PANDEMIC, PESTILENCE AND SHIPPING CONTRACTS: DELAYS AND CONSEQUENCES

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1. The COVID-19 pandemic has, unsurprisingly, affected all aspects of the shipping and commodities industries. In this Note we consider the extent to which parties to common forms of shipping contract are excused, or potentially excused, from performing their obligations as a result of delays caused by the outbreak, whether by reference to express clauses in the contracts concerned or to the common law doctrine of frustration.

CHARTERPARTIES

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Introduction

1. The maintenance of global supply chains is a vital part of the response to COVID-19. Around 90% of world trade is carried by sea and Governments around the world are doing their utmost to ensure that commercial ports within their jurisdiction can continue to function. Notwithstanding these efforts, the potential for delays and difficulties in performing charterparties are obvious: vessels are likely to be delayed as a result of quarantine measures; there may be difficulties in obtaining bunkers or spares; lack of shore personnel may lead to delays in loading/discharge/repairs; crew changes may be prohibited; cargo may not be delivered to port due to inland transportation restrictions; vessels may be unable to sail due to ill health of their crew. It is conceivable that more stringent measures may yet be adopted, such as the closure of ports and the detention of vessels.

2. It is not surprising that, against this uncertain backdrop, the concepts of frustration and force majeure are now being mentioned with increasing frequency. This note is intended to highlight whether and how these two concepts – and the related but distinct concept of exceptions clauses – might be engaged.

Force Majeure

3. As a matter of English law, "force majeure" refers to a contractual clause (as opposed to a doctrine of law) which makes provision in relation to the parties' obligations in the event of certain extraordinary events which are beyond the control of the parties. Typical force majeure clauses may: list specific events; be expressed in broad terms, for example *"events beyond the reasonable control of the parties"* or even simply *"in the event of force majeure"*; or comprise a combination of the two. Force majeure clauses are comparatively uncommon in charterparties, but are more likely to be found in Contracts of Affreightment.

4. The scope and effect of such clauses depends upon the application of the usual contractual principles of construction. For contracts governed by English law, this will mean, in particular, that the starting point is to consider the natural meaning of the words used and that ambiguities will be resolved against the party seeking to rely on the clause (the *contra proferentem* rule).

5. Key issues of construction are likely to involve:

    - Whether COVID-19 falls within the scope of a general "catch-all" provision in a force majeure clause which does not specifically mention disease/epidemic/pandemic;
    - Whether the force majeure clause requires the performance of the contract to be prevented, or merely hindered or delayed;
    - Whether the effect of the clause is to suspend performance of the contract, terminate the contract and/or whether it provides a mechanism for allocating losses/expenses which have already been or will be incurred.

6. Other practical issues to bear in mind include complying punctiliously with any notification requirements and preparing a clear evidential record of the existence of a force majeure event and the necessary causal link to impossibility/difficulty of performance. It is noted that the China Council for the Promotion of International Trade is offering "Force Majeure" certificates to local companies that are unable to fulfil their contractual

obligations. Similarly a number of Indian ports have declared "Force Majeure". Such certificates/declarations are not binding as a matter of English law, but may be of evidential value.

Exceptions Clauses

7. A more common form of clause in both voyage and time charters is an Exceptions Clause. This operates to exclude the liability of the parties that would otherwise arise for loss or damage or failure to perform in relation to certain specified events. For example, the NYPE form contains the following exceptions clause:

"The act of God, enemies, fire, restraint of Princes, Rulers and People, and all dangers and accidents of the Seas, Rivers, Machinery, Boilers and Steam Navigation, and errors of Navigation throughout this Charter Party, always mutually excepted."

8. Again, such clauses will be subject to the ordinary rules of contractual construction. The charterparty must be construed as a whole, so that if an additional clause has imposed a specific responsibility on either party, that obligation is unlikely to be overridden by an exceptions clause contained in the standard wording: **The TFL Prosperity** [1984] 1 Lloyd's Rep 123.

9. It appears that the phrase "Restraint of Princes, Rulers and People" is apt to cover the kind of restrictions that ports are imposing in response to COVID-19. However, delays arising from quarantine may be dealt with expressly in the charterparty. See, e.g., clause 17 of the Asbatankvoy form, which provides:

"Should the Charterer send the Vessel to any port or place where a quarantine exists, any delay thereby caused to the Vessel shall count as laytime; but should the quarantine not be declared until the Vessel is on passage to such port, the Charterer shall not be liable for any resulting delay."

Frustration

10. The doctrine of frustration operates to bring a contract to an end in circumstances where *"a supervening event renders the performance of the bargain "radically different", when compared to the considerations in play at the conclusion of the contract"*: **Canary Wharf (BP4) T1 Limited v European Medicines Agency** [2019] EWHC 335 (Ch) at [27].

