

English Law COVID-19 Q&A Series ? Ship Refit and Repair Contracts

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PRACTICES Shipping Dispute Resolution, Ship Construction and Conversion, Europe, Middle East and Africa, Shipping

Does the Covid-19 pandemic (or actions taken to counter the spread of Covid-19) constitute a Force Majeure in a refit/ repair contract? Is there any implied right of relief for the contractor or the owner?

Under English law, unlike civil law systems, a force majeure is neither defined nor automatically applicable to commercial contracts.

In order for a party to be excused for non-performance of a contractual obligation by relying on the force majeure principle, the contract must explicitly incorporate a force majeure clause (such clause often headed “*Disruptions*” in refit/repair contracts) which can either have a closed list providing for specific events that would constitute force majeure events, or a wider definition such as “events outside the parties’ control”.

The Covid-19 outbreak may potentially fall under multiple force majeure categories. It will almost certainly be covered in a repair/refit contract that includes a “pandemic” or “epidemic” as a force majeure event (which became common practice following the SARS and MERS outbreaks). Though “pandemic” is the most obvious option in the current scenario, it may also be possible to rely on other force majeure events, provided these are included in the pertinent clause of the contract, such as “quarantine,” “entry and exit restrictions,” “restraint of princes, rulers or people” or “requirements of government authorities,” especially in cases where the contractor’s employees’, contractor’s suppliers’ and/or contractor’s sub-contractors’ performance has been hindered due to a measure imposed to curb the spread of Covid-19.

As an alternative to the force majeure principle, a party may seek to rely upon the English law doctrine of frustration. Frustration requires the presence of a supervening unforeseen event through no fault of the parties that has occurred after the formation of the contract. For an event to be a frustrating event, it must make performance of the contract illegal, impossible or radically different from what was anticipated by the parties. If a party establishes that its performance of the contract has been frustrated, then the contract is automatically terminated, and parties discharged from any future performance. The threshold to establish frustration is typically very high as it provides for the existence of strenuous circumstances and severe events that undermine the purpose of the contract.

In the context of a refit/repair contract that anticipates pandemics as a possible force majeure event and legislates for how any associated delay is dealt with, it is unlikely that frustration will be an available remedy. However, it is possible that supply contracts could be frustrated which in turn would have an impact on any force majeure claim by the contractor.

If the Covid-19 pandemic (or actions taken to counter the spread of Covid-19) constitutes Force Majeure what might that mean for:

A) the contractor?

For the contractor to trigger a force majeure clause, depending of course on the specific wording of the contractual provision, the following requirements need to be satisfied: a) there is a force majeure event within the meaning of the contract; and ii) the force majeure event is preventing or delaying the contractor from performing the contractual obligation, i.e. any delay claimed must be due to/ caused by the force majeure event.

The drafting of the force majeure clause will require careful considerations as the clause may only apply to events that occur after the delivery of the vessel to the refit/repair yard by the owner, which in turn may mean that the contractor is unable to rely in the force majeure clause in the event the owner seeks to deliver the vessel in accordance with the contract but the contractor is itself prevented from taking delivery of the vessel.

It is also important in clauses where giving notice of the force majeure is a condition precedent to claiming an extension of time that the notice requirements have been fully complied with (the force majeure notice provision should be carefully reviewed to determine if the notice is in fact a pre-condition to claiming an extension of time).

The contractor should also be aware of any provisions imposing an obligation on the party seeking to invoke a force majeure event to mitigate losses and effects of the force majeure event.

Additionally, the contractor who is successful in invoking a force majeure event is usually entitled to an extension of the contract period or the contractual re-delivery date, subject to any duties to mitigate such delay. However, the contractor should be mindful that if the aggregate number of days of delay due to force majeure event and/or certain of the delays exceed a prescribed number of days, the owner may (although this is not usually a term of many standard form repair/refit contracts) be entitled to terminate the contract and claim damages (to the extent the relevant claims and/or losses are not excluded or capped under the contract).

B) the owner?

Refit/repair force majeure clauses primarily benefit the contractor as they do not typically confer any rights to the owner. Accordingly, even if the Covid-19 pandemic falls within the scope of the force majeure clause and prevents (or delays) the owner performing certain of its contractual obligations (for example, delivery of the vessel to the refit/repair yard on the contractual delivery date, completion of any “owner’s work”, provision of “owner’s supplies” to the refit/repair yard, maintenance of an owner’s representative at the refit/repair yard, maintenance of crew – which in turn could impact ability to comply with insurance obligations) or exercising certain of its contractual rights, the force majeure clause is unlikely to afford the owner any rights or benefits.

As a result, the owner could find itself in breach of contract or unable to exercise its rights and will need to carefully consider the relevant clauses in the contract to determine the consequences this could have with respect to the refit/repair of the vessel and the contractor’s rights.

Significantly, refit/repair contracts rarely include any form of cap on the extension of the contract period or re-delivery date, and therefore if there is a protracted extension to the contract (which may well be likely with the rolling extension of Covid-19 restrictions in many countries) a prudent owner should take legal advice before deciding to terminate a refit/repair contract for delays or other failure by the contractor to perform the works.

Also, the owner may face difficulty to even make milestone payments (for example if the owner is unable to drawdown on its intended source of funding). This is likely to trigger a contractual termination right for the contractor. Whilst contractual cure periods may provide some leeway to the owner, if there is a concern that this may happen, it may be prudent for the owner to take early steps to ensure that payment can be made and, if not, reach out to the contractor to see if an extension of time for payment can be agreed (noting that the contractor may also be concerned with issues relating to its ability to perform its own contractual obligations).

