

COVID-19 Contract Guide

Cancellations, force majeure, frustration and non-performance due to COVID-19: A general legal guide.

Please note this document contains general information only and is not a substitute for seeking legal advice on your specific business contracts and circumstances. Each contract and the best course of action for your business should be evaluated on a case-by-case basis, taking into account the potential financial, operational, legal and reputational risks and impacts on the business, while maintaining customer and industry goodwill.

This guide provides a general overview of key legal issues and guidance relevant to common operational and contract issues facing business as a result of recent COVID-19 lockdowns and government health orders. In the current COVID-19 context, each business will be affected differently, due to varying state government restrictions and health directives, as well as different customer and supplier contract terms and conditions and cancellation policies. As the liability and rights of parties arise primarily from these individual contractual arrangements and specific circumstances (and is subject to different state and federal COVID-19 legislation and restrictions), **we strongly recommend you seek legal advice in relation to your specific circumstances.**

Regulators such as the Australian Competition and Consumer Commission (**ACCC**) have publicly indicated their expectation that businesses must treat consumers fairly and are watching closely for any unconscionable conduct or breaches of applicable consumer protection laws. Accordingly, when considering the most appropriate response for your business to business contracts and customer requests, we recommend that you carefully balance your specific financial and legal obligations (including any applicable contract terms or cancellation policy) with long term potential relationship and reputational impacts in order to find fair, practical and ideally mutually agreed solutions for all parties concerned.

Contracts: Key legal concepts

In legal terms, there are a few key concepts that will determine how you must deal with contractual obligations in an environment where a party to the contract is prevented from performing the contract due to:

- a **'force majeure'** event (like the Coronavirus pandemic or government health orders); or
- a situation where a contract may be **'frustrated'**; or
- other circumstances in which your **cancellation policy** or relevant **contract** provisions may apply.

Critical first steps

It is critical that you work out:

- (a) What COVID-19 government restrictions and health orders apply to you and your business?**
There is a difference between choosing not to deliver goods/services and not being able to deliver.
- (b) What do your contracts say?** Make sure you know, or get advice on, which of the above three concepts (force majeure, frustration or cancellation policy/contract terms) apply in your circumstances, how they interact and that you understand the relevant terms of your contracts so that they can be relied on and/or complied with.

A COVID-19 related shut down of your business may not necessarily mean your contract is frustrated or that you don't have to perform your obligations. Take the time to check if you have contractual terms in place that address the issue such as a force majeure clause, suspension, delay or other cancellation or policy terms. Importantly, review contracts for potential liability, damages and costs claims associated with such delay, suspension or termination.

What if I don't have a contract?

Whether you have written terms and conditions or not, upon a business accepting an order or booking, you create a form of contract between yourself and the other party. Part of that informal contract may be an oral agreement, or set out in a purchase order. It is in the interests of both parties that you have a clear understanding of what those contract terms and conditions are (and generally, the best way to do so is to have written terms and conditions).

You should seek specific advice as to your obligations, as this can be unclear where there are no written terms and the two parties may have differing expectations.

1. What is a Force Majeure Event?

A Force Majeure Event is usually defined as an 'act of God' or some other extraordinary event that is outside the control of the parties. Firstly, you should check your contracts (or relevant terms and conditions) to confirm:

- (a)** if it contains a force majeure clause providing relief from non-performance or delayed performance; and
- (b)** whether or not the Coronavirus pandemic falls within the contract's definition of force majeure event in order to access the protections offered by the clause.

Typically, a person whose performance of a contract is hindered or prevented by a force majeure event is relieved from their obligations and liabilities to the extent they are unable to perform the contractual

obligations due to the occurrence of that force majeure event. Sometimes the clause will include a right to terminate the Contract following the continued occurrence of a force majeure event for a certain period.

Practical Tips

Contract interpretation: Read your contract carefully to see what circumstances are covered. You may need to seek legal advice to determine how broadly a force majeure clause can be interpreted to confirm whether the Coronavirus pandemic is covered.

Notice and timing: If you do have a force majeure clause in your customer terms and conditions or other type of contract (and COVID-19 is covered), it is important to also check for any technical notification obligations or relevant time periods which apply to giving notice, updates, and exercising your force majeure (and any termination) rights.

No force majeure clause: If you don't have a force majeure clause in your contract, it may be possible to rely on the common law doctrine of 'frustration', however this is quite a high bar (see below).

2. When is a Contract 'Frustrated'?

The common law principles of 'frustration' acts to relieve parties of liability where, due to the occurrence of an unforeseeable, supervening event beyond the control of the parties, there is a radical change in the circumstances in which a contract is to be performed. The simple alteration of circumstances in which a contract is to be performed is not enough. The event must have a substantial impact.

