

International Arbitration Alert

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The English Court of Appeal applies ‘but for’ test to “Force Majeure Clause” – FIDIC’s “Exceptional Events” now under threat?

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International Construction Arbitration has received a shock. Consistent with the leading textbooks, a party seeking to rely on force majeure in a construction contract did not have to show that ‘but for’ the force majeure event it would have performed its obligations. That approach is now under threat. We say this because the English Court of Appeal in *Classic Maritime Inc v Limbungan Makmur Sdn Bhd* [2019] EWCA Civ 1102 has made it clear that there is no default position whereby it is unnecessary to prove ‘but for’ causation in order to rely on a “force majeure clause” or a so-called “exceptions clause”. If words in the particular clause indicate a causation requirement, the party seeking to rely on the force majeure clause will need to pass the ‘but for’ test. Patently, this is an important decision for all employers and all contractors because force majeure clauses or Exceptional Events (under the FIDIC 2017 suite of contracts) feature in all international construction contracts, typically have a link to causation and are considered a fundamental right to additional time and money. Express amendments to such clauses may now be required in order to best reflect the parties’ commercial agreement. Arbitrators in International Construction Arbitration will see an increase in the application of the ‘but for’ test in the context of Exceptional Events, force majeure and exceptions clauses.

The Court of Appeal held that the force majeure clause required the party to show that the force majeure event (a dam burst) was **the** cause for its default so that ‘but for’ the dam burst it would have complied with its contractual obligations. The Court found that the ‘but for’ test had not been satisfied as the party would have defaulted irrespective of the dam burst. Contractors should thus be aware that if there are ‘competing causes’ for a contractual default they may be unable to rely on a force majeure clause even though it would have been impossible to perform the relevant obligations. There is a similar debate in the context of concurrent delay to completion. It is therefore of fundamental importance that construction contracts specify with precision who should bear the risk for events beyond the parties’ control including whether a given event should be a force majeure event and whether ‘but for’ causation is required.

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The Court of Appeal Approach: Causation

Classic Maritime Inc v Limbungan Makmur Sdn Bhd considered a contract under which a charterer was required (but failed) to provide a number of shipments of iron ore pellets from Brazil to Malaysia. The contract included a force majeure¹ clause which stated:

*Neither the Vessel, her Master or Owners, nor the Charterers, Shippers or Receivers shall be Responsible for loss or damage to, or failure to supply, load, discharge or deliver the cargo **resulting From:** (...) accidents at the mine (...); or any other causes beyond the Owners', Charterers', Shippers' or Receivers' Control; **always provided that any such events directly affect the performance of either party under This Charter Party. If any time is lost due to such events or causes such time shall not count as Laytime or demurrage (unless the Vessel is already on demurrage in which case only half time to count).***

The charterer relied on this clause to argue that it was exempted from liability because the dam burst was a force majeure event. It was common ground that the dam burst classified as an “accident at mine” which was “beyond the (...) Shippers' control”. In addition, it was undisputed that: (i) due to the dam burst, it would have been impossible for the charterer to provide the shipments in accordance with the contract; but (ii) the charterer would have defaulted regardless of the dam burst. The Court was asked to determine whether:

- the force majeure clause required the charter to prove that ‘but for’ the dam burst it would have performed its contractual obligations; or
- the charterer could rely on the force majeure clause even though it would have defaulted regardless of the dam burst, meaning that the dam burst was not the ‘real’ cause of its default.

In respect of “contractual frustration” clauses, the English Courts have typically followed approach (b) so that a party relying on such a clause does **not** have to prove ‘but for’ causation (based on the House of Lords decision in *Bremer Handelsgesellschaft mbH. v Vanden Avenne-Izegem PVBA*²). Prior to *Classic Maritime Inc v Limbungan Makmur Sdn Bhd*, it may have been thought that the Court would apply the same approach to so-called force majeure clauses. However, the Court distinguished this strand of case law because contractual frustration clauses are different in nature from force majeure clauses and held that there is no general principle that ‘but for’ causation is not required in cases of ‘contractual impossibility’. Instead, the Court stressed that a force majeure clause must be interpreted like any other contractual clause: construed as a whole and in accordance with the “modern iterative approach” to construction as set out in *Wood v Capita Insurance Services Ltd*³. The label of the clause is not determinative because “*what matters is not the label but the content of the tin*”⁴. In *Classic Maritime Inc v Limbungan Makmur Sdn Bhd*, the Court of Appeal relied on a number of features of the clause which, in combination, indicated that ‘but for’ causation was actually required. This included the parties’ choice to use words such as “resulting from”, “directly affects” and “causes”⁵.

