

# COVID-19 and its Impact on Contractual Relations: How to Mitigate Damages, Renegotiate Your Contracts and Avoid Disputes (Part I)

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# Introduction

In response to the rise of COVID-19 cases in Kenya, the Government has implemented various measures and restrictions to contain the spread of the virus across the country. These include cessation of movement into and out of four counties, namely Nairobi, Mombasa, Kilifi and Kwale, a nation-wide curfew between the hours of 7 p.m. to 5 a.m. and travel restrictions with a general embargo on international passenger flights.

Both the pandemic and restrictions imposed by the Government have triggered a large-scale disruption of the Kenyan economy, leading to a slowdown in many sectors, and in particular in the tourism, hospitality, trade and transport industries. Given the local and global effects of the pandemic, businesses are grappling with their inability to meet their obligations under existing contracts.

In this series of articles we analyse the sudden and unexpected impact of COVID-19 on existing contractual agreements and what companies should be doing to mitigate the impact with a primary focus on the position under Kenyan law.

# The impact of COVID-19 pandemic on contractual agreements

An indicator of the economic effect of COVID-19 on the Kenyan economy can be seen in the sudden loss of value of more than KES 120 billion (approx. USD 1.2 billion) in the market capitalisation of companies listed on the Nairobi Securities Exchange (NSE), the single largest drop in the history of the NSE. Kenya Airways, an NSE-listed company and one of the continent's flagship brands, is reportedly losing KES 800 million (approx. USD 7.5 million) a month due to the shutdown of air travel into and out of the country.<sup>1</sup>

Consumer spending has significantly declined as people seek to save money and restrict their mobility by avoiding offices, restaurants, shopping malls, recreational facilities and other public places to maintain social distancing. Additionally, many businesses are faced with delays in their supply chains putting additional stress on their cash-flow and their contractual obligations.

The general rule under contract law is that where a party fails to perform its contractual obligations, such failure constitutes a breach of contract and gives rise to liability in favour of the counterparty. Accordingly, it is important that parties affected by the COVID-19 pandemic identify how they can best protect or mitigate against losses or liability during this time.

There are various legal reliefs or defenses to non-performance or delay in the performance of contractual obligations, which could assist in an economic downturn. In this series, we consider three of these defenses: the doctrine of *force majeure*, the doctrine of frustration of contract and the principle of material adverse change. The first article in the series addresses *force majeure*.

## Force majeure

*Force majeure* is defined as “an event or effect that can be neither anticipated nor controlled. The term includes both acts of nature (e.g. floods and hurricanes) and acts of people.”<sup>2</sup> In its simplest form, *force majeure* refers to those situations outside the control of a party and which prevent the party from performing its obligations under its contract.<sup>3</sup> Initially a civil law concept found in the French Civil Code, *force majeure* found its way into English common law as far back as 1863<sup>4</sup> following a fire which razed the Surrey Gardens & Music Hall to the ground leaving the owners unable to perform their contractual obligations. In this matter, the English Courts held that absolute liability should only apply to definitive contractual obligations and not to those obligations to which there was an express or implied condition. The Court reasoned that the continued existence of the Music Hall was an implied condition essential for the fulfillment of the contract.

Over the years, the doctrine has been employed to either delay performance or alleviate liability for non-performance of obligations upon the occurrence of an extraordinary event beyond the control of the parties and which renders the performance of their obligations impossible.

<sup>1</sup> NSE hit by coronavirus pandemic as shares tumble (<https://www.nation.co.ke/business/Economic-cost-of-coronavirus-Kenya/996-5492854-gnf7jh/index.html>) 17 March 2020.

<sup>2</sup> Black Law's Dictionary

<sup>3</sup> Pankaj Transport PVT Limited v SDV Transami Kenya Limited [2017] eKLR

<sup>4</sup> *Taylor v Caldwell* [1863] EWHC QB J1

## Effect and operation of *force majeure*

*Force majeure* is a creature of contract. Accordingly, reliance on the doctrine will only work if there is a properly defined *force majeure* clause in a contract. Normally, a *force majeure* clause will provide a list of *force majeure* events, which if they were to occur, would excuse a party from performing its obligations under the contract for so long as the particular event continues.

The interpretation of a *force majeure* clause is usually strict and will depend on the wording of the clause, with due regard to the nature and general terms of the contract as a whole. Ordinarily, in addition to stipulating what will constitute a *force majeure* event, *force majeure* clauses will refer to performance being hindered, delayed or prevented. Consequently, depending on the impediment posed by the *force majeure* event and its effect, the remedies available to an affected party may include:-

1. Excusing the affected party from the delay in performance of its obligations and extending the time required to enable it to meet its obligations under the contract;
2. Entitling the affected party to suspend contractual performance for the duration of the *force majeure* event; or
3. Providing a platform for the renegotiation of the contract.

