

# COVID-19 or Oil Price Crash' Competing Causes for Termination for Force Majeure

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**PRACTICES** Energy, Power and Natural Resources, Europe, Middle East and Africa, Oil and Gas, Litigation

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On 8 March 2020, Saudi Arabia initiated a price war with Russia which has caused a major fall in the price of oil. This is disastrous for an industry that had only just recently recovered from the 2014 crash and companies are now looking at how to best get through another difficult downturn.

On 11 March 2020, the World Health Organisation declared that the outbreak of COVID-19 was a pandemic, and in the following weeks, many countries have imposed major travel restrictions and ordered people to stay at home to slow the spread of the coronavirus.

In the wake of this, there has been a spate of contract terminations in the oil and gas industry, many parties claiming an entitlement to do so based on force majeure, but what is the real reason for these terminations? Under English law, it is well established that, in order for a force majeure claim to be valid, the force majeure event must be the sole cause of performance having been prevented or delayed. In the circumstance, you may wonder whether a number of these terminations are genuinely due to COVID-19 or whether this is simply a convenient mechanism to attempt to get out of a contract that is no longer looking profitable.

## **Do these events constitute force majeure?**

The decline in oil price is almost certainly not force majeure. Many companies will be suffering from the reduction in oil price and may choose to cut down on discretionary spend until such time as the oil price may recover, however, this is a commercial decision and it is not likely to be caught by a standard force majeure clause.<sup>1</sup>

The outbreak of COVID-19 on the other hand, may well be a force majeure event. It is not uncommon for force majeure clauses to refer to pandemics as a force majeure event. In the alternative, many clauses include “acts of government” or “changes in law” and the current restrictions on travel that are being caused by COVID-19 are likely to fall into that category.

## **Causation**

At present, it seems that most parties will find themselves in circumstances where they are affected both by the oil price decline and by COVID-19 and they may therefore wish to reduce their expenditure and take steps to ensure they can survive in this difficult climate. In doing so, they may look to see which contracts they are able to terminate.

However, a company taking the decision to terminate in these circumstances must be very clear on why it is terminating and it should not assume that it can rely on the contractual force majeure provisions where there are other reasons, which do not constitute force majeure, that may be preventing it from performing its contractual obligations. In the case of *Seadrill v Tullow* [2018], there was a force majeure event preventing drilling in a certain area. However, there were also

practical and economic difficulties that did not constitute a force majeure event preventing drilling in another area. The judge held that whilst the force majeure event had in some respects prevented Tullow from performing, there were other reasons that contributed heavily to Tullow's decision to stop drilling and terminate the contract. In the circumstances, the judge held that Tullow was not entitled to rely on the force majeure event to excuse its non-performance.

In a subsequent case of *Classic Maritime v Limbungan* [2019] the Court of Appeal found that the party that claimed that it was entitled to be excused from performance because of a dam burst would not have performed the contract even if there had been no dam burst and therefore was not excused from performance.

If a company is actively looking to reduce expenditure due to the oil price crash, or if it knows that it is likely to be prevented from performing due to financial difficulties, it may be prevented from terminating contracts for force majeure on the grounds of COVID-19 and should seek legal advice before giving any force majeure notices. This is particularly important given that unlawful termination of a contract is likely to be a repudiatory breach of the contract giving rise to a claim for damages.

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[1] It may be possible for parties to negotiate a clause that states that a decline in oil price constitutes a force majeure, however, it is more likely that a party may have a right to terminate for convenience, which is a right that usually comes with some sort of payment or compensation to the other party.