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Force Majeure Clauses

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SUMMARY

This paper considers a number of issues associated with the drafting and construction of force majeure clauses, including the general approach taken by the courts to the interpretation of such clauses, when failure of suppliers will constitute force majeure, the appropriate method of allocating shortfalls caused by force majeure events, notice requirements in force majeure clauses, whether acts of sub-contractors may constitute force majeure and whether events subsisting as at the time a contract is made may constitute force majeure.

INTRODUCTION

The purpose of a force majeure clause is to relieve a party of liability for inability to discharge its contractual obligations due to circumstances beyond that party's control, or beyond its reasonable control.

The need for such clauses arises due to the fact that contractual obligations are generally treated by the courts, in the absence of express stipulation to the contrary, as absolute.

In the absence of a force majeure clause, to be relieved of liability where it is unable to perform a contract due to circumstances beyond its control, a party must bring itself within the common law doctrine of frustration. However the operation of this doctrine is limited, in that to establish a contract has been frustrated it is necessary to show that the occurrence of an event, beyond a party's control, has so radically changed the situation in which the contract is to be performed that the contract should be regarded as having come to an end. The majority of events which are likely to prevent or hinder performance of an energy contract, such as supply failures, machinery breakdowns, failure to obtain approvals and shortages of specialist labour or equipment, will rarely, if ever, be regarded as having frustrated a contract.

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As a force majeure clause is a contractual mechanism, rather than an underlying common law doctrine, its effectiveness in protecting a party's position will depend upon the manner in which it is drafted.

Generally such clauses are drafted in a similar manner.

1. First there is a definition of "force majeure". For example:

   (a) an event beyond a party's control (or reasonable control) which by the exercise of reasonable care the party is not able to prevent or overcome; or

   (b) an event beyond a party's control (or reasonable control) which by the exercise of reasonable care, but excluding measures which are not economically or commercially feasible, the party is not able to prevent or overcome.

   Specific examples of force majeure events are then usually listed. Common examples include acts of God, industrial action, breakdown of machinery, inability to obtain approvals, failure of suppliers and native title claims. Certain clauses will effectively deem such examples to be force majeure events by providing that a force majeure event means "an event beyond the reasonable control of a party, including the following". Other clauses will provide that the examples only constitute force majeure events to the extent they are beyond the control of the relevant party; that is, "an event beyond the reasonable control of a party, including the following (provided they are beyond the reasonable control of the relevant party)".

2. It is usually then provided that a party affected by a force majeure event, or whose performance of a contract is hindered or prevented by a force majeure event, is relieved from liability to the extent it is unable to perform its contractual obligations due to the occurrence of that force majeure event.

3 The party affected by a force majeure event is generally required to use reasonable endeavours or reasonable diligence to overcome the effects of that event. A clause will often provide that an affected party is not relieved from liability from the time by which, by the exercise of reasonable care, it could have overcome the effects of the force majeure event.

4 Some form of notification obligation is usually imposed upon the affected party, requiring the affected party to provide details to their counterparty regarding the force majeure event. These details may include:

   (a) the nature and cause of the force majeure event;

   (b) its likely duration;

   (c) the means proposed to be adopted to overcome the effects of the force majeure event; and

   (d) evidence that the affected party has employed these means.

5. Most clauses expressly provide that a party is not relieved by a force majeure event of an obligation to pay a sum of money.

There have been a substantial number of cases considering force majeure clauses, particularly in England. Despite this, there is not an established body of law as to the manner in which such clauses operate and should be construed. Rather, the construction of a particular clause depends upon the particular words used in that clause and the intention of the parties as reflected in those words and the remaining clauses of the relevant contract.

The above said, a consideration of the case law highlights certain issues to which regard should be had in drafting a force majeure clause. The purpose of this paper is to examine certain of these cases, with the intent of highlighting these issues. The paper is not designed to provide a comprehensive overview of the case law, but rather focuses on the following issues:

1. When will failure of a sub-contractor constitute force majeure?
2. Can an event existing at the time a contract is entered into constitute force majeure?
3. When will a failure of a specific source of supply constitute force majeure?
4. How should a supplier allocate a shortfall caused by force majeure across multiple customers?
5. What is the effect of a failure to strictly comply with the notification requirements set out in a force majeure clause?

First this paper briefly considers the operation of the common law doctrine of frustration.

FRUSTRATION

Overview of the Doctrine

The common law doctrine of frustration acts to relieve parties of liability where, due to the occurrence of a supervening event beyond the control of the parties, there is a radical change in the circumstances in which a contract is to be performed.[1]

Whether an event constitutes a "frustrating" event depends upon the terms of the relevant contract and the facts of the particular case. Mere alteration of the circumstances in which a contract is to be performed is not sufficient to constitute frustration – rather there must be a radical change in such circumstances. This includes, but is not limited to, performance of the contract becoming impossible

[1] *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696 at 729 per Lord Radcliffe (approved *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675 at 688, adopted *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337).

due to the occurrence of the relevant event. The fact a bargain becomes less profitable due to a change in circumstances is not frustration.[2]

Formulations of the test of a frustrating event include:

(a) that the event must make further performance different in substance from that which was contracted for;
(b) that the event creates a fundamentally different situation from that contracted for; and
(c) that the event deprives a party with further obligations to perform of substantially the whole benefit which it was intended, as expressed in the contract, that he or she should derive from performance of those obligations.[3]

Examples of frustrating events include physical destruction of the subject matter of a contract, death or incapacitation of a person, state intervention, natural disaster and war. Terrorist acts, depending on their magnitude, could constitute frustrating events.

For an event to be regarded as a "frustrating event", generally it must have been unforeseeable at the time the contract was entered into.[4] Consequently, a contract cannot be frustrated by circumstances which were in existence as at the time of entry into the contract, by an event which was likely to occur or, even, by an event which although not likely to eventuate, would have been considered a possibility by the parties. The underlying logic is that if an event was foreseeable, the parties had the opportunity to provide for this expressly in the terms of the contract and the frustration doctrine should not operate.

Other limitations upon the operation of the doctrine are:

(a) the relevant event must not have been caused by the fault of either party;[5]
(b) the doctrine cannot be invoked where, despite the contemplated method of performance becoming impossible, there is a reasonable alternative method of performance;[6] and
(c) courts do not lightly find that a contract has been frustrated.[7]

At common law, where frustration occurs the contract is automatically discharged and the parties are released from performance of all further obligations. That is, termination for frustration does not require any election to be made by the parties but rather occurs automatically. A frustrated contract cannot

2 *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169, *Lindsay-Owen v Associated Dairies Pty Ltd* [2000] NSWSC 1095 at [11], *Western Power Corp v Normandy Power Pty Ltd* [2001] WASC 202 at [198].

3 *Halsbury's Laws of Australia* [110-9600].

4 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337 at 358.

5 See discussion in *Penrith Rugby League Football Club Ltd v Fittler* (1996) 40 AILR 5-087.

6 *Albert D Gaon & Co v Societie Interprofessionelle des Oleagineux Fluides Alimentaires* [1960] 2 QB 334, *Tsakiroglou & Co Ltd v Noblee Thorl GmbH* [1962] AC 93 ("The Suez cases").

7 *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169 at 200 per Latham CJ.

be reinstated, although the parties can, of course, always enter into a new contract. A frustrating event operates to discharge the whole of the relevant contract, even where a contract contains severable obligations. No right to claim damages arises due to a contract being frustrated.

Liabilities accrued prior to the occurrence of a frustrating event may continue to be enforced, after a contract has been discharged by frustration, where, prior to the occurrence of the frustrating event, the promisee possessed an unconditional right to enforce the relevant obligation. The test applied by the courts to determine whether such an unconditional right exists is whether the promisee would be entitled to recover the relevant amount in a claim for restitution based on a total failure of consideration.[8] This common law requirement that there be a total failure of consideration severely restricts the ability of a party to recover money paid, expenditure incurred or payment for work performed prior to a contract being frustrated.