Importantly, the 'frustrating' event must have been *unforeseeable* at the time the contract was entered into. This becomes relevant where, for example, a booking or order is made after lockdown restrictions are made. The event also must not have been caused by the fault of either party to the contract. As with force majeure, if alternative arrangements can be made in order to perform the contract then the doctrine of frustration cannot be invoked. It will be difficult for a party to rely on the frustration principle merely because it has been let down by one of its suppliers or employees, change of mind, delays or if performance of the contract has simply become more expensive.

Certain legislation addresses some of these issues. For example, in NSW the *Frustrated Contracts Act 1978 (NSW) (Act)* addresses what happens in the case of frustration and the mechanisms controlling it, including in relation to payment and/or refund of money.

What is the effect of frustration on a contract?

If it can be established that a contract is 'frustrated', the entirety of the contract will be discharged (i.e. no longer binding and the parties released), other than obligations which survive termination or expiry. There is no right for a party to the contract to claim damages (note damages is a different concept to refunds). In other words, losses lie where they fall. No party can claim damages for non-performance because no party is at fault. However, you should check the applicable provisions under Act to confirm whether you have a right to be paid for services performed or conversely, an obligation to return amounts paid prior to the frustration of the contract (see also the ACL below in this regard).

Of course if the parties are happy with current arrangements and a contract can remain on foot (e.g. by complying with social distancing and other government COVID-19 legislation or by postponing booking/delivery dates) you can effectively avoid frustration of contract issues by agreement.

3. Cancellation Policies and Contract Terms

Where your contract does not have a force majeure clause (or it is not drafted broadly enough to cover the Coronavirus pandemic) and the circumstances do not quite constitute 'frustration', you should look to your cancellation policy, if you have one, or cancellation terms in your contracts. It is important to ensure your cancellation policy has been appropriately incorporated into the contract with your customer (e.g. in your contract terms, by notice on your website or a 'tick box' style acceptance).

Cancellation policies should be **clearly expressed and transparent**, and should set out:

- in what circumstances customers may cancel;
- any timing or notice requirements for cancellations;
- cancellation or administration fees (see unfair contracts section below);
- in what circumstances customers are entitled to a refund (e.g. cancellations at least seven days prior to the booking date, or such other specified time frames).

The terms of the cancellation policy must be **fair and reasonable**, and if online platforms are used, relevant terms and conditions of sale including the cancellations policy should be clearly identifiable online at the time of the order or booking.

Cancellation Fees

A business' ability to claim cancellation fees from a customer depends on the circumstances of the cancellation. If the business charges a cancellation fee or administrative charge, the fee should not be excessive otherwise it may be regarded as an unfair contract term or as a penalty which generally cannot be enforced.

Businesses should generally limit any cancellation fee to the reasonable costs associated with carrying out the cancellation (if any).

The ACCC has indicated that businesses proposing to charge a cancellation fee, or to retain an amount to cover expenses, should:

- (a) clearly communicate to consumers at the time the remedy is offered:
 - (i) that the cancellation fee will be charged;
 - (ii) the reasons or circumstances in which the fee is being charged; and
 - (iii) the amount of the fee to be charged;
- (b) expressly identify for consumers the legal source of their right to the fee or amount to be retained; and
- (c) on request, provide an itemised breakdown justifying the amount charged or retained.

The ACCC and ACL regulators expect that:

- only a single fee or deduction will be applied to a booking; and
- in most circumstances, any amount charged or retained will be a nominal sum relating to reasonable administrative expenses incurred.

We have seen a trend toward such cancellation fees being waived following pressure from the regulators during the pandemic and also to maintain loyal customer relationships and encourage return customers in the future once restrictions ease.

Credit notes

A 'credit note', rather than a refund, may be an appropriate remedy in certain circumstances. Businesses should advise consumers upfront about any terms that govern the use of a credit note.

The ACCC and ACL regulators have expressed an expectation that any credit notes provided should have:

- at a minimum, the same value as the amount paid for the booking;
- an expiry date that will allow the consumer a reasonable period in which to use the credit after the COVID-19 restrictions are lifted, or alternatively, no expiry date.

They also recommend businesses should be prepared to extend any expiry period to take into account the extension of any travel restrictions, to allow the consumer a reasonable period in which to use the credit after the COVID-19 restrictions are lifted, or to otherwise receive a refund. Alternatively, businesses may prefer to provide credit notes with expiry periods that do not start to run until after the COVID-19 restrictions are lifted.

Option of refund or credit note

Businesses may wish to offer consumers who are entitled to a refund the option of accepting a credit note instead. It is to be noted that in these circumstances, the choice between accepting a credit note or refund lies entirely with the consumer.

Note: Businesses should exercise great caution to ensure they do not, in suggesting the above options, mislead consumers regarding the circumstances in which they are required to accept a credit note rather than a refund.

