How Force Majeure Differs In The US, Europe And China

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COVID-19 has had a grave impact on the energy industry, triggering delays and issues in the supply of both labor and materials. While the situation continues to change on a daily basis, it is of utmost importance that parties affected by COVID-19 familiarize themselves with their legal rights and obligations in order to be best placed to respond to the current turmoil.

This article looks at the impact of the pandemic on supply chains in the energy sector. Specifically, we use a hypothetical to shed light on some of the issues that are likely to arise in this context.

Consider an overseas oil and gas major that notifies its U.S. suppliers it will not take delivery of cargoes because of the spread of COVID-19, and the drastic measures taken by its government. This buyer seeks a force majeure exemption, claiming that these two events have prevented it from complying with its contractual obligation to receive delivery of the shipments.

This scenario raises the issue of whether a pandemic and related government measures may be characterized as a force majeure — an issue that is likely to be at the core of the majority of the energy sector disputes which come to fruition over the coming months.

Let's take a look at the buyer's arguments from a U.S., French, German and Chinese law perspective.

The Buyer's Arguments Under U.S. Law

The law in the U.S. varies to some degree from state to state. However, generally speaking, courts applying U.S. laws will enforce the terms of the parties' agreement even when that will result in harsh or difficult outcomes for one of the parties.

For that reason, the buyer should look to the terms of the contract, and identify whether the force majeure provision is likely to cover the current situation. If the provision mentions a pandemic, epidemic or health crisis, the buyer is likely to have good arguments for refusing the delivery.

Even if those specific terms are not present, there may be other broader categories in the force majeure provision that could apply. If the provision includes government action or labor or supply shortages, it may allow the buyer to claim force majeure.

If the buyer can fit the COVID-19 circumstances into the contract's force majeure clause, the next step is to determine whether the clause has been triggered. A force majeure clause usually requires performance of contractual obligations to be "prevented," "impeded,"

"hindered" or "delayed."

"Prevent" requires that the obstacle to perform is insurmountable — for example, that it is no longer physically possible or legally permissible to perform the contract. "Impede," "hinder" and "delay" can be construed more broadly, and do not require the affected party to prove impossibility to perform.

The buyer must carefully consider these terms, and their interpretation under the state law governing the contract. Finally, the buyer must consider whether and for how long the force majeure clause allows performance to be suspended, and any specific actions (notice, mitigation, etc.) that are required.

If there is no force majeure clause, or the event is not covered by the contract wording, the buyer may have other options, but they are likely to be limited. The buyer should consider whether the contract has provisions such as those dealing with material adverse change, price adjustment, liability limitations and exclusions, extensions of time, variations or changes in law (for example, laws prohibiting employees or transport from working, which slow down the supply chain) that may be helpful.

The buyer could also consider common law arguments, such as impossibility of performance or frustration of performance, to avoid taking delivery. But these doctrines tend to be difficult to establish, and should be considered only after all contractual provisions are evaluated.

The Buyer's Arguments Under French Law

Under French law, as under U.S. law, the first step is to check the terms of the contract. If a force majeure clause includes a reference to an epidemic or pandemic, the buyer will likely have good grounds to argue that nonperformance should be excused.

If the contract is silent on this matter, or does not contain a force majeure clause, the buyer may still be able to rely on the French Civil Code for assistance (or case law, if the contract was concluded before February 2016).

The Civil Code specifies three conditions for an event to qualify as force majeure. If met, they should also excuse the buyer from failing to perform its contractual obligations. First, the event must be unavoidable; that is, its effects could not have been avoided by taking appropriate measures.

Second, it must have been unforeseeable at the time the contract was entered into. Third, it should be beyond the control of the person relying on it. While French case law has generally been reluctant to recognize epidemics as force majeure events, the buyer could argue that today's drastic lockdown measures — not witnessed for at least 75 years — are exceptional and meet all three of these conditions.

The buyer would then need to establish a causal link between the force majeure event and its inability to perform. In doing so, the buyer could argue that the lockdown measures, applicable to it since it is considered part of a nonessential industry, prevented performance of its obligations.

The buyer should pay particular attention to this point, bearing in mind that under French law, the success of a force majeure claim often depends on the strength of the causal link between the force majeure event and the party's failure to perform.

The Buyer's Contract Under German Law

If the buyer signed a contract governed by German law, it would first have to look at the terms of the contract, as there is no fallback statutory provision regarding force majeure. Therefore, a careful review of contractual provisions will prove crucial to the buyer, enabling it to determine whether it is entitled to rely on a potential force majeure clause to suspend the contract's performance.

If the buyer finds that disease or pandemic (which would in principle cover coronavirus) is not a listed force majeure event, it would have to rely on the German courts to determine the parties' intent at the time of drafting the force majeure clause.

The buyer would need to show that the event was unavoidable and outside the parties' control, the two main criteria required for force majeure under German law. As under French law, the buyer will then need to show the causal link between the COVID-19 pandemic and its inability to receive shipment.

The buyer could also make the argument that it was impossible for him to comply with its contractual obligations due to strict government intervention. Indeed, in the absence of a force majeure clause, German statutory law allows for a contract to be amended or terminated as a result of events or circumstances that have made the continued performance impossible or excessively onerous.

Finally, the buyer could argue that circumstances have changed drastically since the time it initially entered into the contract with its supplier. German law allows for a contract to be amended if the circumstances that existed when the parties entered it have changed to a significant, unforeseeable extent, rendering performance of the contract unreasonable.

If the buyer does make that argument, it will have to demonstrate the exceptional nature of the COVID-19 epidemic, as German case law sets strict requirements as to the existence of such a change of circumstances.

The Buyer's Options Under Chinese Law

Under Chinese law, force majeure events are defined as unforeseeable, unavoidable and insurmountable events. To rely on a force majeure clause, there must also be a showing that the force majeure event caused the contract's nonperformance.

Therefore, the buyer's claim that the event was unforeseeable may be challenged on the basis that local laws and regulations specifically address the prevention and treatment of infectious disease. The buyer's claim will be further weakened as epidemics have historically been a frequent occurrence in the buyer's region.

The buyer could counter, however, that the global nature of coronavirus and the categorization of the disease as a pandemic sets this disease apart from previous epidemics, providing weight to the argument that this is an unforeseeable event. The buyer would then still have to show that there exists a causal link between the occurrence of the force majeure event and the contract's nonperformance.

Here, the buyer could argue that the local law requirements that trade be suspended as a result of the severe lockdown measures justifies nonreceipt of the cargoes. Of course, as under most legal regimes, the fact that the buyer gives its supplier timely notification and

sufficient evidence of its inability to perform the contract, and the reasons for its failures, will lend more weight to its argument, and will potentially help mitigate losses caused to the supplier.

Conclusion

The differences between the potential issues and solutions noted in this scenario highlight the importance of the governing law in determining the legal positions of parties affected by COVID-19. As such, the primary step to be taken by a party impacted by the consequences of COVID-19 should be to identify the governing law of their contracts.

Once the governing law of the agreement has been identified, parties will be in a better position to understand how their contract — including any force majeure clauses — will likely be interpreted, and to recognize other legal concepts that could be used to help the parties to navigate these turbulent times.

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