Covid-19 as a Force Majeure, and Other Contractual Considerations

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Over the past few months, as the world has become familiar with new phrases like "social distancing", the legal community has revisited old concepts like *force majeure* and frustration of contract. While there is no doubt that Covid-19 has had a significant impact on the world, the question of whether Covid-19 actually constitutes a *force majeure* or is sufficient to frustrate a contract remains a fact-driven, open ended one.

To aid in the determination of contractual obligations during and in the aftermath of the pandemic, this article summarizes the current state of the law on *force majeure* and frustration.

(A) Force Majeure — a "Superior Force"[1]

Fundamentals

Force Majeure is a French legal term which translates into English as a "superior force". It is usually known in the English-speaking world as an "act of God". *Force majeure* clauses in contracts are intended to allocate risk for future events beyond the control of the parties that impair a

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[1] Outside of Canada, there is greater variation with respect to interpretation of *force majeure* clauses and the common law doctrine of frustration.

party's ability to meet its contractual obligations. *Force majeure* clauses vary from contract to contract. They may just specifically enumerate the included events or may include a broader catchall provision. In either case, they absolve the non-performing party from performance, liability, or both upon the occurrence of such an event.

There is no common law right to claim *force majeure*. The doctrine of frustration (discussed below) is the only common law right to avoid contractual obligations in the case of an event beyond the control of the parties.

Force majeure clauses typically excuse non-performance of a contractual obligation upon the occurrence of an extraordinary supervening event or circumstance beyond the control of the parties, which was not foreseeable when entering into the contract.[2] Whether any given event (e.g. Covid-19) is a *force majeure* will be a fact-specific determination based on the specific wording of the clause and the overall contract, and applying the general rules and principles of contractual interpretation.[3]

In 1976, the Supreme Court gave the following, somewhat controversial, definition of a *force majeure* clause:

> An act of God clause or *force majeure* clause [. . .] generally operates to discharge a contracting party when a supervening, sometimes supernatural, event, beyond control of either party, makes performance

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[2] See *Atlantic Paper Stock Ltd. v. St. Anne-Nackawic Pulp & Paper Co.* (1975), [1976] 1 S.C.R. 580 (S.C.C.) at para. 4 [*Atlantic Paper*].

[3] Courts will seek to determine the intention of the parties by reading the contract as a whole, giving the words used in a *force majeure* clause their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of the formation of the contract. *Creston Moly Corp. v. Sattva Capital Corp.*, [2014] 2 S.C.R. 633, 25 B.L.R. (5th) 1 (S.C.C.) at para. 47.

> impossible. The common thread is that of the unexpected, something beyond reasonable human foresight and skill.[4]

While this language suggests that for a *force majeure*, the event must be unforeseeable and render performance impossible, subsequent commentary has suggested that the Supreme Court's analysis in this regard was influenced by the law of frustration,[5] and that in the context of a negotiated *force majeure* clause, the specific language in the clause in question should govern. In *Atlantic Paper*, there was no reference to "foreseeability" in the clause at issue. Despite the reference to events beyond foresight in the passage cited above, the decision in *Atlantic Paper* focused more on the important question of whether the event in question was *beyond the control* of the parties.

Choice of Language Matters

There is no correct general answer to the abstract question of whether COVID-19 constitutes *force majeure*. It will depend on the specific wording of the contract.

In considering whether Covid-19 may be a *force majeure* in relation to a specific contract, consider:

- Does the clause have language closely tied to Covid-19, such as "disease", "illness", "pandemic", "epidemic", "contagion", "outbreak", "health emergency", "work stoppages", "supply chain disruption", "transportation shortages", "unavailability of labor", "unavailability of materials", "government action", "government

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[4] *Atlantic Paper*, *supra*, note 2.

