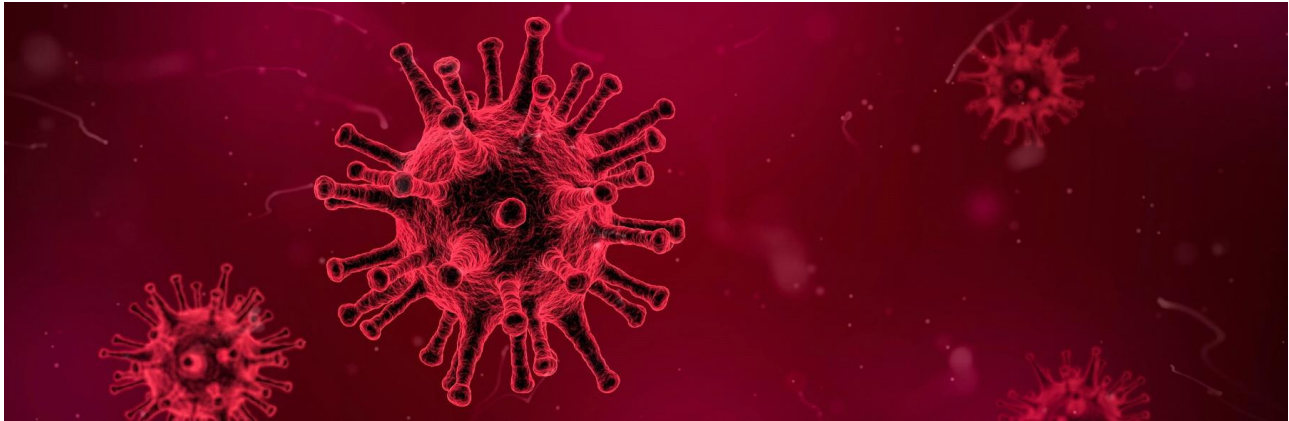


## Force Majeure, Frustration and Covid-19



On 16<sup>th</sup> March 2020, the Malaysian Prime Minister announced the imposition of a Movement Control Order (“MCO”) in an attempt to control the outbreak of Covid-19 in Malaysia. The MCO was initially announced for a period beginning from 18<sup>th</sup> March 2020 until 31<sup>st</sup> March 2020. The MCO has since been further extended to 14<sup>th</sup> April 2020. Companies in Malaysia are now struggling to comply with their contractual obligations as a result of the Covid-19 pandemic and the implementation of the MCO. The issue at hand is whether their non-fulfilment of contractual obligations due to the global Covid-19 pandemic and the implementation of the MCO would constitute a force majeure event, frustration or provide them with any legal basis for them to contemplate termination of the contract.

### **Force Majeure**

A force majeure event refers to an occurrence which is outside the control of a party to a contract, and which causes the party from performing or completing its contractual obligations. A force majeure clause is a fairly common clause in commercial contracts, and generally comprises of two facets:

- (1) the description of the occurrence(s) which would constitute a force majeure event; and
- (2) the consequences of the said force majeure event.

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In order to prove the occurrence of a force majeure event, the party claiming force majeure will have to do so based on the terms of the contract in question, particularly any terms stipulating force majeure (if any). If the claim is successful, the claimant may (i) be excused from their performance of the contract for the period of the force majeure event; (ii) exclude liability for such non-performance; and (iii) receive compensation.

Proving a force majeure event requires three (3) criteria to be satisfied:

- (1) the force majeure event must be proven to be outside the reasonable control of the party claiming force majeure;
- (2) the event must have caused the party's inability to perform, execute or complete their contractual obligations; and
- (3) the party must have exhausted all reasonable efforts to either avoid and/or mitigate the force majeure event or the consequences resulting from the event upon the contract.

In the pursuit of determining whether force majeure could be invoked, the following must be considered:

- (a) Whether a force majeure clause is included in the contract;
- (b) Whether the scope of the clause identifies the event in issue as a force majeure event or is sufficiently wide to encompass the force majeure event;
- (c) Whether it was foreseeable that the said event would occur, at the time the parties entered into the contract;
- (d) Whether the completion or performance of the contract is rendered impossible or materially affected due to the said event; and
- (e) Whether any relevant stipulations, procedures or prerequisites had been fulfilled in order for the force majeure clause to take effect, as prescribed in the contract.

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A pertinent factor in deciding whether Covid-19 qualifies as a force majeure event is rooted within the language and terminology of the contract. In some cases, force majeure clauses may provide for a lengthy and exhaustive list of events which may constitute force majeure events, which includes all of the categories and nature of events which would invoke the clause.

Other clauses may provide for broad definitions, which include all occurrences that are beyond the control, or reasonable control, of the parties. In the case of *CIMB Bank Bhd v Anthony Lawrence Bourke & Anor [2018]*, the Federal Court upheld the rule stipulating that an agreement must be construed based on the language used within the agreement.

In the circumstance that the force majeure clause in question had expressly included terminology such as 'disease', 'pandemic', or 'global health emergency', for example, the Covid-19 outbreak may qualify as a force majeure event. If the contract fails to provide for such occurrences, the pandemic may still be able to qualify as a force majeure event if the force majeure clause includes matters such as 'acts of God', 'events beyond the control (or reasonable control) of the parties' and 'events that make it impossible for the parties to complete their contractual obligations'.

