WHO has commented that this definition "implies a situation that: is serious, unusual or unexpected; carries implications for public health beyond the affected State's national border; and may require immediate international action."[2]

Even if the outbreak and rapid transmission of the coronavirus is considered an event beyond the parties' control, it is noted that relief from fulfilment of a party's contractual obligations is only permitted if the virus has in fact prevented or frustrated performance of such contractual obligations. This may be the case if the performance of services or transport of goods is prevented by the limitations imposed by local and national authorities on the movement of people and/or goods in several countries and areas suffering under the coronavirus outbreak.. Following the Norwegian government's advice against travel to any country that is not considered necessary in the period 14 March to 14 April 2020[3], business internal travel restrictions to all countries in the same period is likely to constitute force majeure providing relief from fulfilment of a party's contractual obligations in the event it is dependent upon such travel. The same applies to the extent production or continuing services is dependent on personnel that are restricted access into Norway, a specific county or any other place of operation, or is required to comply with specific quarantine provisions that goes beyond what is reasonable to expect that such personnel expose itself to.

In addition to travel restrictions, many countries have implemented other infection control measures that may affect the performance of contractual obligations, and employers must consider what measures to implement in order to comply with such measures imposed by local and national authorities. This includes e.g. various mandatory quarantine requirements, but may also include measures that more indirectly impact a party's possibility to perform its contractual obligations. The latter may be measures like closure of schools and kindergartens, limitations on access to public transportation and the like, that may prevent employees and consultants from coming to work. The consequences of such measures may in most circumstances be related back to the Covid-19 outbreak and hence qualify as hindrances caused by force majeure.

In addition to such measures, any employer must of-course always consider what measures they consider required to protect and safeguard its employees and business continuation. However, not all such measures will necessarily constitute force majeure and provide for relief related to consequential failures to perform under contracts if they go beyond what has been imposed by the authorities. The main rule is still that contracts are binding upon the parties and shall be fulfilled according to its terms.

Notwithstanding the above, one should note that the situation may be very different for new contracts entered into. The typical definition of a force majeure event generally contains a carve-out for events that were, or reasonable should have been, known at the time of entering into the contract. It is therefore important to discuss and address the outbreak of the coronavirus in contracts being entered into as the outbreak and the potential commercial impacts are now commonly known. If not, there is a risk that the contract will not provide relief from fulfilment of the contracting parties' contractual obligations should it be effected by the outbreak.



[1] Article 1, International Health Regulations (2005), *https://apps.who.int/iris/bitstream/handle/10665/246107/9789241580496eng.pdf;jsessionid=C27F680B20E1EE483AAF0480A25D689A?sequence=1*

[2] IHR Procedures concerning public health emergencies of international concern (PHEIC), World Health Organization, *https://www.who.int/ihr/procedures/pheic/en/*

[3] *https://www.regjeringen.no/no/aktuelt/frarader-reiser-som-ikke-er-strengt-nodvendige-til-alle-land/id2693564/*

3. Limitations imposed by local and national authorities

In addition to a force majeure event directly effecting the performance of a contract, e.g. by a pandemic indisposing a significant number of project personnel, many are currently experiencing limitations on the execution of projects due to local and national authorities imposing limitations on the mobility of goods and people as well as services, customs and commercial activities, e.g. through quarantine regulations affecting both foreign and national personnel, due to the rapid spread of the coronavirus.

For example, if contractor is using a supplier in a country that has implemented strict quarantine restrictions or that has closed its boarders for a crucial delivery in a project, many suppliers in these areas have notified that they will not be able to deliver in accordance with the contract due to the limitations imposed by the national authorities. Provided the coronavirus is the reason for such limitations, it is likely that the effects of the limitations will also be considered force majeure.

Limitations imposed by local and national authorities may also excuse closing down contractor's production facilities, a construction site or a specific project if keeping production is indefensible as restrictions on the mobility of contractor's personnel or imposed temporary quarantine arrangements affecting contractor's personnel may render the production unmanned or only manned to an extent that effectively prevents safe and proper production. We are currently seeing examples of this in Norway even in projects that are not using foreign personnel, as various local authorities are imposing mandatory 14 days quarantine for anybody coming from the southern parts of the country, which is the Norwegian region hardest hit by the outbreak of the coronavirus.

