

LEGAL IMPACT ON CONTRACTS ARISING FROM THE COVID-19 PANDEMIC AND MOVEMENT CONTROL ORDER



Arising from the implementation of a nationwide Movement Control Order (“MCO”) announced by the Malaysian Prime Minister from 18 March 2020 to 14 April 2020 to curb the spread of global Covid-19 pandemic cases (“Covid-19”), many local and multinational businesses are adversely affected and hindered from carrying out their contractual obligations. The following common questions then arise:-

- (a) Whether a party affected by Covid-19 may rely on a force majeure clause from fulfilling their contractual obligations?
- (b) For a contract without a force majeure clause, what are the options available to an affected party?

(A) Whether a party affected by Covid-19 can rely on a force majeure clause?

Force majeure is not an implied provision and will only apply if parties have specifically incorporated the same in their contract to excuse performance when, inter alia:

- (a) performance has been rendered impossible to fulfil or something radically different from what was originally contemplated; or;
- (b) performance becomes commercially impractical because of extreme and unreasonable difficulty, expense, injury or loss; or
- (c) the value of performance is destroyed by unforeseen circumstances which are beyond the reasonable control of the parties.

Whether Covid-19 falls within the force majeure clause?

Whether Covid-19 may be classifiable as an unforeseen circumstance falling within the definition of force majeure would largely depend on the factual circumstances of each case. Generally, a party relying upon a force majeure clause will be required to prove the occurrence of the unforeseen circumstances which were beyond the control of the parties which prevented, hindered or delayed the performance under the contract and that there were no reasonable steps which could have been taken in order to avoid or mitigate the event or its consequences¹.

Although it is likely that Covid-19 will be deemed as an epidemic or pandemic amounting to a force majeure event, the specific circumstances of each contract still needs to be considered.

It is pertinent to note that establishing a force majeure event by itself does not automatically discharge the affected party from its contractual obligation(s) in its entirety. It merely allows the affected party to temporarily suspend its performance without liabilities until such time the contract is revived upon the cessation of the force majeure event². Having said that, there are some force majeure clauses which allow the affected party to terminate the contract for a prolonged force majeure event, after a specific period of time has elapsed.

In order to rely upon a force majeure clause, the affected party ought to notify the other party as soon as the force majeure event is discovered.

¹ Intan Payong Sdn Bhd v Goh Saw Chan Sdn Bhd [2004] 1 LNS 537
Magenta Resources (S) Pte Ltd v China Resources (S) Pte Ltd [1996] 3 SLR 62
Chitty on Contracts, 28th Edition Vol.1

² Yong Toi Mee & Anor v Malpac Capital Sdn Bhd & Anor [2013] 6 MLJ 453

(B) For a contract without a force majeure clause, what are the options available to an affected party?

In the event a contract does not specifically provide for a force majeure clause, the affected party may rely on **Section 57(2) of the Contracts Act 1950** which provides for the doctrine of frustration.

Whether a contract is frustrated as a result of Covid-19?

A contract is not frustrated merely because it becomes difficult to perform³. A contract is frustrated when a supervening event occurs that renders a contract physically impossible of performance and/or unlawful to perform.

An affected party who is desirous on relying on Section 57(2) of the Contracts Act 1950 ought to prove the following:-

- (a) the circumstances upon which a party relies as having frustrated the contract must have been one for which no provision has been made in the contract. If provision has been made, then the parties must be taken to have allocated the risk between them;
- (b) the circumstances must be one for which the party is not responsible. It means that self-induced frustration is ineffective; and
- (c) the circumstances which is said to discharge the contractual obligations must be such that renders performance radically different from that which was undertaken by the contract. The court must find it practically unjust to enforce the original promise⁴.

Consequences of Frustration

A contract discharged by frustration becomes void.

Section 66 of the Contracts Act 1950 provides the remedy of restitution when a contract becomes void whereby any person who has received any advantage under the agreement or contract is bound to restore it, or to make compensation for it, to the person from whom he received it.

The law further provides restitution as a remedy for a frustrated contract under **Section 15 of the Civil Law Act 1956** whereby:-

- (a) all sums paid or payable to any party pursuant to the contract before the time when the parties were so discharged, shall, in the case of sums so paid, be recovered from him or cease to be payable⁵;
- (b) if the party to whom the sums were so paid or payable incurred expenses before the time of discharge, the court may, if it considers it just, allow him to retain or recover the whole or any part of the sums so paid or payable⁶; and
- (c) any party to the contract who has obtained a valuable benefit before the time of discharge, there shall be recoverable from him by the other party such sum, as the court considers just⁷.

³ Pacific Forest Industries Sdn Bhd & Anor v Lin Wen-Chih & Anor [2009] 6 MLJ 293

⁴ Guan Aik Moh (KL) Sdn Bhd & Anor v Selangor Properties Bhd [2007] 4 MLJ 201

⁵ Section 15(2) of the Civil Law Act 1956

⁶ Section 15 (2) of the Civil Law Act 1956

⁷ Section 15(3) of the Civil Law Act 1956

STEPS TO BE TAKEN

STEP (1) Check your contract

Check your contract in order to establish what has been expressly agreed upon between the parties. It is important to identify the governing law clause, the force majeure clause (if any) and the default clause.

STEP (2) Record Keeping

Ensure that you have proper records of the adverse effect(s) suffered as a result of Covid-19 and the steps taken for mitigation.

STEP (3) Notify

Notify your counter-party on an ongoing basis of the problems you are facing as a result of Covid-19 and steps taken by you to address the same.

STEP (4) Mitigate

Mitigate your losses.

STEP (5) Follow the news

Keep a close watch on the developments and government directives/action.

KEY CONTACTS



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Partner



YAP JYY HUEY
Partner



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Associate

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