Therefore, at common law, there is no mechanism for adjustment of the parties' position where a contract is frustrated but only a limited right to recover sums where there is a total failure of consideration. Certain of the States (New South Wales, Victoria and South Australia) have enacted legislation governing the adjustments to be made between parties to a frustrated contract with the aim of ensuring a more equitable outcome than that resulting from the application of the common law.[9]

Frustration as Compared to Force Majeure

The principal differences between the doctrine of frustration and "standard" force majeure clauses are:

(a) the doctrine of frustration is a common law doctrine, whereas a force majeure clause is a contractual term the contents of which are agreed by the parties. The parties to a contract can design a force majeure clause to operate in whatever manner they consider appropriate;

(b) for a contract to be frustrated there must be a radical change in circumstances, such that contractual obligations are required to be performed in a fundamentally different situation. Force majeure events are usually defined in considerably less strict terms. A force majeure event must, generally, be beyond the reasonable control of a party and not capable of being overcome by the exercise of reasonable means. However a force majeure event does not need to produce a radical change in circumstances. For example, in a two year gas supply contract, there could be a force majeure event which lasts for only two hours;

(c) frustrating events must generally not have been foreseeable. In the case of many force majeure events, such as machinery breakdown and failure of suppliers, while the parties may anticipate that it would be more likely than

[8] *Halsbury's Laws of Australia* [110-9900].
[9] *Frustrated Contracts Act* 1978 (NSW), 1959 (Vic), 1988 (SA).

not that such events will not occur, the events are certainly foreseeable possibilities; and

(d) frustrating events discharge a contract. The effect of a force majeure event depends upon what is provided for in the relevant force majeure clause. Certain clauses can extend the time within which performance is required. Other clauses relieve a party of liability for failure to perform during the period of force majeure but require performance to be resumed upon the expiration of the effects of the force majeure event. A contract will often provide that, where a force majeure event prevents performance for more than a certain period or affects performance beyond a certain magnitude,[10] that one or both parties may elect to terminate the contract. Many contracts will relieve the unaffected party (that is, the party not claiming force majeure) of the obligation to make payments for such period during which the party affected by force majeure is unable to perform its obligations.

In short, force majeure clauses allow parties the flexibility to provide expressly for the consequences which should follow where a party is unable to perform its obligations due to circumstances beyond its control. The frustration doctrine operates in a far narrower range of circumstances. Rarely, in the context of energy contracts, would a party which considers there is a risk it will be unable to perform its obligations due to circumstances beyond its control consider it satisfactory to rely upon the "protection" of the doctrine of frustration.

In contrasting the doctrine of frustration and force majeure clauses, it is also relevant to consider whether the inclusion of a force majeure clause will prevent the operation of the doctrine of frustration. This would appear to depend upon the width with which the relevant force majeure clause is drafted. Where a force majeure clause is drafted broadly so as to regulate all circumstances where a party cannot perform its contractual obligations due to events beyond its control, then there would appear to be limited scope for the doctrine of frustration to operate.[11]

In contrast, where a force majeure clause is drafted narrowly and does not regulate the consequences of the occurrence of certain events, the doctrine may still operate where those events occur.[12] Also, if a force majeure clause operated so as to suspend performance but did not address what should occur if performance is prevented for a substantial period of time, then it would be open for the courts to find, where performance ceases to be possible, that the relevant contract is frustrated.[13]

Given the unsatisfactory operation of the doctrine of frustration, particularly in relation to the regulation of the parties' rights upon a contract being discharged by frustration, if the parties do agree to regulate their relationship by way of a force

[10] For example, 50% of deliveries of a product cannot be made.

[11] *Claude Neon Ltd v Hardie* [1970] Qd R 93, *Empresa Exportadora de Azucar v Industria Azucarera Nacional SA (The Playa Larga)* [1983] 2 Lloyd's Rep 171 at 188, *Thors v Weekes* (1989) 92 ALR 131 at 142.

[12] *Bank Line Ltd v Arthur Capel and Co* [1919] AC 435, *Simmons Ltd v Hay* [1964-65] NSWR 416 (SC), *Wong Lai Ying v Chinachem Investment Co Ltd* (1979) 13 BLR 81 (PC).

[13] *Metropolitan Water Board v Dick, Kerr & Co Ltd* [1918] AC 119.

majeure clause it may be preferable if that clause is drafted widely so as to supersede the operation of the doctrine.

APPROACH TO INTERPRETATION OF FORCE MAJEURE CLAUSES

Discussion

As noted above, the overriding principle which has been developed by the courts in construing force majeure clauses is that the meaning of a force majeure clause depends upon the precise words used in that clause.

In interpreting such clauses, the general approach of the courts is to start with an assumption that parties are to be held to their contractual obligations and are not, in the absence of express stipulation to the contrary, to be released lightly from such obligations.

An example of how this starting assumption affects the court's approach to interpretation is the Canadian case of *Atcor Ltd v Continental Energy Marketing Ltd.*[14] In this decision the Alberta Court of Appeal, in interpreting the intended operation of a force majeure clause in a gas supply contract, placed principal emphasis upon its understanding of the commercial purpose of the clause.

The case concerned a gas supply contract between the plaintiff and the defendant which contained the following force majeure clause:

> "Subject to the other provisions of this paragraph, if either party to this Agreement fails to observe or perform any of the covenants or obligations herein imposed upon it and such failure shall have been occasioned by, or in consequence of force majeure, as hereinafter defined, such failure shall be deemed not to be a breach of such covenants or obligations.
>
> (a) For the purposes of this Agreement, the term 'force majeure' shall mean any acts of God, including therein, but without restricting the generality thereof, lightning, earthquakes and storms and in addition shall mean any strikes, lockouts or other industrial disturbances, acts of the Queen's enemies…well blowouts, craterings, pipeline tie-ins, pipeline connections, pipeline repairs and reconditioning, the orders of any court or governmental authority, the invoking of force majeure pursuant to any gas purchase contracts, any acts or omissions (including failure to take gas) of a transporter of gas to or for Seller which is excused by any event or occurrence of the character herein defined as constituting force majeure, or any other causes, whether of the kind herein enumerated or otherwise, not within the control of the party claiming suspension and which, by the exercise of due diligence, such party is unable to overcome.

[14] 38 Alta LR (3d) 229.

(b) Neither party shall be entitled to the benefit of the provisions of paragraph 9 hereof under any or all of the following circumstances…to the extent that the failure was caused by the party claiming suspension having failed to remedy the condition, and to resume the performance of such covenants or obligations with reasonable dispatch."

Due to compressor breakdowns and pipeline repairs, deliveries of gas by the pipeline operator to the defendant were curtailed. The defendant, relying on the above force majeure clause, curtailed deliveries to the plaintiff. It was agreed that the failure of the pipeline was an event within para (a). The trial judge held that, given the failure of the pipeline fell within para (a), the defendant was relieved from liability and was not under an obligation to look for a solution to alleviate the shortage in its gas supplies caused by the breakdown. He held that the seller was under no obligation to overcome the relevant event unless the event was within the seller's control.

The Court of Appeal held that the trial judge's interpretation was incorrect. It was contrary to the intention of the parties to interpret the clause in such a manner as to allow the defendant, effectively, to terminate the contract at will merely because an event disruptive to the defendant's business occurred. Rather the intention of the parties, and the framework against which the clause should be interpreted, was that the seller did not need to show that the relevant event made performance impossible but needed to show that the relevant event created, in commercial terms, a real and substantial problem. If the consequences of the event could be rectified by commercially feasible means, the defendant was required to employ such means.

The Court of Appeal stated:

"the obligation to mitigate by resupply must be commercially feasible. On the one hand, the supplier should not be able to cancel a contract merely because an expected profit will not occur as a result of new events. On the other hand, the purpose of the term is to protect the supplier from effects that are, in terms of what is commercially feasible or reasonable, out of his control. In sum, and in the absence of clearer words to the contrary, a supplier is not excused from non-performance by a force majeure event if the sole consequence of that event is to drive him to buy from another supplier and make a smaller profit. He is excused, however, if that solution, in all the circumstances, is not reasonable.