In this respect, one should also note that various other rules and regulations may be relevant to consider. Such rules and regulations may as an example effectively require that the project is closed down or continued in a very different mode. The parties to a contract should carefully consider their obligations in respect to such rules and regulations, e.g. under the Norwegian Construction Client Regulations (Nw. "Byggherreforskriften").

Even if it is contractually safe to put all work on hold, the parties should be careful to address how they may limit the potential losses of such preliminary "close down" or suspension of activities (e.g. how they can secure the work already performed) and what measures they will have to implement to secure the safety of third parties, nature and other stakeholders. If such measures may give basis for additional compensation under the contract may differ from contract to contract, but it is not given that these are handled in the same way as the direct costs being incurred as a result of force majeure.

It should be noted that limitations imposed by local or national authorities may also entitle contractor other rights under the contract, e.g. a variation order. Typically this may include specific provisions regarding changes in laws, governmental orders etc. To what extent a measure or order imposed by governmental or local authorities as a direct response to a force majeure event, may provide rights under such "change of law"-provisions instead of being subject to the ordinary force majeure provisions, may vary. This must be assessed on a case-by-case basis, but in most situations where the original cause for the order or regulation is a force majeure event it will be the force majeure provision that takes priority.

A specific question that may arise in relation to the various measures imposed by local and governmental authorities is which of the parties that is actually prevented from performing its obligations under the contract. E.g., it can be asked whether the boarder control in Norway prevents a foreign contractor from providing its services or the client from receiving the services. These kind of questions may become relevant if the contract includes different rules regarding compensation depending on who invoked the force majeure provision.

4. Implications of official travel advice

As mentioned above, implementing internal travel restrictions is in itself not likely to be considered force majeure if they are stricter than what is generally required pursuant to official advice from governmental sources. Restrictions on travel aligned with official travel advice will normally be assessed different.

In Norway, the Ministry of Foreign Affairs provides the public with travel advice, which can be found for each country on their website.[4] The Ministry of Foreign Affairs generally refers to the Norwegian Institute of Public Health (FHI) for travel advice related to health issues[5], however, given the current situation, the responsibility for the situation in Norway has been taken over by the Ministry of Justice and Public Security.[6]

As of 14 March 2020, the official advice in Norway is to avoid all travel to any country that is not considered necessary (see footnote no. 3)

Internationally, travel advice may come from e.g. the WHO[7] and the European Centre for Disease Prevention and Control.[8]

If internal travel restrictions are aligned with official travel advice, either on a national or international level, and this has adverse effects on a party's ability to perform its contract obligations, this is likely to be considered force majeure.

[4] https://www.regjeringen.no/no/tema/utenrikssaker/reiseinformasjon/id2413163/

[5] https://fhi.no/nettpub/coronavirus/fakta/reiserad-knyttet-til-nytt-koronavirus-coronavirus/

[6] https://www.regjeringen.no/en/topics/health-and-care/innsikt/koronavirus-covid-19/id2692388/

[7] https://www.who.int/emergencies/diseases/novel-coronavirus-2019/travel-advice

[8] https://www.ecdc.europa.eu/en/current-risk-assessment-novel-coronavirus-situation

5. Implication of other industry players' actions

In addition to official travel advice, certain trade organisations have proposed travel restrictions for their members, and several companies have followed and implemented such restrictions. E.g., the Norwegian Oil and Gas Association (NOROG) did at an early stage advise that their members implement certain restrictions and measures based on a particular need to use caution in offshore operations. Such restrictions may extend beyond what a normal force majeure definition gives grounds for. However, to the extent the decision to implement such restrictions has been made public, this may very well impact on the interpretation of a particular force majeure provision if the counter party to a contract with a customer having implemented such restrictions invokes the same or similar restrictions on its operations.

If contractor's customer has introduced restrictions that limit contractor's possibility to perform its obligations under the contract arguing force majeure, contractor will itself not be liable for its failure to fulfil its obligations prevented by the customer's actions. In certain circumstances, contractor may however be entitled to further remedies caused by such actions. This must be determined on a case-by-case basis.