## **Frustration**

In cases where force majeure is not specifically provided for in the contract or that it is difficult to trigger the clause, the doctrine of frustration provided for in Section 57 of the Malaysian Contracts Act 1950 may be applicable. Section 57 provides that the frustration of a contract occurs when "a contract to do an act which, after the contract is made, becomes impossible, or by reason of some event which the promiser could not prevent, unlawful, become void when the act becomes impossible or unlawful". This section, however does not define what "impossible" means.

Similar to the requirements to invoke a force majeure clause, the requirements for a party to rely on frustration of a contract as set out in the case of *Guan Aik Moh (KL) Sdn Bhd & Anor v Selangor Properties Bhd [2007] 4 MLJ 201* include:

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- (1) The event upon which the promisor relies as having frustrated the contract must have been one for which no provision has been made in the contract. If a provision has been made then the parties must be taken to have allocated the risk between them;
- (2) The event relied upon by the promisor must be one for which he is not responsible for. Self-induced frustration is ineffective; and
- (3) The event which is said to discharge the promise must be such that renders it radically different from that which was undertaken by the contract. The court must find it practically unjust to enforce the original promise.

In *Ramli Bin Zakaria & Ors v Government of Malaysia* [1982] 2 MLJ 257, the court held that “a contract is frustrated when there is a change in the circumstances which renders a contract legally or physically impossible of performance”. Further, in *Pacific Forest Industries Sdn Bhd & Anor v Lin Wen-Chih & Anor* [2009] 6 CLJ 430, the court held that a contract is not deemed to be frustrated merely because it becomes difficult to perform. As such, even if a contract is not absolutely impossible to perform, it could be frustrated and deemed void provided the contract has fundamentally changed and this was not contemplated by the parties at the time the contract was entered into.

As demonstrated above, proving that frustration of a contract has occurred requires a high standard. In *Hong Leong Bank v Tan Siew Nam & Anor* [2014] 5 MLJ 34, the court reiterated the judge’s statement from *Ooi Yoke In & Anor v Public Finance Bhd* [1992] MLJU 25 in that “the doctrine of frustration is to be confined to very narrow circumstances, the reason being, I think, that commercial bargains should not be lightly avoided or brushed aside merely upon a change of circumstances”.

Therefore, the Covid-19 outbreak may indeed be construed as an event which has occurred beyond the control of parties to a contract and may not have been contemplated by the parties when entering into the contract. However, whether the contract would be “impossible” to perform would very much depend on the evidence the party who wishes to rely on it has, to prove that the contract can no longer be performed as a result of the outbreak. The nature of the contract would also need to be taken into account.

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In circumstances where high reliance is placed on third party suppliers, sub-contractors or employees in order for a party to carry out its contractual obligations, this would depend on whether the party claiming frustration can prove that such suppliers, sub-contractors or employees could not uphold their own obligations following restrictions placed by the Government, namely the MCO, resulting in the impossibility of performing the contract. This is because mere inconvenience, difficulty or financial loss as a result of the outbreak may not render the contract impossible to perform. If only a part of the contract is rendered impossible by frustration, and other parts of the contract have been fully performed prior to the frustrating event, the Court is empowered under Section 16(4) of the Malaysian Civil Law Act 1956 to sever the performed part of the contract from the original contract, and treat it as a separate contract which may be enforced, depending on the facts and circumstances of each particular case.

On the other hand, if the contract can be deemed frustrated, the contract will be rendered void. Section 57(2) of the Malaysian Contracts Act 1950 provides that *“a contract to do an act which, after the contract is made, becomes impossible, or by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful”*. The effect of a void contract is set out under Section 66 of the Malaysian Contracts Act 1950, which states that *“when an agreement is discovered to be void, or when a contract becomes void, any person who has received any advantage under the agreement or contract is bound to restore it, or to make compensation for it, to the person from whom he received it.”* Further, as provided in Section 15 of the Malaysian Civil Law Act 1956, monies paid towards the performance of the contract may be returned or recovered to the respective party depending on the circumstances of the particular facts and whether it is just to do so, taking into account expenses incurred by the parties towards performance of the contract.

If a contract becomes impossible to perform due to a frustrating event, the contract would be deemed void upon the occurrence of the frustrating event, and the parties would be discharged from further performance of the contract. The Court then has a wide discretion to allocate the parties' rights and liabilities, including return of monies paid or payable, claim for expenses incurred and compensation for benefits rendered to the other party prior to the frustrating event.

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In conclusion, the applicability of force majeure clauses and frustrating events would vary depending on the facts and circumstances of each particular case. It is therefore imperative that parties entering into contracts identify and consider from the outset, the scope of circumstances which are to be addressed within the force majeure clause itself, the notice requirements (if any), and the consequences of the contract if the force majeure clause can be relied upon, in light of the Covid-19 outbreak.

Parties which have already entered into contracts should therefore consider undertaking the following steps:

- (1) Identify and construe the **force majeure clause** within the contract (if provided for) and whether the circumstances listed in the provision covers the Covid-19 outbreak.
- (2) Identify the **notice requirements and time limit** in respect of notifying the other party regarding the occurrence of a force majeure event, if any, within the contract. Force majeure clauses generally contain notice requirements in order to invoke the force majeure clause and it would be prudent for a party seeking to rely on it to comply with the specific notice requirements and time limit to compile evidence.
- (3) Identify if there are any **mitigating steps** that may be undertaken to reduce the impact of the outbreak on the contract and to possibly avoid the need to terminate the contract.
- (4) To seek **legal advice** on their contractual rights and obligations in respect of force majeure events and actions which may be taken in the event a contract becomes frustrated due to the Covid-19 outbreak.

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