In my view, it is not often commercially reasonable to drive a supplier to make fundamental changes to the way he does business…Before us, Mr Yorke-Slater said that the supplier was a seller of gas, not a buyer of gas, and his client should not be asked to go into the market in a way fundamentally at variance with its business. With deference, however, the agreed facts provide that his client did not sell only gas from its own wells, but other gas from other producers, the purchase of which presumably was negotiated on the open market. Moreover, I think I should take notice that, in general terms, recent years have seen new developments in the commerce of gas

> supply. Those who distribute natural gas to consumers tend today to buy pipeline supply rather than well production, and brokers deal in that supply. A spot market now exists for natural gas. Are purchases on that market utterly foreign to the supplier's business. I see no evidence of that."[15]

The Alberta Court of Appeal did not consider the precise nature of the commercially feasible steps which should have been taken by the seller but rather remitted the matter for further hearing by the trial judge.

An example where consideration was given to this issue is the English Court of Appeal case of *B & S Contracts and Design Ltd v Victor Green Publications Ltd*[16] where the issue was the steps required to be taken by a party affected by a strike. The force majeure clause in that case provided:

> "Every effort will be made to carry out any contract based on an estimate, but the due performance of it is subject to variation or cancellation owing to an act of God, war, strikes, civil commotions, work to rule or go-slow or overtime bans, lock-out, fire, flood, drought or any other cause beyond our control."

The plaintiffs agreed, for a contract price of £11,731.50, to erect stands for an exhibition to be held by the defendants. The plaintiffs' work force (which had been notified it was to be made redundant) then went on strike over a demand for severance pay (to which pay the workers had no legal right). The defendants paid £4500 to the plaintiffs to pay to its workers to get them to resume work. The defendants deducted this from the contract price. The plaintiffs sued the defendants to recover the entire contract price. A question arose as to whether the plaintiffs could rely on the force majeure clause.

The Court of Appeal held that the plaintiffs could not rely on the clause. In the court's opinion the plaintiffs had to make every reasonable effort to perform the contract. The court considered the plaintiffs should, on the specific facts of the case, have paid the £4,500 to the workforce and that this was a "simple solution to the problem".

Griffiths LJ stated:

> "Clauses of this kind have to be construed upon the basis that those relying on them will have taken all reasonable efforts to avoid the effect of the various matters set out in the clause which entitle them to vary or cancel the contract…Quite apart from that general principle this particular clause starts with the following wording: 'Every effort will be made to carry out any contract based on an estimate,' which is saying in express terms that which the law will imply when construing such a clause."[17]
>
> "The plaintiffs were going to close down their subsidiary company; they had already dismissed the workforce and the men were working out their time. There is no question here of any ongoing industrial situation between the plaintiffs' subsidiary company and the workforce. There was no question of principle at stake; the plaintiffs were perfectly prepared to pay

[15] Paragraphs 35-36.
[16] [1984] ICR 419.
[17] At 426.

> what the men were demanding save for the fact, they said, they did not have the money available. Well, then there came the offer of the defendants to make the money available by giving them an advance. In those circumstances I can see no reason why they should not have accepted the money and paid the workforce save their own immediate economic interests, and they chose not to do that but to put pressure on the defendants by refusing the offer and indicating that the only way out was for the defendants to hand over the £4,500 as a gift rather than as an advance…I think that that was thoroughly unreasonable behaviour."[18]

It has also been a repeated theme of the courts in construing force majeure clauses that a reduction in profitability due to the occurrence of an event beyond a party's control is not force majeure.[19]

For example, in *B & S Contracts*, Kerr LJ noted that "mere difficulty of additional expense is not a sufficient ground to enable a party to invoke an exception clause".[20]

Brauer & Co (Great Britain), Ltd v James Clark (Brush Materials), Ltd[21] concerned a contract for shipment of goods from Brazil. The contract provided it was subject to any Brazilian export licence and also contained the following force majeure clause:

> "Should shipment be prevented or delayed owing to prohibition of export, revolution, riots, strikes, lock-outs, blockade, hostilities, force majeure or plague, shipper shall be entitled at the termination of such cause or causes to an extension of time for shipment prior to the outbreak of such cause or causes."

The sellers, subsequent to entry into the contract, found that the Bank of Brazil would only let them export the relevant goods at prices of £180 per ton and £135 per ton, which prices were £28 and £40 above the contract price. The sellers claimed the protection of the force majeure clause and subject to licence clause.

The Court of Appeal held neither clause protected the sellers. In respect of the subject to export licence clause Singleton LJ considered the sellers had failed to demonstrate they had taken reasonable steps to obtain a licence. He stated the sellers may have been entitled to rely on the clause had they been able to demonstrate they could not obtain a licence except on prohibitive terms or terms entirely outside the contemplation of the parties. However there was no such evidence in the present case.

Denning LJ stated:

> "this clause is a special exemption inserted in favour of the sellers. In order to enable them to take advantage of it they must show that, notwithstanding

[18] At 426-427.
[19] *Comptoir Commercial Anversois v Power, Son and Company* [1920] 1 KB 868; *Produce Brokers Ltd v Weiss and Co* (1918) 18 The Law Times 111, 23 March 1918.
[20] At 427.
[21] [1952] 2 All ER 497.

that all reasonable steps were taken by them, they could not obtain a licence to export during any part of the shipment period."[22]

His Lordship stated a price one hundred times higher than the contract price between the sellers and the buyers would create a fundamentally different situation entitling the sellers to relief. But a mere standard increase in market prices did not provide relief.

Another generally established principle is that a party must not have contributed to the occurrence of the relevant event claimed to be beyond its control. For example, in *Mamidoil-Jetoil Greek Petroleum Co SA and Moil-Coal Trading Co Ltd v Okta Crude Oil Refinery AD (No 2)*[23] the force majeure clause referred to "acts or compliance with requests of any governmental authority… beyond the control of the party affected". It was held that a party which had initiated the government on its line of inquiry which resulted in the government subsequently making a request that the contract not be performed, could not claim the benefit of this clause.[24]

Drafting Implications

The general approach of the courts appears to be to interpret force majeure clauses relatively strictly and to require a party claiming to have been affected by a force majeure event to demonstrate that it took adequate precautions to overcome the effects of the event. A party seeking to rely on a force majeure event must establish both the occurrence of the event and that the event could not have been overcome by the employment of reasonable measures.

Force majeure clauses are generally silent on the nature of the steps which are required to be followed by a party affected by a force majeure event or will describe such events in relatively general terms; for example, that a party will use reasonable diligence or undertake commercially or economically feasible steps. While such concepts might have meaning in the abstract, applying them in an actual force majeure situation and advising a party as to what steps it should take in such a situation is a difficult task. As each case depends on its own facts, the case law can provide little guidance other than indicating that the mere need to incur additional expense is not a justification for failing to pursue a step. Further even if a step will turn a profitable contract into a loss making contract this does not, of itself, mean that the step is not reasonable or commercially feasible.

Ideally the parties would specify with precision the nature of the steps which a party is required to take to overcome a force majeure event and the limitations

[22] At 501.

[23] [2003] 2 Lloyd's Rep 635.

[24] The court stated at 638: "The essential issue is whether, if it is the case that Okta instigated or initiated the requests contained in the November and May letters, they can rely on the letters as constituting 'requests…beyond their control.' Once the question is posed in that form, it is clear that they cannot, for the simple reason that they need not have set the process in motion at all. They could, instead, have decided to comply with their contractual obligations."

upon those steps. In practice, it will rarely be practicable to reach such a degree of precision nor are parties in a commercial negotiation likely to be able to agree upon the precise nature of the steps which are required to be taken to overcome a force majeure event. Nevertheless where a party has a significant degree of bargaining power it may be appropriate to give consideration to specifying, for example, that a seller is not required to source a product from an alternative source if the cost of that product from that source exceeds the price to be paid by the buyer (or exceeds the cost charged by the seller's standard source).

FAILURE OF SUB-CONTRACTORS

Discussion

Does a failure of a sub-contractor constitute force majeure? That is, where a party fails to perform its obligations under a contract due to the act or omission of a party to whom it has sub-contracted performance, is it entitled to claim force majeure? In one sense, such a failure is beyond the control of the party, since the party does not have direct control over its sub-contractor.