Further, industrial trade organisations' recommendations and individual companies' decisions may contribute to determine a joint understanding of what measures are required implemented in view of the circumstances and hence if such measures are relevant consequences of the outbreak and thereby constitutes a relevant force majeure event. However, such recommendations cannot be compared to official guidelines.

6. The effects of force majeure

As mentioned above, a valid force majeure situation may release a party from its obligations under the contract until the force majeure situation ceases. The party will therefore not be liable to pay compensation, e.g. liquidated damages, for the non-fulfilment of its contractual obligations. On the other side, the party will in general not be entitled to claim compensation from the other party for its losses caused by the force majeure event. In other words, the party must bear its own costs resulting from the force majeure event.

The party that encounters force majeure must generally notify the other party. Most contracts have rather stringent requirements for how and when such notification must be provided, and the contract must always be checked to ensure that any time limits are complied with. It is often required that such notice also be given at the end of the force majeure situation. If the party does not notify the other party about the occurrence of force majeure, it may become liable to compensate the other party for losses incurred thereby. It may also, under certain contracts, lose its right to invoke force majeure.

Although most parties now will accept that a force majeure event exists in relation to the coronavirus pandemic, everyone should be careful to comply with the specific provisions of the contract and provide timely notification of the effects on the relevant project. Parties may suffer significant losses due to the current situation, and one should expect that many parties may come out of this period with a need to recollect whatever they can. To prevent unnecessary disputes it is therefore better for all parties that contracts are strictly complied with.

We also stress that the notice requirements i.a. provides a possibility for the other party to limit its losses – e.g. by taking down its own organisation or implementing other measures – and facilitates for the commencement of a joint effort to find potential measures to limit the impacts on the completion of the parties' obligations under the contract.

In many contracts, but not generally, it is set forth that each party shall cover its own costs and expenses incurred as a result of the force majeure. Under some contracts, including some of the industry standard contracts generally used in Norway, contractors may however be entitled to compensation for various costs and expenses incurred by the contractor, e.g. in safeguarding and protecting the goods, if the customer has invoked a force majeure event preventing it from meeting its obligations required for contractor's delivery or fulfilment of its obligations. This may for example be the situation if the customer fails to provide required access to sites and facilities. It is not always clear if it is the customer or the contractor that is prevented from fulfilling its obligations. This must be considered on a case-by-case basis, if relevant for deciding on the effects.

It is not always clear to whom a particular cost or expense belongs to and hence who is responsible for carrying the cost consequences. The main concept of force majeure is, as previously mentioned, to postpone fulfilment of an obligation and to allocate the risk for damages and other liabilities incurred due to a situation that neither party is in control of. It may hence be somewhat unclear who is responsible for carrying the costs related to e.g. scaffolding, offices, machines, tools etc. that are mobilised at a site, but cannot be used as intended due to the force majeure event. At the outset this will be increased costs of preliminaries caused by the delay/prolongation of the project that contractor cannot claim compensation for. However, if such preliminaries are paid by the month or on other reimbursable basis, it may also be argued that it is within the customer's risk-sphere whether such items is used as intended or not.

Finally, many force majeure provisions entitle the parties to terminate the contract when a force majeure situation has lasted for a specified period of time. The usual range for such a period is from 3 months to 6 months. One should note that this implies that it is not straight forward to terminate a contract with a supplier that is prevented by a force majeure event to instead procure the same from another supplier that is not prevented by such event. In some instances it may however, at the same time be a reasonable measure to overcome the force majeure event to procure the missing goods from another source. If this is a reasonable measure or not, will have to be examined on a case-by-case basis, i.a. accounting for the potential losses incurred by the contract counter party if such alternative sourcing is not implemented.

7. How to handle a force majeure event

7.1 For contracts currently being negotiated

Many contracts exclude events that could reasonably have been foreseen at the time of entering into the contract from the force majeure definition. Hence, if you are currently negotiating a contract under which fulfilment of obligations may be impacted by the coronavirus, and this is not explicitly discussed and handled, such effects may not be covered by the force majeure provisions in the contract.