The FIDIC 2017 suite of contracts uses the term “Exceptional Events” to provide relief against performance. It is now arguable that the FIDIC contracts do require compliance with the ‘but for’ test. We say this because the FIDIC suite uses words “*If a Party is or will be prevented from performing any obligations under the Contract due to*

an Exceptional Event ...” and because relief in terms of an extension of time requires the Exceptional Event to cause delay to completion. Clause 18.2 of the Yellow Book states:

If a Party **is or will be prevented** from performing any obligations under the Contract due to an Exceptional Event (the “affected Party” in this Clause), then the affected Party shall give a Notice to the other Party of such an Exceptional Event, and shall specify the obligations, the performance of which **is or will be prevented** (the “prevented obligations” in this Clause).

This Notice shall be given within 14 days after the affected Party became aware, or should have become aware, of the Exceptional Event, and affected Party shall then be excused performance of the prevented obligations from the date such performance is prevented by the Exceptional Event. If this Notice is received by the other Party after this period of 14 days, the affected Party shall be excused performance of the prevented obligations only from the date on which this Notice is received by the other Party.

Thereafter, the affected Party shall be excused performance of the prevented obligations for so long as such **Exceptional Event prevents the affected Party from performing them**. Other than performance of the prevented obligations, the affected Party shall not be excused performance of all other obligations under the Contract.

However, the obligations of either Party to make payments due to the other Party under the Contract shall not be excused by an Exceptional Event.

In a situation where a contractor is in a period of culpable delay and then suffers an Exceptional Event, Arbitrators in International Construction Arbitration governed by English Law and dealing with a 2017 FIDIC contract will need to decide if the Exceptional Event “prevented [the contractor] from performing any obligations” and/or caused a delay to completion or whether the culpable delay prevented the contractor or caused the delay to completion. The tangible temptation to follow the Court of Appeal’s analysis in *Classic Maritime Inc v Limbungan Makmur Sdn Bhd* may provide a real difficulty for contractors.

The Court of Appeal Approach: Measure of Damages

The Court at first instance had held (like the Court of Appeal) that the force majeure clause did not exempt the charterer from liability, but it awarded only nominal damages to the ship owner. It reasoned that, because the dam burst had made contractual performance impossible, the measure of damages should be based on the difference between: (i) the position the ship owner was in now; and (ii) the position the ship owner would have been in had the charterer been willing to perform. The judge found that the shipowner was – in effect – in the same position as under scenario (ii) because the charterer would not have been able to perform its contractual duties due to the dam burst.

The Court of Appeal rejected this reasoning and held that the ship owner was entitled to substantial damages in the sum of US\$ 19,869,573. Because of its finding that the force majeure clause did not apply (because the ‘but for’ requirement had not been satisfied), that clause could not be invoked to **reduce the amount of damages**. The Court clarified that the correct measure for damages was the difference between (i)

the position the ship owner was in now; and (ii) the position the ship owner would have been in *had* the charterer performed the contract (even though such performance would, on the facts, have been impossible). The Court affirmed that there is no basis under English law to take account of the *reason* for a contractual breach when assessing damages.

We understand that the decision has been appealed to the United Kingdom Supreme Court.

***Classic Maritime Inc v Limbungan Makmur Sdn Bhd* [2019] EWCA Civ 1102; [2019] 6 WLUK 422 (Court of Appeal (Civil Division))**

1 The Court of Appeal did not find the attempt to distinguish between clauses on the basis of the labels “contractual frustration clauses”, “exceptions clauses” and “force majeure clauses” helpful. The latter two labels are typically understood to deal with events that give relief from performance of certain obligations as opposed to automatically cancelling the contract.

2 [1978] 2 Lloyd’s Rep 109.

3 [2017] UKSC 24.

4 *Classic Maritime Inc v Limbungan Makmur SDN BHD* [2019] EWCA Civ 1102 at paragraph 62.

5 *Classic Maritime Inc v Limbungan Makmur SDN BHD* [2019] EWCA Civ 1102 at paragraph 39 - 47.

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