Force majeure clauses rarely appear to address this issue. However many contracts will provide that sub-contracting does not relieve a party of its obligations under the contract. This would suggest that a party generally could not claim force majeure in respect of the act or omission of a sub-contractor. But what if the relevant act or omission is one not contemplated by the relevant sub-contract?

There does not appear to have been a great deal of judicial consideration of this issue. However the matter was considered in a statutory context in *Re Atomic Skifabrik Alois Rohrmoser v The Register of Trade Marks*.[25] The *Trade Marks Act* 1955 permitted the Registrar to extend the period for lodgment of an objection to the registration of a trade mark if, due to circumstances beyond the control of the objecting party, the objection was not lodged within the time required by the Act. The applicant failed to lodge its objection within the required time due to the negligent omission of its patent attorney. The applicant argued this circumstance was beyond its control.

Jenkinson J of the Federal Court disagreed. The court held that circumstances beyond the control of the person concerned meant circumstances which "neither the person concerned nor any person acting on his behalf to do the act or take the step could prevent."[26]

The judgment did give examples of limited circumstances where the acts of an "independent" contractor may constitute an event beyond a person's control. The examples given were a mail carrier or office cleaner who destroyed documents which were meant to be filed. That is, acts or omissions of a contractor who had

[25] (1987) 7 IPR 551.
[26] At 558.

not been contracted to perform the specific obligations for which force majeure was claimed.

While this decision relates to interpretation of a statute, the judgment would seem equally applicable to a contractual force majeure clause. Therefore it would appear that, in the absence of a force majeure clause evidencing an intention to the contrary, a party will not be able to claim force majeure because a sub-contractor has failed to discharge its contractual obligations, unless the sub-contractor's own failure was caused by circumstances beyond its control.

Drafting Implications

It would appear the approach in *Skifabrik* would be adopted to interpret most force majeure clauses. The decision is consistent with what the courts are generally likely to regard as having been the intention of the parties.

Therefore if a party wishes to claim force majeure relief due to the default of its sub-contractors, it will be necessary to expressly provide for this in the relevant force majeure clause.

EVENTS EXISTING AS AT THE TIME A CONTRACT IS MADE

Discussion

Can an event existing as at the time a contract is executed constitute force majeure?

The authorities suggest that a pre-existing event can constitute force majeure but the matter depends on the wording of the specific force majeure clause and the circumstances of the specific contract and force majeure event.

An example where a pre-existing event was successfully relied upon as a force majeure event is *Reardon Smith Line Ltd v Ministry of Agriculture, Fisheries and Food*[27] where the issue was whether a strike could be relied upon as a force majeure event even though it was in existence as at the time the contract was made. Sellers LJ stated:

> "there is no settled rule of construction that a specific exception, such as strikes or war, cannot be relied upon if the strike or war was operative at the time when the contract was made or the ship ordered to the affected port. It must depend on the proper construction of the contract."[28]

The Court of Appeal, influenced by the fact that the strike was a matter of public knowledge (and therefore a matter of which both parties were aware when they made the contract) and the fact it was not inevitable the strike would still

[27] [1962] 1 QB 42.
[28] At 83.

operate when the charter party came to be fulfilled, held that the relevant force majeure clause did extend to apply to the strike.

In contrast, a force majeure clause did not provide protection against a pre-existing event in *Trade and Transport Incorporated v Iino Kaiun Kaisha Ltd*[29] where a force majeure clause in a charter party provided protection in the case of "shortages of cars, wagons…or other unavoidable hindrances in mining, transporting, loading, discharging or receiving the phosphate…and any other causes or hindrances happening without the fault of the charterer, shippers or suppliers of cargo, preventing or delaying the mining, supplying, loading, discharging or receiving of the cargo".

The charterers intended to load the cargo by means of a contract they had with an Israeli company, Tovala (who was the only company capable of providing the relevant transportation service). However, in breach of its contract with the charterers, Tovala was unable to supply sufficient lorries to enable the cargo to be loaded.

Kerr J rejected the contention that the charterers could not rely on the protection of the clause if the relevant hindrance was a breach of contract by their transport contractor:

> "An act or omission by someone in the position of a transport contractor, such as Tovala, with whom the charterers or shippers had to contract in order to enable the cargo to be brought to the port or to be loaded, is in my view within the clause if the state of affairs resulting from such act or omission could not have been avoided by the charterer or shipper."[30]

However Kerr J found that the charterers were unable to rely on the clause because Tovala's inability to perform its transport contract existed as at the time the charter party was made and the charterers would have become aware of this had they made appropriate inquiries. This applied even though Tovala's failure to provide the lorries was a breach of its contract with the charterers. Kerr J considered it would have been an ordinary business precaution for the charterers to verify with Tovala whether lorries were available. They had not done so and it was inconsistent with the underlying intent of the clause to excuse the charterers from liability for failure to take this ordinary business precaution. Drawing upon the judgment in *Reardon Smith* Kerr J found that a party could not rely upon a pre-existing cause as force majeure if:

(a) the pre-existing cause was inevitably doomed to operate on the adventure; and
(b) the existence of facts which showed that the excepted cause was bound to operate:
    (i) were known to the parties at the time of entry into the contract (or at least to the party seeking to rely on the exception); or

[29] *The Angelia* [1973] 1 WLR 210.
[30] At 224.

(ii) should reasonably have been known to the party seeking to rely upon them and would have been expected by the other party to the contract to be so known.[31] [32]

As pointed out by Kerr J, the difference between *Reardon Smith* and *The Angelia* was that, in *Reardon Smith*, both parties knew about the strike at the time they entered the contract and it was not inevitable the strike would still subsist at the time the charter party came to be performed.

Drafting Implications

Whether a party can rely upon an event existing as at the time a contract is entered into to found a claim of force majeure depends upon the wording of the relevant force majeure clause and also whether the existence of the event was known to one or both parties. Each case will turn on its own facts.

Therefore where a draftsperson knows that their client may wish to rely upon such an event, the relevant force majeure clause should be drafted so as to expressly acknowledge that it extends to events in existence as at the time the relevant contract was made.

FAILURE OF SUPPLIERS

Discussion

Where a supplier enters into a contract intending to supply its customer using a particular source of supply, and due to force majeure that source of supply becomes unavailable, is the supplier relieved of liability?

The case law indicates that the supplier is only relieved from liability:

(a) where pursuant to the relevant contract, the supplier's supply obligation is limited to an obligation to supply from that particular source of supply; or
(b) if not, where the supplier can demonstrate that there was no other source of supply from which it could obtain the relevant product.

For example, *In re Thornett & Fehr and Yuillis Ltd*[33] the defendant contracted to sell to the buyers two specified brands of Australian beef tallow. There was provision for delay, or eventual cancellation, of shipment in the case of force majeure. The defendant's Australian supplier failed to supply to the defendant the requisite quantity of beef tallow. However the court held that, as the contract was not a contract for the sale of goods from a specific source of supply, the mere fact that the defendant's intended source of supply failed did not permit the defendant to claim force majeure.

[31] At 227.
[32] Applied by the Full Court of the Tasmanian Supreme Court in *Asia Pacific Resources Pty Ltd v Forestry Tasmania (No 2)* (1998) Aust Contract R 90-095.
[33] [1921] 1 KB 219.

In *PJ Van Der Zijden Wildhandel NV v Tucker & Cross Ltd,*[34] the court considered a failure by the defendant to supply Chinese frozen rabbits due to the failure of its supplier. The court held that the defendants were unable to rely on the force majeure clause because they could not demonstrate that they could not have acquired Chinese frozen rabbits from an alternative source:

> "All that they have been able to show was that the imports of Chinese frozen rabbits into Holland were at all material times much smaller in quantity than the amount called for under these contracts. They have quite failed to obtain any finding from the arbitrator that they were unable to buy in Chinese frozen rabbits from some supplier other than the one with whom they have a contract. Unless they can do that, they are unable to show that they were prevented from fulfilling their contract by a cause beyond their control.
>
> The contract called for Chinese rabbits, cif. Their obligation was, therefore, to tender documents, not to ship the rabbits themselves. If there were any Chinese rabbits afloat, they could have bought them, and it is for the sellers to show that no such rabbits were available."[35]

George Wills and Sons, Ltd v R S Cunningham, Son and Company, Ltd[36] concerned a contract for the delivery of steel "unforeseen contingencies excepted". The contract did not identify a source of supply. Due to the French occupation of the Ruhr, the defendant was unable to access the steel from its intended source of supply.