Given the current status of the outbreak, it should be considered in all tenders and negotiations of contracts for delivery of goods or services whether a specific regulation relating to the coronavirus should be included.

7.2 How to handle force majeure invoked by a contractor or sub-contractor

Considering the recent development of the spread of the virus, it is likely that customers will experience non-performance by contractors, and contractors will experience non-performance by sub-contractors, asserting that the non-performance must be excused as caused by force majeure.

In the event you receive a notification of a force majeure situation from a contractor/sub-contractor, it must be determined whether the described situation/event is covered by the force majeure clause in the relevant contract (ref. above), and whether any time limits relating to such notification have been met.

We have noticed that many customers are receiving a large number of notifications that do not notify of an actual delay caused by the force majeure event, but rather is a general notice that the coronavirus might affect the delivery time, i.e. an actual force majeure event has not yet occurred. Such notifications may very well be prudent to send, but depending on the wording of the contract, it may be wise to provide the contractor/sub-contractor with a reminder of its continuing obligation to notify once an event relevant for its performance actually occurs. This is particularly important if the notification is received from a sub-contractor where the claim needs to be forwarded to a customer under a contract providing for strict time limits that the contractor will need to comply with. Such notices should normally be updated or new notices be sent when new aspects of the situation occurs.

7.3 Can force majeure invoked by a sub-contractor be invoked towards the end customer?

Upon receipt of a notice from a sub-contractor, it must be determined whether the non-performance by the relevant sub-contractor will affect contractor's own performance under the main contract. Only if contractor's own performance is impacted does the question rise as to whether the force majeure situation affecting the sub-contractor can be invoked as force majeure towards the end customer, or if the event must affect the contractor directly for the contractor to be entitled to invoke force majeure.

This question cannot be answered on a general basis as the assessment depends on an interpretation of the relevant provisions in the contract. Some standard contracts contain provisions that address the question directly, whilst others contain force majeure provisions that are silent on the matter of force majeure effecting the delivery from a sub-contractor.

Ultimately, an interpretation of the force majeure regulations in the relevant contract will be deciding. However, there are certain situations that are more likely to be covered by the regulations than others. For example, if a sub-contractor is providing materials specifically designed for a particular project, and such sub-contractor is affected by a force majeure event, this will generally also qualify as force majeure under the main contract as contractor will not reasonably be able to source the item from another supplier. On the other hand, if the affected sub-contractor is providing materials that are interchangeable with materials from another supplier, or the materials can be procured from several suppliers, there is a significant risk that contractor cannot invoke force majeure towards the customer. However, under the current situation where all suppliers may be suffering from the same problem to deliver, this may be more likely than not to constitute a relevant force majeure event also towards the end customer.

One should under the current situation be aware that a subcontractor's or vendor's failure to deliver in time may not become very relevant in relation to the end customer if contractor is also failing on all other aspects of the contract due to official regulations preventing more or less any progress under the contract.

Further, a party has an obligation to try to overcome the effects of the force majeure event preventing it from fulfilling its obligations, for instance by implementing other measures. How far contractor's obligation to try overcoming these effects goes is not certain, but must be assessed on a case-by-case basis. For instance, it may very well not be considered a "reasonable measure" to have to source new goods or material from a new sub-contractor if the contractor thereby incurs a loss caused by its obligation to also fulfil all its obligations under the original contract with the sub-contractor actually being prevented by the force majeure event.

Each case must however be assessed on the specific contract and facts of the specific event, and legal advice should be sought if required.

8. Legal advice – Haavind Corona-desk

As part of Advokatfirmaet Haavind AS' co-operation agreement with the Norwegian Federation of Industries the member companies of the Norwegian Federation of Industries are entitled to certain advantageous terms with Advokatfirmaet Haavind AS. One of these advantages is that the members are entitled to a first immediate consultation (e.g. a phone call regarding the understanding of a specific contract clause) free of charge.

To be able to co-ordinate the response to its clients' concerns and need for legal support in relation to the outbreak of the coronavirus, Haavind has established a separate desk that is available to its clients and hence also the members of the Norwegian Federation of Industries. Please do not hesitate to send an e-mail or call one of our desk members:

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