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COVID-19: A Natural Disaster Or A Contractual One?

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As the seemingly everlasting COVID-19 pandemic transcends from “unprecedented” to the “new normal”, businesses have had to deal with the contractual fallout after the obstacles they have faced in fulfilling their contractual obligations. The common question posed by these businesses is “*am I protected by the force majeure clause in my contract?*”

Force majeure clauses are “normally used to describe a contractual term by which one (or both) of the parties is entitled to... [be] excused from the performance of the contract, upon the happening of a specified event or events beyond their control [...]”. A French phrase which literally translates to “greater force”, it is a common provision in commercial contracts which ensures that parties will not be held liable for non-performance due to events or circumstances which could not have been foreseen at the time the contract was entered into.

The widespread COVID-19 outbreak has caused great disruption to businesses worldwide, there has been much debate on whether COVID-19 absolves parties from their contractual obligations under force majeure clauses. This is especially true as some contracts have become “commercially impossible” to complete as originally envisaged.

The Malaysian Approach

In Malaysia, the Courts treat force majeure clauses like any other contractual clause in that it must be construed strictly according to the words used in the force majeure clause to reflect the intention of the parties at the time of contracting. As a general approach, the party who seeks to rely on a force majeure clause bears the burden of proving the following:

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¹ Chitty on Contracts 32nd Edition, Chapter 15, page 152

- (a) the existence of a force majeure clause in the contract in issue.
- (b) that the circumstances sought to be relied upon falls within the description of a force majeure event under the force majeure clause.
- (c) as a result of the force majeure event, the party could not perform his part of the obligations under the contract.

Therefore, if a force majeure clause explicitly provides “outbreak”, “epidemic”, “pandemic” and “global health emergency”, or “government actions”, “quarantines” and “lockouts” (in the case of the Movement Control Order) as a force majeure event, then the COVID-19 pandemic may fall within the scope of the force majeure clause.

However, a phrase such as “acts of God” is arguably insufficient as it is less specific. “Acts of God” has been defined as “*an accident due to natural causes, directly and exclusively without human intervention, and which could not have been avoided by any amount of foresight and pains and care reasonably to be expected of*”².

Further, difficulty often arises when a force majeure clause provides for “other circumstances” or “extraordinary circumstances” due to its generality. Generally, the Courts tend to be conservative with their application of force majeure clauses. For instance, in *Global Destar (M) Sdn Bhd v Kuala Lumpur Glass Manufacturers Co. Sdn Bhd*³, the High Court held that a “depressed economy” did not fall within the ambit of “other circumstances” in a force majeure clause. This is because “the ups and downs of business or economic climate are part of the risk of doing business”. This decision was later confirmed in *Malaysia Land Properties Sdn Bhd v Tan Peng Foo*⁴ by the Court of Appeal.

Following from the principle laid down in *Global Destar*, it appears that for an event to qualify as a force majeure event which could fall within the umbrella term of “other

² Halsbury’s Law of England (3rd Ed) page 183

³ [2007] MLJU 91

⁴ [2014] 1 MLJ 718

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circumstances” or “*extraordinary circumstances*”, the event relied upon must have been something that is beyond reasonable control of the parties, which is not contemplated at the time of contracting. The chances are strengthened if a force majeure clause clearly sets out example of force majeure event(s) without limitation by incorporating the phrase “including but not limited to” or “without limitation to”.

JN Contemporary Art LLC v. Phillips Auctioneers LLC

In a decision delivered in December 2020, the United States District Court for the Southern District of New York saw no difficulty in qualifying the COVID-19 pandemic as a circumstance beyond the parties’ reasonable control.

Judge Denise Cote appears to be one of the first judges to explicitly hold that the COVID-19 pandemic falls under the ambit of a “*circumstance beyond [either party’s] reasonable control*” and “*natural disaster*” in a force majeure clause in *JN Contemporary Art LLC v. Phillips Auctioneers LLC*⁵.

In this case, JN Contemporary Art LLC (JN), an art dealer, sued an art auction house, Phillips Auctioneers LLC (Phillips), after Phillips terminated the parties’ contract, in which Phillips had agreed to auction off JN’s painting at a May 2020 New York auction. Phillips moved to dismiss JN’s breach of contract claim on the ground that Phillips’ performance was excused because it had validly invoked the contract’s termination provision when the auction had to be postponed because of the COVID-19 pandemic and related government shutdown orders.

The termination provision permitted Phillips to terminate the agreement without having to make a guaranteed \$5 million payment to JN if the auction was “*postponed for circumstances beyond [either party’s] reasonable control, including, without limitation, as a result of natural disaster, fire, flood, general strike, war, armed conflict, terrorist attack or nuclear or chemical contamination . . .*”

Prior to the outbreak of the COVID-19 pandemic, the phrase “*natural disaster*” is commonly applied in the case of environmental disasters or weather. Despite that, the U.S.

⁵ No. 20cv4370 (DLC), 2020 WL 7405262

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District Court observed that the COVID-19 pandemic fits the common meaning of the words "*natural disaster*" found in dictionary definitions i.e., Black's Law Dictionary defines "*natural*" as "[b]rought about by nature as opposed to artificial means" and "*disaster*" as "[a] calamity; a catastrophic emergency". Likewise, the Oxford English Dictionary defines a "*natural disaster*" as "[a] natural event that causes great damage or loss of life such as a flood, earthquake, or hurricane".

The U.S. District Court further held that "*a pandemic requiring the cessation of normal business activity is the type of 'circumstance' beyond the parties' control that was envisioned by the Termination Provision.*". The U.S. District Court took into account the relevant government proclamations e.g, the State disaster emergency and the major disaster declaration, as a result of the COVID-19 pandemic.

In summary, the U.S. District Court held that the properly invoked Termination Provision ended Phillip's obligations to JN and Phillips was no longer required to offer the Stingel Painting at a subsequent auction or to pay JN the guaranteed minimum.

Conclusion

In Malaysia, there has yet to be a judicial authority to rule on the interpretation of COVID-19 within force majeure clauses. The position of the law is that the burden of proof falls on the party who is intending to rely on the force majeure clause.

Given this and the recent development in the *JN Contemporary Art* case, it is arguable that COVID-19 should fall within the ambit of "acts of God" in force majeure clauses. Further, with the presence of a relatively general phrase such as "circumstance beyond either party's control" or a description of force majeure event(s) without limitation, the case of *JN Contemporary Art* demonstrates the willingness of the U.S. Court to qualify COVID-19 as a force majeure event. We see this as a sound finding in the light of the wording of the force majeure clause in issue and the basis where the U.S. District Court arrived at its decision. This is especially true given that the COVID-19 pandemic has been affecting economies and business adversely for a continuous

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period since early 2020. The U.S. District has employed a rather practical approach in relieving parties to a contract within the parameters of the law.

Authored by Calan Eskandar, a pupil with the firm's Dispute Resolution practice.

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