Greer J stated:

> "The question is how the exception is to be applied to a contract which does not fix any particular source from which the goods are to come; had it done so the exception would have been much easier to interpret…It is not enough for the defendants to show that it was impossible for them to get the goods from the particular source they contemplated when entering into the contract. If they could have obtained goods elsewhere which would have satisfied the contract they were bound to do so."[37]

In *Exportelisa SA v Rocco Giuseppe & Figli Soc Coll*[38] the sellers contracted to sell to the buyers Argentinean wheat. The sellers intended to fulfil their contract by contracting with an Argentinean company. However the Argentinean government then extended its monopoly over wheat, such that the seller could only obtain wheat by purchasing it from the government at a price set by the government. This price was substantially greater than the price at which the sellers had contracted to sell wheat to the buyers.

The question before the court was whether the sellers could rely on the following force majeure clause:

[34] [1975] 2 Lloyd's Rep 240.
[35] At 242.
[36] [1924] 2 KB 220.
[37] At 221 to 222.
[38] [1978] 1 Lloyd's Rep 433.

> "Prohibition – should the fulfilment of this contract be rendered impossible by…any executive or legislative act done by or on the behalf of the Government of the country of origin of the goods…this contract or any unfulfilled part thereof, to be cancelled."

The court held that the sellers could not rely on this clause:

> "They are not so excused merely because, by reason of a change in Argentine law or by the act of the executive government in the Argentine, they may have been precluded from buying from a particular seller from whom they intended to buy in order to perform the contract: the circumstances being that, on the facts as found, they could have bought the goods, albeit at a much higher price, from another seller in the Argentine."[39]

The above cases demonstrate that, if a supplier intends to fulfil a contract from a specific source of supply, then to ensure that the supplier can claim force majeure if that source of supply is unavailable the relevant contract should specifically identify that source of supply as the means by which the contract will be fulfilled. A general reference to "force majeure" or "unforeseen circumstances" will generally not be sufficient to protect a supplier unless the supplier can establish that the relevant force majeure event affected all possible methods of performance.

These principles would equally apply where a contract is intended to be fulfilled by the use of a specific labour source, sub-contractor or by the use of specific materials.

Another example of this principle is the decision of the New South Wales Court of Appeal in *European Bank Ltd v Citibank Ltd.*[40] The case concerned the following force majeure clause:

> "Citibank will not be liable for any failure to perform any obligation in respect of an Account if the performance is prevented, hindered or delayed by…any event which occurs due to reasons beyond the reasonable control of Citibank so as to prevent the due performance of an obligation."

The appellant made a deposit in $US with Citibank. These funds were transferred by Citibank to a Citibank account in New York in accordance with the bank's usual procedures. The funds were then seized by a US Marshall. The appellant sued to recover its funds. Citibank claimed force majeure on the basis it had intended to pay the appellant using the funds held in the New York account and these funds were no longer available. The court rejected this argument. The contract between Citibank and the appellant did not specify that the funds would be repaid through the New York account and Citibank was still capable of fulfilling the contract by alternative means. Therefore it was not prevented from performing its obligation. There was nothing in the contract to suggest that the obligation to make payment was contingent upon Citibank being able to access specific funds held by Citibank.

[39] At 437.
[40] [2004] NSWCA 76.

Spigelman CJ stated:

> "Merely because both parties expect a contract to lead to certain consequences or to involve particular events, does not mean that the words used in the contract should be construed in such a way that a failure of the expectation affects contractual rights and duties."[41]

Also, in relation to failure of suppliers, the courts will not, as would be expected, relieve a supplier of liability where the supplier has assumed that its own suppliers or transporters are available to provide to it supplies or other services and has not entered into arrangements to ensure this is the case. For example,[42] the case of *Thomas Borthwick (Glasgow), Ltd v Faure Fairclough, Ltd*[43] which concerned the following force majeure clause:

> "Sellers shall not be responsible for delay in shipment of the goods or any part thereof occasioned by any Act of God, strike, lockout, riot or civil commotion, combination of workmen, breakdown of machinery, fire or any cause comprehended in the term 'force majeure'."

The sellers contracted to sell to the buyers, by a February 1996 shipment from Bathurst, groundnut cake expellers. A typed slip attached to the contract provided that shipment was to be effected by a West African Conference Lines vessel nominated for "contractual period of shipment". However no Conference Lines vessel was loaded at Bathurst in February 1996, due to a determination by Conferences Lines not to load at that port in that month.

The sellers claimed the protection of the force majeure clause. This claim was rejected by Donaldson J who stated:

> "The 'sellers' inability to ship in February resulted from the failure of the Conference Lines to put in a vessel to load during that month. This failure was not caused by any unforeseen or unusual peril such as collision, storm, breakdown of machinery or the closing of the Suez Canal. So far as is known the Conference simply decided not to provide a vessel to load cargo at Bathurst in February to carry it to Avonmouth. This is not in my judgment force majeure."[44]

Drafting Implications

Where a party intends to fulfil its contract using specific supplies, labour or materials and does not wish to be placed in a position, should those supplies, labour or materials be unavailable, where it is obliged to source alternative supplies, then the contract should expressly identify that it is to be performed using that specific source.

However even identification of such specific source may not, of itself, be sufficient to protect a party. A force majeure clause which requires a party to use

41 At [9].
42 See also *The Angelia,* op cit n 29.
43 [1968] 1 Lloyd's Rep 16.
44 At 28.

its reasonable endeavours to overcome the effects of an event could, arguably, be read as requiring the party to seek to obtain alternative supplies. Therefore the draftsperson should ensure that it is clear both that:

(a) the contract is to be performed using that specified source; and
(b) (assuming this reflects the commercial agreement of the parties), there is no obligation to seek to access another source of supplies, materials or labour if that specific source is unavailable due to the occurrence of force majeure.

Ultimately the extent of a party's obligation to endeavour to perform a contract using a different methodology from that contemplated depends upon the intention of the parties as reflected in the contract. In the case of a contract with a gas producer for the supply of gas from a specified basin, it may not be difficult to find an intention that there is no obligation to supply gas from an alternative source.

In contrast, in the case of a retail gas supply contract, it will be considerably more difficult, in the absence of an express provision to the contrary, to imply that a failure of the source from which the retailer traditionally sources gas relieves the retailer from performance where alternative sources of supply are available. Even if the contract were written at a time when there was only one source of supply and refers to that source (unless the contract specifies that source as the exclusive source of supply) a court may well consider, given that gas at a retail level is an unascertained good, that the retailer's obligation is to supply gas from such sources as are available from time to time.

ALLOCATION OF SHORTFALLS

Discussion

The majority of suppliers in the energy, mining and petroleum industries will have a number of customers. For example, gas producers will sell their production to a number of retailers and retailers will inevitably have a large number of customers. A pipeline operator will usually have a number of shippers utilising its pipeline.

Where a force majeure event impacts upon a party's ability to supply a product or services (for example, transportation services) then that party will need to make a decision as to how to allocate the resultant shortfall between its customers. However in many circumstances force majeure clauses are silent as to the mechanism for allocation of such a shortfall. In such cases, determining the manner in which a shortfall is to be allocated is a matter of determining the parties intent as reflected in the drafting, and surrounding circumstances, of the relevant contract.

Is Allocation Permitted?

There is, of course, an initial question as to whether the force majeure clause will permit allocation of shortfalls at all. It may be that a clause will not permit a

supplier to claim relief if it is able to supply its counter-party's requirements even though the supplier is unable to supply the requirements of each of its customers. Such was the conclusion reached by the Privy Council in the case of *Hong Guan & Co Ltd v R Jumabhoy & Sons Ltd*.[45] The case concerned an importer of cloves (the respondent) who had contracted to sell to the appellants, in December, 50 tons of Zanzibar cloves "subject to force majeure and shipment". The respondent shipped, in December, sufficient cloves to supply the 50 tons but shipped insufficient cloves to meet its commitments to its other customers. The respondents allocated the cloves it did ship to its other customers and allocated none to the appellant.

