

Is It a Bird? Is It A Plane?

*Categorising COVID-19 Events into
“Force Majeure” Versus “Change of Law”*

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Introduction

The COVID-19 pandemic has had far-reaching impacts on discharge of contractual obligations by suppliers *and* on financial performance, both private and public, arising out of supply chain disruptions as well as product *and* factor market closures caused by government-regulated lockdowns. This has brought into sharp focus once again the importance of “force majeure” and “change of law” clauses that otherwise tend to get ignored in policy and legal discussions worldwide. Policy debates have now emerged in India on not just simpler issues such as partial waiver of individual/ firm-level tax liabilities *and* short-term time extension of contracts; but even around areas such as whether revenue shortfalls can be used by public agencies for avoiding their payment liabilities. Within this latter category, we have seen guidance from the MNRE issued in April this year advising revenue-impacted energy utility companies not to rely on force majeure clauses to avoid their payment liabilities to power producers: discussions that have now moved to complex – *almost* constitutional – debates in the GST Council on the mechanism and quantum for compensation to state governments in the backdrop of tax revenue shortfalls.

Drawing Distinctions between “Force Majeure” and “Change of Law”

While “force majeure” (FM) and “change of law” (COL) clauses may look similar, there are some fine legal distinctions between the two, of course largely dependent on what specific meaning is assigned to them in a specific contract. More generally, FM clauses address “Acts of God” such as natural disasters and pandemics; while COL clauses address “Acts of Men” (or more appropriately, “Acts of Governments created by Men”) such as lockdowns, import restrictions and tax changes. Their legal implications can also therefore be very distinct: a FM clause may only allow a supplier to seek unilateral terminal of his obligations or a time extension without liquidated damages *and* without price escalations; whereas a COL clause may even allow a supplier to seek higher prices for supplies and services depending on the nature and severity of regulatory changes subsequent to contract formation.

COVID-19 Policy Responses in India

In March this year, India’s Union Cabinet Secretary issued directions for adoption of a *whole-of-Government* approach for building comprehensive and robust responses to the coronavirus pandemic – one of the most ambitious and well-coordinated policy responses to COVID-19 procurement issues anywhere in the world. In fact, the MoF had already been receiving queries from a number of government entities on applicability of the FM clause for delayed deliveries in view of COVID-19 pandemic; and it

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had clarified in February itself that the pandemic could be considered a case of natural calamity and FM clauses could be invoked using para 9.7.7 procedures of the Manual of Procurement of Goods, 2017.

There is some debate whether restrictions on movement of persons or supplies or those on opening of manufacturing/ warehousing facilities more appropriately amount to “change of law” (COL) as these are not “Acts of God” *per se*, but the MoF guidance was perhaps constrained by the absence of a specific COL para on the 2017 Manual. In addition, while a FM clause generally allows a government contractor to either unilaterally terminate its contract or to seek extension of time without liquidated damages/ price escalations; para 9.7.7 specifically quoted in MoF orders limits either party to terminate a contract without any financial repercussions on either side. Given the more elaborate nature of a FM clause as commonly understood in contrast to para 9.7.7, it is not surprising that some ministries such as MNRE have allowed more expansive invocation of FM clause for granting time extension as well.

Subsequent to MoF’s February orders, it then issued another set of comprehensive and well-crafted guidelines, starting with a circular in May allowing automatic time extension for a short period without any penalty on a contractor in certain cases. Simultaneously, MoF also issued another important instruction allowing partial refund of performance security to a contractor under specific circumstances, in proportion to contract work completed relative to the total contract value – something that brings about a refreshing and impactful change, given that such a

dispensation was hitherto not permitted under GoI’s procurement rules for goods and services.

Conclusions

Once MoF starts reviewing practical implementation of its February/ May orders, it is quite possible that a “change of law” para for “Acts of Men-made Governments” – one that already forms part of large and complex contracts being awarded by Central and state governments/ PSUs in India – specifically designed to deal with regulatory changes and events will find its way into its procurement rules, in addition to the existing “force majeure” para for “Acts of God”. Another refinement that may perhaps become necessary, sooner than later, is that contractors typically have the option of meeting their performance guarantee requirements in a number of different ways, including piece-meal deductions from their running account bills. In view of this, some administrative departments may perhaps need to issue supplementary guidance in order that the clear high-level intent of providing relief to stressed projects through “proportionate refund” is fully reflected in terms of faster progression of COVID-stressed public projects. Last but not the least, relying on “change of law” as a fundamental legal argument complementing (or supplementing) current “force majeure” based discussions in the GST Council, may perhaps even fundamentally alter the scope and nature of how states’ GST compensation claims could get resolved in the Council in the near future.