As a general rule, it is for the party invoking the *force majeure* clause to demonstrate that the clause applies, to prove that the event falls within the clause in the contract and that the event has prevented or delayed the performance of its obligations under the contract. This is the position taken by the High Court in *Pankaj Transport PVT Limited v SDV Transami Kenya Limited*<sup>5</sup> where Justice E.K. O. Ogolla stated “a party pleading *force majeure* must prove that the failure to perform an obligation was a result of impediment beyond his control and that he could not reasonably be expected to have taken the impediment and its effects upon his ability to perform the contract into account at the time of the conclusion of the contract; and that he could not reasonably have avoided or overcome it or at least its effects.”

From the decision in *Pankaj*, it is clear that three pertinent conditions must be fulfilled for a successful claim of *force majeure*:

1. Non-performance was due to circumstances beyond the control of the affected party;
2. The *force majeure* event was not foreseen at the time of concluding the contract; and
3. There were no reasonable steps that the affected party could have taken to avoid or mitigate the event or its consequence.

As the obligation to demonstrate the effect of the *force majeure* event is on the party claiming *force majeure*, it is incumbent on the party making the claim to notify the other party. As a result, it is important to confirm whether the affected party is obligated to serve the other party with a notice under the *force majeure* clause and what the notice requirements are before suspension of performance. If such a requirement exists, the affected party should comply with any set timelines and other requirements (such as to delivery) of issuing notices as most contracts will have specific notice and time-bar related clauses.<sup>6</sup>

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<sup>5</sup> *Pankaj Transport PVT Limited v SDV Transami Kenya Limited* [2017] eKLR

<sup>6</sup> ALN Covid Hub

## Would the pandemic fall within the concept of *force majeure*?

Whether a party can rely on *force majeure* under the current circumstances will depend first and foremost on whether such a clause was included in the relevant contract. If included, then whether the COVID-19 pandemic may be regarded a *force majeure* event will depend on (i) the actual wording of the clause, (ii) the nature of the party's contractual obligation and (iii) the actual impact of the pandemic on that obligation. A specific reference to an "epidemic" or a "pandemic" will make it easier to succeed on a *force majeure* claim. However, the failure to explicitly refer to an "epidemic" or "pandemic" is not necessarily a bar to relying on such a clause. If the clause does not use such specific language, the party will need to consider whether COVID-19 can be argued to fall under a general catch-all *force majeure* clause or under the concept an "act of God" or an "action by Government" if such wording is included in the contract, noting, however, that as *force majeure* is a creature of contract the Courts will be reticent to expand the agreed definition set out in a contract.

It is important to note that the *force majeure* event need not be COVID-19 itself. It is the consequences of COVID-19 and their impact on a party's ability to fulfill a contractual obligation, such as the inability to deliver goods into a particular territory, which will be relevant to any analysis. Such consequences may well come about through requirements for social distancing, travel restrictions, curfews or a full lock-down which would ordinarily be deemed to be outside of a party's control. However, such events must have translated into a physical or legal constraint to the party's ability to perform its obligations and not merely created additional economic hardship for the party.

A party seeking to rely on a *force majeure* clause in their contract should do so with care, because a wrongful claim could result in a finding of contractual breach or repudiation of the contract and could entitle the other party to claim damages or terminate the contract. In general, Kenyan Courts are unlikely to interpret *force majeure* against the plain meaning set out in the contract and will likely apply the *contra proferentem* rule<sup>7</sup> where there is any ambiguity in the drafting. Additionally a party should be careful not to invoke a *force majeure* clause if their own acts or omissions may have led to or exacerbated their inability to perform their obligations as the party seeking to rely on *force majeure* must be able to demonstrate that it has sought to mitigate the effects.

It is worth noting that there is relatively little Kenyan jurisprudence on the doctrine of *force majeure* and, as far as we are aware, there is no reported Kenyan case law on the operation of *force majeure* clauses in the context of epidemics or pandemics. This is also the case in jurisdictions to which Kenyan courts would have looked for precedential value, as a pandemic of this magnitude had not impacted the world in over 100 years. Accordingly, the courts in Kenya and elsewhere will have to grapple with novel issues that will set new precedents. What is certain is that any analysis of the applicability of a *force majeure* clause will be highly contextual.

Where a contract does not have a *force majeure* clause, a party may still rely on the common law principles of frustration and potentially on the doctrine of impossibility or impracticability of performance. We delve into these doctrines in our next article in the series.

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<sup>7</sup> The *contra proferentem* rule states that an ambiguous clause should be interpreted against the party that is seeking to rely on that clause.

## Key contacts

Should you have any questions on the impact of COVID-19 on your contractual agreements, please do not hesitate to contact [Dominic Rebelo](#), [Luisa Cetina](#), or your usual A&K contact:



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