[5] Michael P Theroux and April D Grosse, Force Majeure in Canadian Law, 2011 49-2 Alberta Law Review 397, 2011 CanLIIDocs 134, at page 406.

inaction", "national emergency", "local emergency", or "quarantine"?[6]

- Is there provision for a "change in law or regulation", and does the governmental response to Covid-19 affect performance under a contract?
- If there is no specific reference to those events, is it reasonably caught by broader language such as "any other cause beyond the party's control" or "an act of God", in light of the industry-specific reasonable commercial expectations of the parties?[7]
- Has Covid-19 affected the parties directly, or has it affected the supply chain? If the latter, consider the specific wording of the clause. In *Tenneco Canada Inc. v. British Columbia Hydro & Power Authority*,[8] the BC Court of Appeal found that "strike", an enumerated event in a *force majeure* clause, applied to a strike at the workforce of the invoking party's major customer. This was not express in the agreement, but the Court reasoned that the effect would have been identical had the contracting party's workforce been beset by the strike and so the strike at the customer's workplace was captured by the term "strike" in the *force majeure* clause.

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[6] The importance of specific contractual language was emphasized in *Telecom Decision CRTC 2005-17*, 2005 CarswellNat 8189, 2005 CarswellNat 8190 (C.R.T.C.), where the Tribunal held that the approach to be adopted in order to determine whether or not SARS-related events were sufficient to trigger *force majeure* clause protections was a case-by-case consideration in light of the surrounding circumstances.

[7] *Atcor Ltd. v. Continental Energy Marketing Ltd.*, 1996 ABCA 40, 25 B.L.R. (2d) 1 (Alta. C.A.) at para. 14 [*Atcor Ltd.*].

[8] 1999 BCCA 415 (B.C. C.A.) at paras. 44-45.

In general, *force majeure* clauses are construed narrowly.[9] It is presumed that parties do not intend to exempt performance, and courts are reluctant to relieve parties of their obligations. Courts will interpret the clause only to protect parties from events outside the normal risks encountered in the ordinary course of business. This will vary from industry to industry.[10]

Cause and Extent of Interference with Performance

As noted above, the language used in the contract should generally determine the degree of impairment necessary to trigger a *force majeure* clause. If the contract is silent on the point, the case law is mixed. Certain decisions suggest the standard is impossibility[11] while others have set a lower threshold such as "real and substantial problems" rendering performance commercially unfeasible.[12]

If performance has become more expensive or difficult, due to specific circumstances or prevailing market forces, that likely is not sufficient to constitute impairment under a *force majeure* clause unless the parties specify otherwise, based on the limited available jurisprudence.[13] The *force majeure* clause will not be enforced if the event in question merely renders it more expensive, difficult or onerous to perform, or "economically disadvantageous".[14] The payment of money will typically be ex-

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[9] Geoff R. Hall, *Canadian Contractual Interpretation Law*, 2nd ed. (LexisNexis Canada: Markham, 2012) at p. 288.

[10] *Atcor Ltd.*, *supra*, note 7 at paras. 11–14.

[11] *Atlantic Paper*, *supra*, note 2.

[12] *Atcor Ltd.*, *supra*, note 7 at para. 11.

[13] See *Domtar Inc. v. Univar Canada Ltd.*, 2011 BCSC 1776, 98 B.L.R. (4th) 316 (B.C. S.C.) at para. 86 [*Domtar Inc.*]; *Tom Jones & Sons Ltd. v. R.*, 1981 CarswellOnt 680 (Ont. H.C.) at paras. 13–15 [*Tom Jones*].

[14] *Domtar Inc.*, *supra*, note 13 at para. 86; *Tom Jones*, *supra*, note 13 at para. 15.

pressly excluded as a form of obligation from which a party can be relieved under the terms of the clause.