The Privy Council held that the respondent was not entitled to rely on the force majeure clause/subject to shipment clause. The respondent could not rely on its obligations to its remaining customers as a basis for relief from its obligation to the appellant. The court stated:

> "Their Lordships are clearly of the opinion that the respondents cannot be allowed to excuse their non-performance by reference to their other commitments, or to seek to give those other commitments priority over the appellants' claim. The contract of November 7 contains no reference to other contracts or other commitments. Such other commitments were of no concern to the appellants. The contract was simply a contract for the sale by the respondents of cloves of the quantity and description set out in the contract, and the respondents failed to fulfil their obligations to the appellants.
>
> Apart from these considerations their Lordships find it difficult to see how it can be said that the 50 tons were 'shipped in fulfilment of other contracts.' If it is asked: 'Which contract or contracts?' no satisfactory answer can be given and none was given. The respondents urged that the words 'subject to shipment' meant 'subject to our in fact shipping enough to satisfy our commitments' or 'subject to our shipping enough to satisfy all contracts that we will have made up to the date of arrival of the last ship of December shipments.' In their Lordships' view it would be quite unreasonable and would be an unwarranted straining of interpretation to place any such meaning upon the words now being examined."[46]

In short, the respondent's responsibilities to its other customers were irrelevant to the appellant. The contract between the respondent and the appellant made no reference to such other customers nor gave any recognition to the fact that the respondent may need to allocate a shortfall between multiple customers.

There was no suggestion in the judgment that the respondent's position would have been different had it allocated the shortfall between all of its customers. The basis of the judgment was that, as long as the respondent had sufficient supplies of cloves to fulfil its obligation to the appellant, it could not rely on the force majeure/subject to shipment clause.

[45] [1960] AC 684.
[46] At 701-702.

The strict, and arguably commercially impractical, approach taken in *Hong Guan* in part reflected the drafting of the force majeure/subject to shipment clause. In other cases the courts have taken an approach to construction of force majeure clauses which would appear more practical. For example, the House of Lords decision in *Tennants (Lancashire) Ltd v CS Wilson & Company Ltd*[47] which case was referred to in *Hong Guan* but distinguished. In that case, the force majeure clause provided:

> "deliveries may be suspended pending any contingencies beyond the control of the sellers or buyers…causing a short supply of labour, fuel, raw material, or manufactured produce, or otherwise preventing or hindering the manufacture or delivery of the article."

The relevant contract was for the supply of magnesium chloride. Due to the outbreak of World War One there was a shortage of the product. The defendants were able to procure, at a substantially increased price, sufficient magnesium chloride to satisfy their obligations to the plaintiff but insufficient quantities to supply the requirements of all their customers.

The majority of the House of Lords held that the defendants were entitled to rely on the clause. For example, Earl Loreburn stated: "To place a merchant in the position of being unable to deliver unless he dislocates his business and breaks his other contracts in order to fulfil one surely hinders delivery."[48]

Viscount Haldane stated:

> "I do not see how the appellants could have lawfully delivered to the respondents without also delivering proportionately to the other firms with whom they had entered into similar contracts. They were either bound to all their customers equally or they were not bound to any of them."[49]

Lord Dunedin stated:

> "They [the respondents] say, however, that if the appellants had supplied them in preference to all others there would have been sufficient for them. It is obvious that if this is a good answer each of the other contracting parties could have made it in turn, damages would have been due to all, and the clause would be no protection whatever."[50]

The different results in *Hong Guan* and *Tennants* appear to reflect the drafting of the force majeure clause in each case. In *Tennants*, the court regarded the force majeure clause, in particular its reference to hindering, as acknowledging the existence of customers of the defendant in addition to the plaintiff and requiring regard to be given to these customers in determining the extent of the relief provided by the clause. The force majeure clause in *Hong Guan* did not permit regard to be had to other customers.

47 [1917] AC 495.
48 At 510.
49 At 511-512.
50 At 515.

A similar case to *Tennants* is *Pool Shipping Co, Ltd v London Coal Co of Gibraltar, Ltd*[51] where the force majeure clause referred to events which "prevents the supply, shipment, carriage or delivery of all or any one or more of the descriptions of coal herein contracted for…or the normal working of this contract". Branson J held that the phrase "normal working of this contract" indicated that in construing the contract the court was to consider the seller's contractual commitments to other customers.

Methods of Allocation

While the matter has not been conclusively settled, the judicial trend is, where a force majeure clause is silent as to the appropriate allocation method, to permit/require a supplier to allocate shortfalls between its customers, so long as the supplier does so on a reasonable basis.

In *Bowring & Walker Pty Ltd v Jacksons Corio Meat Packing (1965) Pty Ltd*[52] Macfarlan J considered the appropriate manner in which to allocate shortages in the ability to export meat caused by the imposition of Commonwealth export quotas. A entered into a contract to sell B 100 tons of meat and bone meal for shipment in February 1969. A then entered into a contract to sell another 100 tons to C for shipment in the same month. The contract between A and C provided: "This sale is made subject to export quota permits being issued by the Australian Department of Primary Industry allowing export shipment during February 1969." However A was only allocated a quota of 100 tons. A allocated the 100 tons to its contract with B.

To interpret this provision, MacFarlan J had regard to normal practice in the industry, including how that practice was shaped by the Commonwealth's quota system. He considered that he was entitled to have regard to such practice as the contract between A and C was a short form "commercial contract", clearly intended to be interpreted as a commercial document and having regard to commercial practice. In light of this practice, he held that the clause permitted A to allocate the 100 tons it was allowed to export to its contracts on the basis of the date upon which those contracts were entered into. This was consistent with general practice in the industry and therefore was, he held, A's and C's intention as to what should occur if A was not allocated sufficient export quotas to fulfil each of its contracts. He did not consider the contract contemplated a pro-rata allocation due to the practical difficulties this would raise, though his Honour's judgment did not specify what these practical difficulties were.

The issue of shortfall allocation was considered by Lord Denning MR in *Intertradex SA v Lesieur-Tourteaux SARL*.[53] Lord Denning MR, agreeing with the trial judge, stated that where a force majeure clause was silent as to the method of allocating shortfalls between customers, then the shortfall should be allocated on a

[51] [1939] 2 All ER 432.
[52] [1972] 1 NSWLR 277.
[53] [1978] 2 Lloyd's Rep 509.

basis which was proper and reasonable having regard to the practice in the industry in which the parties were engaged. Such practice may require a pro-rata allocation, a chronological allocation or allocation on some other basis.

In *Bremer Handelsgesellschaft mbH v Continental Grain Co*[54] the English Court of Appeal also accepted the principle that shortfalls should be allocated on a basis which is reasonable having regard to the circumstances of the relevant case. The Court of Appeal stated that to successfully claim the protection of the force majeure clause under consideration in that case the sellers had to establish that the method they used for allocation of a shortfall was "at least a reasonable method of allocating any available goods between buyers, although not necessarily the only method".[55]

The Court of Appeal quoted with approval from the 1979 unreported judgment of Goff J in *Westfalische Central-Genossenschaft GmbH v Seabright Chemicals Ltd* where his Honour stated there was no general rule that pro-rata apportionment was always appropriate:

> "No doubt, if apportionment pro rata is carried out it will generally be regarded as reasonable; but it will not invariably be required – for example, if the quantity available is too small to be sensibly apportioned among the relevant purchasers; or his storage problems or a perishable product require one purchaser to be preferred to another."[56]

In *Atcor*, the Alberta Court of Appeal rejected the plaintiff's submission that the defendant had a positive duty to distribute the available gas supplies proportionately amongst its customers.[57] The court agreed with the Court of Appeal in *Bremer v Continental* and stated:

> "any decision must turn on the commercial circumstances of the case…the supplier had to show that this decision [ie its allocation decision] was, in all the circumstances, reasonable. I emphasize again that this means reasonable in commercial terms."