11. In *The Sea Angel* [2006] EWHC 69, the Court of Appeal gave this guidance on the application of the doctrine:

- It requires a *"multi-factorial"* approach. Amongst the factors which must be considered are the terms of the contract itself, the parties' knowledge, expectations, assumptions and contemplations, assessed objectively as at the time of the contract, the nature of the supervening event and the parties' reasonable and objectively ascertainable calculations as to the possibility of future performance;
- The requirement that performance be "radically different" indicates that the doctrine is not to be lightly invoked: the mere incidence of expense, delay or onerousness is not sufficient;
- There has to be a break in identity between the contract as provided for and its performance in the new circumstances;
- Ultimately, the doctrine is one of justice, but this does not mean that the court has a *"broad absolving power whenever a change of circumstances causes hardship to one of the contracting parties…"*

12. In the COVID-19 context, the most likely issue for owners and charterers alike is likely to be increased delay – whether that is in getting to port/berth, carrying out loading or discharge operations or in obtaining cargo. The charterparty will of course contain a carefully balanced allocation of risk of delay – through provisions on cancellation, laytime, demurrage or off-hire as the case may be. However, if the delay becomes exceptionally severe it may be capable of constituting a frustrating event. In assessing the severity of any delay it is relevant to consider (amongst other factors):

- The period of delay as against the duration of the whole charter (in the case of time charters);

- The time the voyage should have taken and the time it actually did take (in the case of voyage charters);
- the nature of the cargo (i.e. whether it will perish as a result of the delay); and
- whether the vessel could proceed to an alternative port.

13. It is possible that circumstances in particular countries may be so severe (or regulations so strict) that it becomes difficult for charterers to obtain specific cargo. This may frustrate the charterparty if there is no other possible source or if the delay in obtaining cargo is sufficiently fundamental.

14. The effect of the doctrine of frustration at common law is that the contract is terminated at the date of the frustrating event. The consequence of this is that both parties are discharged from performance of obligations accruing in the future, but remain liable in respect of obligations accruing before that date. The loss "lies where it falls". This may well give rise to interesting questions as to what is the frustrating event: is it for instance the WHO declaration of the pandemic or the commencement of the specific port regulation. The answer, as in all aspects of frustration, will be fact specific.

15. The potential harshness of the common law consequences of frustration have been mitigated by the Law Reform (Frustrated Contracts) Act 1943 (**"the 1943 Act"**). This provides that:

- Sums paid or payable prior to the discharge of the contract shall be recovered or cease to be payable, provided that if the payee has incurred expenses in the performance of the contract prior to discharge, the court may allow some or all of the sums paid or payable to be retained by the payee, if it considers it just in all the circumstances (section 1(2));
- Where one party has before the time of discharge obtained a valuable benefit by reason of anything done by the other party in performance of the contract, the court may order the suitable sum to be paid, not exceeding the value of the benefit obtained (section 1(3)); and
- If part of the contract can properly be severed from the remainder of the contract, the court may treat that part of the contract as if it were a separate contract which has not

been frustrated. Thus, if a 12 month charter is frustrated halfway through, the court may treat the charter as valid for the first six months, so that payments due but not paid in respect of that period remain payable.

16. It should, however, be noted that the 1943 Act does not apply to any charterparty except a time charterparty (held to include trip charters: **The Eugenia** [1964] 2 QB 226) or a demise charterparty (section 2(5)).

SHIPBUILDING CONTRACTS

Philippa Hopkins Q.C.

Introduction

17. In a similar vein, questions are already arising as to the impact of the crisis on concluded shipbuilding contracts, whether for vessels already partly under construction or for those where construction has not yet commenced.

18. Asia-Pacific yards began to experience delays as early as January this year as staff became unwell. Many yards were forced to close. That in turn led to what was described by some sources as a "boom" for European shipyards – particularly for repair and retrofitting work, though not so much for newbuilds. However, as the virus has spread, it seems that the Far Eastern yards will have the last laugh. European yards are now being forced to suspend operations, whilst Chinese and Korean yards are reopening. According to a Lloyd's List report of 8 April 2020, shipbuilding output remains on course to rise this year, with Chinese yards expected to produce the lion's share of tonnage.

19. But whatever the position in a few months' time, many, if not most, shipbuilding programmes will have experienced significant delay. Where does this leave the contracting parties?

Force majeure clauses: reliance by yards

20. Most shipbuilding contracts, of course, contain detailed express provisions dealing with delays in construction of the vessel and the consequences of those delays.

21. Thus the SAJ form, still in common use despite its age, lists a number of causes of *"permissible delay"* in Article VIII.1; where there are *"delays on account of [those] causes"* (Article VIII.3), the delivery date of the vessel is postponed, without any reduction in the price. (In contrast, *"unauthorised delays"* result in an adjustment to the contract price under Article III.) The causes of permissible delay include the obviously pertinent *"plague or other epidemics"* and *"quarantines"*, as well as "labour shortage" where a yard's staff are absent as a result of the outbreak. Where, for example, construction is delayed not directly by the outbreak of COVID-19 but by government-imposed restrictions resulting from the pandemic, *"requirements of government authorities"* might also be relied on by a yard.