As the world grapples with the economic consequences of Covid-19 and the associated lockdowns, there likely will be further disruption to the ability of parties to perform under contracts. As part of any *force majeure* analysis, the cause of non-performance should be considered. Courts will not enforce a *force majeure* clause if there is no causal link between the event and the impairment of contractual performance.[15] Equally, if a party can mitigate, it is likely unable to claim *force majeure*.[16]

Causation and mitigation are likely to be related. For example, consider a commercial contract requiring a party to deliver a finished product comprised of various parts during the Covid-19 pandemic. Disruption in the party's supply chain may or may not be caused by Covid-19. If a supplier becomes unable to supply the party due to an outbreak at its facility, that may constitute a *force majeure* event under the clause. However, if the party had an alternative supply chain available, then it likely will not be able to show that its supply chain was disrupted due to Covid-19. Relatedly, its failure to avail itself of that alternate supplier could constitute a failure to mitigate.

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[15] In *Caisse Desjardins de St-Paulin c. Bombardier inc.*, 2008 QCCS 3725 (C.S. Que.), the Court held that the events of September 11, 2001 ("9/11") did not constitute a *force majeure* event as it was not the real cause of the invoking party's decision to terminate a service contract for the external painting of aircraft. Rather, the evidence showed that the service contract was canceled because of a purely economic decision to perform those painting services in-house.

[16] *Atcor Ltd.*, *supra*, note 7 at para. 29; See also *Wal-Mart Canada Corp./Cie Wal-Mart du Canada v. Gerard Developments Ltd.*, 2010 ABCA 149 (Alta. C.A.) at para. 17, where the court finds that a party failed to exercise sufficient diligence to meet a contractual deadline.

(B) Frustration of Contract

If a contract has no *force majeure* clause, or if Covid-19 is not captured by a *force majeure* clause, the impaired party may still have recourse to the common law doctrine of frustration of contract. This doctrine relieves contracting parties of their obligations if there is a supervening event, arising through no fault of either party, which alters the nature of their contractual obligations to such an extent that compelling performance despite the new and changed circumstances would be akin to ordering them to do something "radically different" from what they agreed to do in the first place.[17]

Originally, the party claiming frustration had to establish that performance of the contract, as originally agreed upon, would be impossible.[18] The party would have to show physical impossibility or impossibility resulting from a legal development. The modern doctrine of frustration also captures obligations that while physically and legally capable of being performed, are radically different from what the parties had intended.[19]

Frustration can occur due to supervening illegality, which occurs when an unforeseeable change in the law renders it illegal to perform the con-

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[17] *Naylor Group Inc. v. Ellis-Don Construction Ltd.*, 2001 SCC 58, [2001] 2 S.C.R. 943, 17 B.L.R. (3d) 161 (S.C.C.) at para. 55.

[18] G.H.L. Fridman, The Law of Contract in Canada, 4th ed. (Scarborough: Carswell, 1999), at p. 677 [G.H.L. Fridman].

[19] G.H.L. Fridman, The Law of Contract in Canada, 6th ed. (Toronto: Carswell, 2011), at p. 619. See also *Valdivia v. Lony G Inc.*, 2007 CarswellOnt 8659 (Ont. S.C.J.), where the court found that an employer's obligation to provide reasonable notice prior to terminating an employee was likely onerous due to the outbreak of SARS in Toronto in 2003 (and its specific impact on employer's business), however, the nature of the obligation was not "radically changed". Therefore, the doctrine of frustration provided no excuse for the employer's failure to meet its obligations.

tract. This type of frustration is particularly relevant in the context of Covid-19, with the raft of constantly evolving governmental restrictions currently in place. However, any such change in the law "must not be temporary or trifling in nature when viewed in the context of the contract as a whole".[20]

The test for frustration has been articulated in the jurisprudence as follows: (1) the supervening event is not the fault of any party to the contract; (2) the supervening event occurs after the formation of the contract and was not reasonably foreseeable to any party to the contract; (3) the supervening event renders it physically or legally impossible to perform, or transforms the obligation into a radically different obligation from what was initially undertaken;[21] and (4) the event must completely affect the nature, meaning, purpose, effect and consequences of the contract; mere inconvenience or temporary/transient impacts will not be sufficient.[22]

The consequence of frustration is that the contract comes to an end and both parties are automatically released from any further performance.[23] This is more drastic than a *force majeure* clause, which (i) typically stipulates a deferral or suspension of that obligation, rather than outright ter-

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[20] *Petrogas Processing Ltd. v. Westcoast Transmission Co.* (1988), 39 B.L.R. 132 (Alta. Q.B.) at para. 49.