The above English authorities were approved by Brownie J in the New South Wales Supreme Court case of *Cobelfret (UK) Ltd v Austin & Butta (Sales) Pty Ltd*.[58] Indeed Brownie J also appeared to adopt the position in American law that a supplier pro-rating "may set aside allocations for regular customers not under contract at the time when the shortage occurred."[59]

While the matter is not conclusively settled, and will ultimately depend upon the construction of the specific contract, the clear judicial trend is that a supplier should allocate shortfalls in a manner which is reasonable having regard to the nature of, and practice in, the industry in which they operate. However, at a practical level, a supplier which experiences a shortage caused by force majeure is

[54] [1983] 1 Lloyd's Rep 269.
[55] At 293.
[56] Quoted at 293.
[57] Paragraph 18.
[58] Unreported 24 February 1988.
[59] At 59.

still faced with the difficulty of determining what is the appropriate allocation procedure for their particular industry. In certain circumstances, this procedure may be readily apparent but this will not always be the case.

Drafting Implications

Given the ambiguity as to how shortfalls caused by force majeure are to be allocated, and also the possibility that a court could find, as in *Hong Guan*, that no allocation is permitted, where a party supplies a number of customers, that party should, generally, ensure that its force majeure clauses set out a procedure for the allocation of shortfalls between those customers. In the absence of such a procedure the party will need to make a determination as to what is a reasonable method for allocating shortfalls. The party may be exposed to liability if it selects a method which the courts regard as unreasonable. That is, in the absence of stipulating an appropriate procedure in its contracts, a party runs the risk that it will adopt an allocation procedure which will not be accepted by the courts.

When considering an appropriate shortfall allocation method to include in a contract, it is important to have regard to the extent to which, practically, a party will be able to comply with that allocation methodology. While an allocation methodology may look effective on paper, under the pressure of a force majeure situation, it may not always be possible for a party to comply with a prescriptive allocation method.

If shortfalls are to be allocated according to prescriptive criteria, it would be preferable, from the supplier's perspective, to provide that a party is only required to use reasonable endeavours to comply with the relevant procedure (or is required to comply with the procedure to the extent practicable having regard to the circumstances of the force majeure event). Equally a buyer will usually wish to see the use of a methodology which is relatively transparent and prescriptive so as to ensure that, in a shortfall situation, its entitlements are nevertheless maximised and that it can verify it has received an appropriate share of the relevant product or service as compared to the supplier's remaining customers.

Where a supplier uses a prescriptive methodology for the allocation of shortfalls, the supplier will need to ensure that all of its customer contracts incorporate the same methodology, or at least that customer A's contract does not contain provisions preventing the use of the relevant methodology against customer B. Depending upon the strength of a supplier's negotiating power, it may not be possible to ensure this. This is another reason that a supplier should seek to incorporate a flexible rather than a prescriptive method for the allocation of shortfalls.

NOTICE REQUIREMENTS

Discussion

Force majeure clauses generally require a party which wishes to claim the benefit of the clause to:

(a) provide notice to the other party of the occurrence of the relevant event, either within a specified time of the event occurring or within a reasonable time; and

(b) provide various information to the other party in relation to the relevant event – for example, details of the event and a description of the steps being taken by the affected party to remedy the event or overcome its effects.

Rarely will a force majeure clause specify the consequences of a failure to comply with such notification requirements. Does a failure to comply mean the affected party cannot rely on the force majeure clause? Alternatively does the failure merely give rise to a claim for damages in respect of any loss arising due to a failure to give notice?

The leading case on this issue is the House of Lords decision in *Bremer Handelsgesell-Schaft Schaft mbH v Vanden Avenne-Izegem PVBA*.[60] In *Bremer* the House of Lords held that:

(a) where the notice requirements are properly construed as a condition, failure to comply with those requirements will prevent the relevant party claiming force majeure; and

(b) where the notice requirements are an "intermediate" term, failure to comply with them will not prevent a party claiming force majeure, unless such failure seriously prejudices the other party. However the party claiming force majeure will be liable for any damages suffered by the other party due to its failure to comply with the notice requirements.

Whether notice requirements constitute a condition or an intermediate term depends on the form of the force majeure clause (in particular upon the precision and strictness of the notice requirements) and its relationship to the contract as a whole. Generally notice requirements are regarded as intermediate terms.

In *Bremer* the following clause was construed as an intermediate term:

> "In case of prohibition of export … preventing fulfilment, this contract or any unfulfilled portion thereof so affected shall be cancelled. In the event of shipment proving impossible during the contract period by reason of any of the causes enumerated herein, sellers shall advise buyers of the reasons therefor."

The absence of precise time limits for the service of notices indicated that the clause was intended to operate as an intermediate term.

[60] [1978] 2 Lloyd's Rep 109.

In contrast, the strict time limits and comprehensive nature of the following clause indicated that it was to be treated as a condition:

> "Sellers shall not be responsible for delay in shipment of the goods or any part thereof occasioned by any Act of God, strike, lockout, riot or civil commotion, combination of workmen, breakdown of machinery, fire or any cause comprehended in the term 'force majeure'. If delay in shipment is likely to occur for any of the above reasons, Shippers shall give notice to the Buyers… within 7 consecutive days of the occurrence, or not less than 21 consecutive days before the commencement of the contract period, whichever is later. The notice shall state the reason(s) for the anticipated delay. If after giving such notice an extension to the shipping period is required, then Shippers shall give further notice not later than 2 business days after the last day of the contract period of shipment."

Drafting Implications

The more comprehensive and precise the notification requirements in a force majeure clause, the more likely that clause is to be treated as a condition. Where a clause only requires a party to give notice within a reasonable time, then it is more likely to be construed as an intermediate term.

The parties can, of course, put the matter beyond doubt by setting out in a force majeure clause the consequences of failure to comply with the notice requirements of that clause. For example, by providing that a failure to strictly comply with the clause does not prevent a party relying on the clause if the party has substantially complied with the notice requirements or made a good faith attempt to comply with those notice requirements. However this appears to be done rarely.

From the perspective of the party more likely to rely on a force majeure clause (usually the supplier), it is preferable not to include strict notification requirements and precise time limits. There is a significant risk, particularly in the case of a major force majeure event, that a party will fail to comply with such requirements. In drafting the notice and information provision requirements of a force majeure clause, regard should be had to what practically, in the circumstances of an actual event, could be achieved.

Another issue often overlooked in drafting force majeure notice requirements is the effect of confidentiality clauses. A clause may require a party to disclose information which is subject to confidentiality obligations under another contract. Suppose Party X is a gas retailer to Party Y. Party X is unable to supply Party Y due to a machinery breakdown affecting its supplier, Party Z. Party X therefore wishes to claim force majeure as against Party Y. To do so Party X must, by virtue of the notification requirements in its contract, provide to Party Y details of the force majeure event. However the contract between Party X and Party Z contains a general confidentiality clause providing that all information in connection with that contract is confidential. Party X is therefore, potentially, in a position where it must either breach the confidentiality clause in its contract with Party Z or risk

being unable to claim force majeure because it is unable to provide sufficient information to Party Y.

This situation would appear common, particularly as confidentiality clauses are sometimes inserted into contracts as boilerplate clauses with insufficient regard being given to their application to the specific circumstances of the contract. Authorities concerning the construction of confidentiality clauses suggest the courts are reluctant to read down their express terms or read implied exceptions to them.[61]

To avoid the conflict in its obligations to Party Y and Party Z, Party X would either need to have:

(a) made its obligation to disclose information to Party Y subject to any confidentiality obligations owed to Party Z; or
(b) included in its contract with Party Z a right to disclose information to the extent necessary to manage its obligations under its downstream contracts.

The first solution is unlikely to be palatable to Party Y, since it will reduce the amount of information Party Y receives concerning the force majeure event and further reduce Party Y's ability to verify the authenticity of the claim.

In respect of the second option, Party Z may well oppose this due to:

(a) the general reluctance of commercial parties to agree to any disclosure of their confidential information; and
(b) also a concern that it is more likely to encourage actions by Party Y against Party Z (for example, in negligence), if Party Y is informed that Party Z is the cause of the interruption in supply.

