

Insights

FORCE MAJEURE FAQ - HONG KONG SAR LEGAL ISSUES IN COMMERCIAL CONTRACTS

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SUMMARY

As the outbreak of COVID-19 is sweeping through the globe and governments are updating their orders and directives on a daily basis, we are all navigating uncharted waters. In the light of the latest development of the COVID-19 outbreak in Hong Kong SAR and the recent governmental measures, this Q&A serves to provide an update on the key considerations to have in mind when reviewing Hong Kong SAR law governed commercial contracts and assessing the parties' continued ability to perform their contractual obligations.

Q: Does your contract have a force majeure clause?

First check if your contract has a force majeure (FM) clause. It is not implied into a contract under Hong Kong SAR law. If there is no FM clause, you would need to prove instead that your contract has been frustrated. The bar for showing frustration of a contract is much higher and extremely difficult to establish in practice.

Q: Is COVID-19 a force majeure event for the purposes of your contract?

Assuming there is an FM clause, the first stage is to assess whether a FM event within the drafting of your clause has occurred. It is the text of a FM clause and the particular factual matrix which is key. Interpretation will vary greatly depending on timing. For example, the outbreak was only declared a pandemic on 11 March 2020. Until this point, the WHO characterised it as a 'public health emergency of international concern.' This may be of relevance to FM clauses using terminology such as disease, illness, epidemic, pandemic or quarantine.

Likewise, the term 'government intervention' in an FM clause may mean the FM clause is in play, but this ultimately depends on the actions taken by a particular government where the parties operate and/or where the contract is being performed (and construction of the entire contract). In Hong Kong SAR, on 28 and 29 March 2020, the Prevention and Control of Disease (Requirements and

Directions) (Business and Premises) Regulation (Cap. 599F) and Prevention and Control of Disease (Prohibition on Group Gathering) Regulation (Cap. 599G) started to take effect:-

- Under Cap. 599F, businesses such as amusement game centres, bathhouses, fitness centres, places of amusement, places of public entertainment and party rooms must be closed for a period of 14 days, that is until 5:59 pm on 11 April 2020. If businesses, other than those specified in the regulations, elect to close voluntarily without waiting for a government to issue regulations requiring them to do so, this may mean they are not excused liability under the provisions of their FM clause.
- Under Cap. 599G, group gatherings with more than four people in public places are prohibited as of 0:00 am on 29 March 2020 for a period of 14 days, that is until 11 April 2020. Group gatherings for, amongst other things, transportation, work at a place of work, a wedding ceremony at which no more than 20 people attend and no food or drink is served, are exempted. Such restrictions on group gatherings may 'hinder' or 'prevent' performance of contractual obligations. Parties may therefore be excused liability under the provisions of their FM clause on the ground of 'government intervention'.

A shorter form FM clause including the term 'Act of God' (but not specifically including the terms 'epidemic' or 'pandemic' or 'public health emergency') may also cover the COVID-19 outbreak, but the clause itself would need to be construed in light of the contract as a whole.

The changes in governmental strategy (and WHO guidance) to tackle the outbreak also have implications for a company's portfolio of contracts, as whether an event is an FM event can change very quickly overnight. Further, the analysis may vary in each country of operation, as national governments adopt different responses to the outbreak, depending on the point they have reached in the spread of the virus and the strategies they adopt to contain it.

It is important to check if there are any excluded events which would mean a party is unable to rely on the FM event (e.g. financial hardship/ lack of demand/ economic downturn consequent on the FM event is causing the non-performance rather than the COVID-19 outbreak).

Q: When will the FM clause offer relief from performance?

Again, we are seeing a range of thresholds at which a person seeking relief for non-performance is entitled to rely on the provisions of an FM clause. The threshold for triggering protection of an FM clause will vary from contract to contract, with some contracts potentially excusing contractual performance when this has become 'inadvisable' rather than 'impossible' or others where the FM event 'hinders' or 'prevents' performance.

Q: What if your contract has simply become less financially attractive to perform?

Changes in economic or market circumstances affecting the profitability of a contract or the ease with which the obligations can be performed quite probably are not FM events. To be able to rely successfully on an FM clause, a business usually will need to show it is the FM event which is the primary cause of its non-performance.

For catering businesses, various mandatory measures are now required under Cap. 599F, for example, the number of customers at any premises on which food or drink is sold or supplied for consumption on the premises (catering premises) at any one time must not exceed 50% of the normal seating capacity of the premises; and, no more than 4 persons may be seated together at one table within any catering premises. Such measures will inevitably affect the profitability of the catering businesses. However, reduced profitability due to governmental interventions does not necessarily guarantee a successful reliance on the FM clause, a business will need to show it is the FM event which is the primary cause of its non-performance of contractual obligations.

Q: Issuing a FM notice and the duty to mitigate

To rely on a FM clause, a business will need to check and follow the process steps set out in the contract (in terms of form and timing of notice to be given to counterparties). The parties will also need to consider if the contract should be terminated (or merely suspended) depending on what the contractual provisions envisage.

Any party alleging FM will also be under a duty to mitigate the effects of the event. The steps a party would need to take to mitigate will vary according to the nature of the particular contractual relationship. Case law suggests that language in FM clauses referring to events ‘beyond the reasonable control of the relevant party’ can only be relied on by a party if that party had taken all reasonable steps to avoid its operation or mitigate its results. Given this duty to mitigate, it will be important to keep all records of all communications between the parties to document the steps taken in mitigation.

Q: Are there any other relevant considerations?

As practice around containment/ management of the outbreak varies by jurisdiction, so does practice around governmental intervention in private law contracts between parties. The Chinese government proactively started issuing FM notices to suppliers in certain regions in China, but we have not seen this practice adopted elsewhere to date. It is also not yet known how courts outside the PRC would interpret government FM notices in the context of a Hong Kong SAR law FM clause.

Even though Covid-19 might be a FM event under contract, it may not be covered by an insurance policy. It is important to check insurance policies to understand the scope of cover and any exclusions applicable in these circumstances.

Q: What should you be considering in light of the outbreak for new contracts?

- When is the contract to be entered into?
- When is the contract to be performed?
- Where are the contractual obligations to be performed?
- What are the likely impacts of the COVID-19 outbreak on the parties and their ability to perform the contract?
- Is it possible to obtain insurance in case performance is delayed?
- Have the parties discussed who should bear the risk of delayed/ non-performance of the contract? Has this been priced into the contract?
- Do the parties have contingencies to allow staff allocated to the project to continue work during the outbreak (e.g. from remote working)?
- What does the FM clause provide? Consider the relevant events giving rise to a FM event.

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MEET THE TEAM



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