[21] *Capital Quality Homes Ltd. v. Colwyn Construction Ltd.*, 1975 CarswellOnt 852 (Ont. C.A.); *Gerstel v. Kelman*, 2015 ONSC 978, 40 B.L.R. (5th) 314 (Ont. S.C.J.); *Bang v. Sebastian*, 2018 ONSC 6226 (Ont. S.C.J.); *McLean v. Miramichi (City)*, 2011 NBCA 80 (N.B. C.A.).

[22] *Kreway v. Kreway*, 2016 SKQB 115 (Sask. Q.B.) at para. 36; *KBK No. 138 Ventures Ltd. v. Canada Safeway Ltd.*, 2000 BCCA 295, 5 B.L.R. (3d) 167 (B.C. C.A.) at para. 14; G.H.L. Fridman, *supra*, note 18 at 679-80.

[23] *Klewchuk v. Switzer*, 2003 ABCA 187, 36 B.L.R. (3d) 114 (Alta. C.A.) at para. 23.

mination and (ii) typically only relieves the invoking party from the specific obligation impaired by the event, rather than the entire contract.

Consequently, a party claiming frustration has a higher threshold to meet than a party invoking a *force majeure* clause. Performance of the contract must become impossible, or the obligations must have been transformed into something "radically different". As a general proposition, price increases in a given marketplace — even dramatic ones — cannot result in frustration. Price changes are an inherent risk in any market. For example, the increase of the market value of real property, however substantial, did not constitute an intervening event that rendered the contractual obligation to transfer that property "radically different".[24] That decision must be distinguished from the finding, in *Gogal v. Chupa*, 2008 SKPC 89 (Sask. Prov. Ct.), that a cattle leasing contract was frustrated due to mad cow disease, which "dramatically restricted the profitability and viability of livestock operations across Canada". This "fundamentally" changed the cattle leasing agreement and rendered it "completely untenable and inequitable".[25] In that case, there was not simply a price change in the marketplace — there was an unforeseeable and devastating disease which caused that change.

Most provinces have complementary legislation which provide various remedies to be applied after a judicial finding of frustration. For example, if the governing law of the contract is Ontario, the *Frustrated Contracts Act* (the "Act") may apply.[26] Whereas the common law is limited and typically only discharges parties of their obligations under an agreement (akin to rescission), the Act provides for the recovery of payments or other benefits conferred pursuant to those obligations prior to the frustrating event. Further, it allows the severance of frustrated portions of a

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[24] *Paterson Veterinary Professional Corporation v. Stilton Corp. Ltd.*, 2019 ONCA 746 (Ont. C.A.) at paras. 17-18.

[25] *Gogal v. Chupa*, 2008 SKPC 89 (Sask. Prov. Ct.) at paras. 62–64.

[26] *Frustrated Contracts Act*, R.S.O. 1990, c. F.34.

contract from the remainder of the contract if the remainder was substantially performed prior to discharge.

(C) Conclusions

Covid-19 remains a relatively new disease, and there are not yet any reported decisions considering Covid-19 under existing *force majeure* clauses. Prior outbreaks, including SARS and MERS, did not cause the same global disruption, and so there are limited available precedents. Over the next few months and years, courts will be asked to consider and assess whether Covid-19 constitutes a *force majeure*, but until that time, the best avenue available to parties in these unprecedented times may be to try to negotiate a creative solution rather than seeking to rely on these oft-overlooked provisions.