When placed in such a conflict situation, Party X is presumably more likely to breach the confidentiality clause in its contract with Party Z than risk being unable to claim force majeure as against Party Y. If Party X cannot effectively claim force majeure it may leave itself exposed to an action in damages. While breaching a confidentiality clause is also a breach of contract, it is less apparent what damage Party Z suffers from this breach. Also, in the case of a major disruption, at least some information relating to Party Z is likely to enter the public domain and therefore will not be subject to confidentiality obligations.

From the perspective of a party who is required to be provided with information pursuant to a force majeure clause, a difficulty which will commonly arise is the means by which that party can assess the validity and accuracy of the information provided to it.

Force majeure clauses generally require the party claiming force majeure to provide information, in reasonable detail, to the other party as to the nature, and cause, of the event of force majeure as well as to the steps taken by the relevant party to remedy the force majeure.

[61] See *Queensland Coal Pty Ltd v Arco Resources Ltd* (2002) 2 Qd R 288; *Centaur Mining & Exploration Ltd v Anaconda Nickel Ltd* (2001) 19 ACLC 1,375; *Magbury Pty Ltd v Hafele Australia Pty Ltd* (2002) 210 CLR 181.

In practice, a party claiming force majeure will generally provide insufficient information to enable the other party to assess the validity of its claim of force majeure. The information that is provided will be presented with a slant so as to bolster the apparent validity of the claim of force majeure. However given the vagueness of criteria such as "reasonable detail" it is very difficult for a party receiving information to dispute the accuracy of information provided to it or establish that additional information must be provided.

Therefore where a party makes a claim of force majeure, it will generally be very difficult for its counterparty to determine whether that claim is valid. Short of obtaining an order for pre-trial discovery or bringing an action and thereby obtaining discovery of documents, there is little a party can do to obtain sufficient information as to the force majeure event, unless the force majeure clause itself is drafted so as to provide a mechanism by which a party may access such information.

Examples of such mechanisms are:

(a) including a requirement that the party claiming force majeure provide to the other party such information as requested by the other party concerning the alleged force majeure event; or
(b) a right to appoint an auditor or expert to conduct an independent review of the validity of the claim.

It may be difficult to successfully negotiate the inclusion of such mechanisms, but the matter should be considered, particularly in contracts where it is more likely the other party will seek to rely on the benefit of the force majeure clause.

FORCE MAJEURE CLAUSES WHICH PROTECT A BUYER

Discussion

Force majeure clauses will often be expressed so as to operate for the protection of both parties to a contract. However as the obligations of a buyer are usually limited to an obligation to pay for goods supplied to it and ancillary obligations, a force majeure clause is, practically, of more protection to the seller.

The principal circumstance in which a force majeure clause is used to protect a buyer is against the operation of take or pay provisions or provisions requiring the payment of fixed charges. Energy contracts will often provide a buyer with take or pay relief or fixed charge relief where it is unable to take delivery of a product due to a force majeure event. However clauses providing this relief need to be carefully drafted to ensure that they provide a buyer with the commercial protection it requires. Merely because, due to force majeure affecting a part of its business, a buyer's demand may be reduced does not necessarily mean a buyer cannot take delivery.

Also a general force majeure clause providing that a party is relieved from performance to the extent prevented by circumstances beyond its control is

unlikely to relieve a buyer from a take or pay obligation. This is because the take or pay obligation is a payment obligation and a strike, explosion, failure of a pipeline or other similar event does not prevent a buyer making a payment. If it is intended to provide a buyer with relief from a payment obligation where demand or ability to take delivery of product is affected by force majeure type events, the contract should expressly provide for this.

The Ontario High Court case of *Transcanada Pipelines Ltd v Northern & Central Gas Corp Ltd*[62] considered the circumstances of buyer force majeure, though the conclusions reached by the trial judge in that case are not entirely consistent with the above commentary. The force majeure clause in that case provided:

> "In the event of either Buyer or Seller being rendered unable, wholly or in part, by force majeure to perform or comply with any obligation or condition hereof…such party shall give notice…and the obligations of the party giving such notice, other than obligations to make payments of money then due, so far as they are affected by such force majeure, shall be suspended during the continuance of any inability so caused but for no longer period, and such cause shall as far as possible be remedied with all reasonable dispatch.
>
> The term 'force majeure' as used herein shall mean acts of God, strikes, lockouts or other industrial disturbances…any act or omission (including failure to deliver gas) of a supplier of gas to, or a transporter of gas to or for, Seller which is excused by any event or occurrence of the character herein defined as constituting force majeure, any act or omission by parties not controlled by the party having the difficulty and any other similar causes not within the control of the party claiming suspension and which by the exercise of due diligence such party is unable to prevent or overcome."

Due to strikes and explosions affecting its customers there was a reduction in the amount of gas sold by Northern. Northern claimed that, due to these events, which it argued fell within the scope of the clause, it was relieved of its obligation to pay fixed demand charges.

The appeal court rejected Northern's approach.[63] It considered that force majeure events were, unless expressly provided to the contrary, limited to events affecting the parties to the relevant contract. "As a general rule, it would seem to be appropriate to limit the application of a force majeure clause to force majeure events besetting the parties to the contract."[64] In the case of Transcanada (the supplier) there was a clear intention to extend the ambit of the clause to matters affecting Transcanada's suppliers. There was no similar intent to extend the protection of the clause to matters affecting Northern's customers.

The trial judge reached a similar view. However the trial judge also went on to consider what would have been the case had the force majeure clause extended to events affecting Northern's customers.[65] Assuming this was the correct view of

[62] (1981) 128 DLR (3d) 633.
[63] *Transcanada Pipelines Ltd v Northern & Central Gas Corp Ltd* (1983) 146 DLR (3d) 293.
[64] At 300.
[65] This matter was not considered before the Court of Appeal.

the clause, the trial judge rejected Transcanada's argument that in any event Northern was not unable to pay demand charges. The trial judge stated:

> "Transcanda's obligation under the service contract was to stand ready to 'sell and deliver' gas to Northern if and when requested by Northern; Northern's obligation was to 'purchase and receive…such quantities of gas each day as Buyer may request.' The force majeure clause addresses itself to the inability 'wholly or in part…to perform or comply with any obligation' under the contract. This I interpret to mean either the inability to take gas or the inability to supply gas. The obligation to pay demand charges is not the primary obligation of Northern; rather it flows from Transcanada's obligation to deliver if and when called upon to do so. As a result, I would have found, had the force majeure clause applied to the strikes and explosion, that it rendered Northern 'unable wholly or in part', to perform its obligation to 'purchase and receive' such quantities as it might request."[66]

Drafting Implications

Despite the conclusion of the trial judge in *Transcanada* it is submitted there is a significant risk a court will not find (in the absence of an express provision) that a buyer is relieved from fixed payment obligations where a buyer's demand or ability to take delivery of a product is affected by events beyond its control. To ensure a buyer is entitled to payment relief in such circumstances, the relevant contract should be drafted so as to expressly provide for a reduction in the payment of fixed or take or pay charges in such circumstances.

Similarly a reduction in demand does not necessarily mean that a buyer cannot take delivery of a product. Therefore if a buyer wishes to claim a reduction in demand (including due to events affecting its customers) constitutes force majeure, then the relevant force majeure clause should expressly provide for this.

CONSEQUENCES WHERE FORCE MAJEURE AND FRUSTRATION DO NOT APPLY

Where a party is prevented by a supervening event from performing its obligations under a contract and is unable to rely on a force majeure clause or the doctrine of frustration then that party will be liable to damages.

The supervening event may also trigger a right to terminate the contract if:

(a) it triggers an express termination right included in the contract; or
(b) it results in a failure to comply with an essential term of the contract (in which case there will arise a right to terminate at common law, unless such right has been excluded by the terms of the relevant contract).

[66] At 641.

Similarly a supervening event may result in a party being regarded as having repudiated its contract. If, due to a supervening event, a party is, or will be, no longer able to perform a contract, then that party may be regarded as having repudiated that contract.

In the case of both termination for breach of an essential term and repudiation, it is irrelevant that the supervening event and a party's inability to perform did not arise due to a "fault" of that party. In the absence of a force majeure clause, a party takes the risk of the occurrence of events beyond its control.

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