Are there wider practical considerations for a contractor in the face of the Covid-19 pandemic?

As the Covid-19 pandemic is likely to have wide reaching global economic repercussions, the contractor should closely monitor the solvency of the owner, any guarantor and if applicable, any project the vessel is intended to service after re-delivery.

The contractor's supply chain may well be disrupted, impacting the ability of the contractor to source material and equipment. The contractor may wish to review the extent to which its contracts afford it rights to substitute materials and/or equipment with/without the owner's consent, and whether the contract provides for a closed "makers' list". In circumstances where the contractor is being delayed because the contract limits the ability to make substitutions, the contractor should further consider its obligations under the force majeure clause, which may provide that the contractor shall take reasonable steps to overcome or mitigate any delay. In some circumstances, this may potentially extend to using different suppliers or materials. In the event this creates a tension between the mitigation obligation and the makers list, it may be necessary to seek legal advice and/or seek to reach an agreement with the owner.

Additionally, due to governmental travel restrictions and national "lockdowns", service of a notice may become a more complicated process, for example if the contract provides for hand-delivery of notices (although English law typically, in the absence of contrary provisions in the contract, treats courier delivery as hand-delivery) and the owner is not maintaining a representative on site). Accordingly, the contractor should, so far as possible, consider any requirement to give a notice well in advance so that the contractor complies with any notice related time limits.

To the extent that the contractor has required the owner to maintain (and provide copies of) certain insurances, the contractor should review whether any of the owner's insurances require the owner to maintain certain crew/representatives at the refit/repair yard.

Are there wider practical considerations for an owner in the face of the Covid-19 pandemic?

As the Covid-19 pandemic continues, the owner should closely monitor the solvency of the contractor. If the contractor goes into liquidation/ becomes insolvent, then the contractor may be in default under the refit/repair contract so as to give rise to a right for the owner to terminate.

Another practical difficulty that the owner may well face is mobilising or maintaining its supervision team and/or crew at the refit/repair yard. With multiple countries operating "lockdown" policies, the owner may struggle to position its representatives, and as a result, its ability to supervise refit/repair, attend trials and inspections could be severely impacted. It would be prudent to check the extent to which the contract allows the contractor to proceed with construction absent such owner's representation/supervision and attendance at trials and inspections. If the contract provides (as they usually do) that the contractor is able to proceed with works, then it may be worth the owner exploring different ways in which the contractor can evidence/report construction, trial

results, etc., to the owner. It may be possibly useful in those circumstances for the contractor to provide more detailed reports to the owner and consider whether use of photographs and video footage can be used to update the owner and demonstrate the refit/repair works are in accordance with the terms of the contract.

If a vessel is close to re-delivery, lack of crew onboard the vessel will severely restrict the owner's ability, *inter alia*, to remove the vessel from the refit/repair yard after re-delivery. The owner should carefully review its insurances and its contractual obligation to remove the vessel and the consequences of failing to do so as it may be necessary for the owner to negotiate arrangements with the contractor whereby the re-delivered vessel can remain at the refit/repair yard with minimal or no crew onboard.

Additionally, due to governmental travel restrictions and national "lockdowns", service of a notice may become a more complicated process, for example, if the contract provides for hand-delivery of notices (although English law typically, in the absence of contrary provisions in the contract, treats courier delivery as hand-delivery) and the owner is not maintaining a representative on site. Accordingly, the owner should, so far as possible, consider any requirement to give a notice well in advance so that the owner complies with any notice/ consent related time limits.

The owner should also review the vessel's employment arrangements ex-yard. Ideally, the re-delivery of the vessel under a charter party or other form of employment will be tied to the actual re-delivery of the vessel under the refit/repair contract. If not, the owner should review the relevant contracts and their late /non-delivery arrangements.

The owner should carefully review its insurances to determine if they would be negatively impacted by an inability of the owner to maintain a representative/crew at the refit/repair yard. Additionally, the owner should carefully review the contractor's insurances to determine if they contain any minimum manning or inspection requirements with which the contractor is to comply.

If a refit/repair contract is entered into now, will any of the contracting parties have an immediate right to postpone the "Delivery Date" or the "Re-Delivery Date" as a result of the ongoing Covid-19 pandemic?

One of the central elements of the drafting of most force majeure clauses is the "un-foreseeability" of the occurrence of the force majeure event when the contract is signed. Given the obvious impact the ongoing Covid-19 pandemic is already having around the world, it may well be difficult for the contractor to establish that Covid-19 pandemic related disruptions and/or delays constitute a force majeure event entitling the contractor to extend the contract period and/or postpone the "Re-Delivery Date" of the vessel unless the parties amend/waive the requirement for a force majeure event to be unforeseeable.

As mentioned above, it is unlikely that the contract will afford the owner any right to postpone the date or amend the condition in which the vessel is to be delivered to the refit/repair yard. As such the owner should carefully consider its ability to comply with the delivery date and delivery condition and as appropriate include a contractual mechanism to vary these and/or set a cap on the owner's liability arising from a failure to deliver the vessel to the refit/repair yard as required by the Contract.

As both the contractor and the owner may face challenges in their ability to perform their contractual obligations, it would be prudent at the outset for each party carefully to consider its contractual obligations, its potential liabilities and exposures should it fail to perform such

contractual obligations and its ability to cap liability as well as its ability to terminate the contract rather than risk protracted extension of the contract period and the re-delivery date.