Any terms and conditions that govern the use of any credit note offered should be notified to the consumer up front so that consumers can make an informed decision about which option they will choose.

Timing of refunds

Where a consumer is entitled to a refund, the refund must be paid within a reasonable time. However, the ACCC has acknowledged that in the current circumstances of the COVID-19 pandemic, it may take longer than usual for businesses to be able to process the volume of cancellation and refunds. Businesses should communicate regularly with consumers about the timing of any refunds.

Businesses should also endeavour to minimise their monetary losses following a cancellation. If the contract allows the business to reclaim losses from a customer, without taking reasonable steps to avoid them, it may be deemed unfair under the ACL.

Where a refund is due following a cancellation, a business should generally give those refunds in the same form as the customer's original payment.

ACCC and Australian Consumer Laws

Caution: Regulatory scrutiny

The Australian Competition & Consumer Commission (**ACCC**) has indicated that it is alert to any instances of unfair or unconscionable conduct on the part of businesses in dealing with consumers during the COVID-19 crisis. The ACCC has encouraged all businesses to 'treat consumers fairly' during this time.

Businesses should be mindful of obligations under the Australian Consumer Law (**ACL**), which in addition to statutory rights ('consumer guarantees') to refunds or replacement services in certain circumstances, include:

- to **not mislead** customers, including about what the customer is entitled to under the business' terms and conditions or in relation to consumer guarantees and other ACL rights such as rights to a refund;
- to **not act unconscionably** when dealing with customers;
- to not seek to rely on **unfair terms** in standard form contracts with customers.

Application to business to business (B2B) transactions - NEW CHANGES

Businesses should also be aware that in many circumstances, small businesses are also defined as consumers (and so consumer rights and the ACL will apply), especially in relation to dealing with large businesses and for the purpose of unfair contract laws.

On 1 July 2021, Australian Consumer Laws (which includes implied statutory consumer guarantees and rights to refund for products and services) changed, so that they now apply to not just the typically small-scale individual consumer transactions but will also apply to a greater number of business to business contracts and high value industrial and commercial goods.

The relevant ACL threshold has increased (from \$40,000) to capture, and make the ACL applicable to, transactions that cost up to \$100,000 (regardless of the type or purpose of the goods or services, with some exemptions). Under the new threshold, businesses that manufacture or supply goods or services to customers up to \$100,000 will need to understand and comply with legal obligations under the ACL as their business customers may be considered 'consumers' with associated protections.

Read more in our article [here](#) or contact us to get up to date on your Australian Consumer Law obligations under these recently expanded laws as at 1 July 2021.

Exceptions to ACL consumer guarantees

Consumers' rights are not limitless and the consumer guarantees under the ACL do not require you to provide a remedy unless one of the guarantees has not been met.

For example, you may not be required to provide a remedy if:

- a consumer simply changes their mind, decides they do not like the purchase or has no use for it;
- discovers they can buy the goods or services more cheaply elsewhere.

Accordingly, cancellations prior to the government's travel / gathering restrictions merely because the customer had concerns about COVID-19 may be treated as a 'change of mind', depending on the timing and circumstances.

Practical and Policy Considerations

The revised flexible policies many businesses have adopted to reflect the ongoing uncertainties and to align with best practice are strongly encouraged by regulators. Although financially challenging for small business, we expect this will be a continuing trend to maintain customer loyalty, especially as public policy indicates a preference for businesses and consumers alike to take steps to minimise the spread of coronavirus, even if that means permitting last minute cancellations where customers are unwell or affected by government restrictions.

Communication will be key, and it will be in the interests of businesses to find a balance between protecting their financial interests under their cancellation policies, compliance with ACL and 'frustration of contract' obligations to provide refunds in certain circumstances, and incentivising customers to take up a credit note and rebook on appropriately flexible terms. In doing so, businesses will need to be careful to not be misleading about options and rights to refunds vs credit notes. Businesses may also wish to consider adopting a flexible policy which allows for refunds to be granted in special or hardship cases (for example, people who are high risk due to underlying health conditions).

Contact

If you have any questions or are unsure of the best approach in your circumstances or need specific advice on your obligations on how to get out of a contract and minimise your losses, please reach out to our *Commercial Team of The Year 2020* for specific legal advice.

If you require legal advice for your specific circumstances, please contact Suzie Leask, Associate Director or Iain Rennie, Managing Director at Australian Business Lawyers & Advisors on suzie.leask@ablawyers.com.au, iain.ennie@ablawyers.com.au or 1300 565 846 for a confidential discussion and fee estimate. You can also access further legal guides and articles in the COVID-19 Resources Hub at www.ablawyers.com.au/COVID-19-Hub.



**Commercial Team of the Year
2020**