22. Similarly, clause 34 of BIMCO's NEWBUILDCON form provides, by clause 34(a), that *"The Delivery Date shall be extended if any of the following events cause actual delay to the delivery of the Vessel: …(2) any government requisition, control, intervention, requirement or interference…(5) epidemics".* And the AWES form, commonly used by European yards, identifies *"epidemics"* and *"export or import restrictions"* as *force majeure* events (Article 6(d)).

23. So far, so good, from a shipyard's perspective. But there are pitfalls. In the case of most shipbuilding contract forms:

- First, there are notice requirements which must be complied with strictly. Some forms (e.g. NEWBUILDCON) make clear that the failure to meet the notice requirements bars a claim for permissible delay entirely. And even where they do not expressly so state, a court is likely to regard them as having that effect: see **Adyard Abu Dhabi v. SD Marine Services** [2011] EWHC 848 (Comm.) (Hamblen J.).

- Secondly, most *force majeure* clauses will require the yard to show that delay has in fact been caused as a result of the event relied on (see, in a slightly different context, **Classic Maritime Inc. v. Limbugan Makmur Sdn Bhd** [2019] EWCA Civ. 1102. In many instances this will cause no difficulty, but there might be an issue for – for example – yards whose schedule was already tight, leaving scope for buyers to argue that some or all of the delay would have been incurred in any event.

- Thirdly, if the yard could reasonably have avoided the effects of the *force majeure* event, it will not be entitled to rely on the clause: **Channel Island Ferries Ltd. v. Sealink UK Ltd.** [1988] 1 Lloyd's Rep. 323 (CA), **Seadrill Ghana Operations Ltd. v. Tullow Ghana Ltd.** [2018] EWHC 1640 (Comm.) (Teare J.). Whilst any yard will, no doubt, say that it could have done nothing to avoid COVID-19 – which might well be true – arguments might arise as to whether, for example, a yard could have brought in additional workers and so avoided delays. Arguments of this kind are less likely to be available to a buyer where a yard has been closed by government order.

24. As to causation, it is worth noting that in China, the Council for the Promotion of International Trade has issued so-called "force majeure certificates" to thousands of Chinese companies, purporting to certify that they have been affected by government policies in relation to the pandemic. Chinese yards will, no doubt, seek to rely on these; but whatever their status as a matter of Chinese law, such a document is likely neither to be necessary for a yard to claim permissible delays, nor sufficient by itself for it to do so.

25. Finally, yards will need to be astute to ensure that delays in construction are as short as possible. The majority of shipbuilding contracts (see, for example, Article VIII.4 of the SAJ form and clause 39(a)(iii) of NEWBUILDCON) do not allow the yard to postpone delivery indefinitely. Instead, once a specified period – typically 180 or 210 days – has passed, the buyer has the right to cancel the contract and demand the return of all sums paid thereunder.

26. Given the fall in all markets which the pandemic has provoked, it is to be anticipated that many buyers – having agreed to pay far more than their new vessel is now worth – will seek to take advantage of these provisions if they possibly can. It is no surprise that BIMCO reports that new shipbuilding contracts have fallen sharply in recent weeks: see https://www.bimco.org/news/market_analysis/2020/20200403_coronavirus_is_disrupting_the_supply_of_ships_as_well_as_demand. In the months to come, there is every chance that buyers will be faced with having to take delivery of vessels which they neither want nor need, and will seek to exit their contracts if they can find any rational basis for doing so. *Caveat naupegus* (builder, beware).

***Force majeure* clauses: reliance by buyers**

27. It is also worth noting that, although yards are likely to have a good chance of relying on contractual terms that excuse delays to their performance, buyers are not so fortunately circumstanced. Although falling revenues resulting from COVID-19 will impact on some buyers' ability to pay sums due under shipbuilding contracts in a timely fashion, most contracts do not include *force majeure* or similar provisions on which a buyer can rely to excuse a delay in payment. That said, if a yard is concerned about its ability to offload surplus tonnage elsewhere, it may be prepared to agree an extension of time for payment with a still willing but temporarily impecunious buyer.

Frustration

28. Although the doctrine of frustration is in principle capable of applying to shipbuilding contracts, it is unlikely to be of relevance to the current situation. As Simon Curtis points out in *Shipbuilding Contracts* (4th edn. 2012), almost all cases in which shipbuilding contracts have been held to be frustrated have involved the outbreak of war which has prevented construction from taking place at all or has resulted in the vessel being requisitioned. Disruption by COVID-19 is more likely to cause delays than a complete and final cessation of work. More fundamentally, though, it is difficult to envisage the doctrine applying to modern shipbuilding contracts which make extensive provision as to how the vast majority of delays outside the yard's control are to be addressed. Where a contract makes "full and complete provision" for an event, or (to put it another way) expressly allocates the risk of that event between the parties, the doctrine of frustration has no room to operate: see **The Kyla** [2013] 1 Lloyd's Rep. 565 (Flaux J).

29. As has been noted above, most shipbuilding contracts make detailed and comprehensive provision for delays – at least in construction – caused by epidemics and by government restrictions. Thus any court or tribunal is likely to hold that the contract stands or falls by those provisions and that the concept of frustration simply has no room to operate, whatever the impact of the pandemic on the contract in question.