SQUIRE PATTON BOGGS

Beyond Force Majeure

When Does a Conflict Actually "Frustrate" a Contract, What Is My Strategy, and What Questions Should I Ask?"

The Financial Times released an article today headed "Qatar warns war will force Gulf to stop energy exports within days". In our previous bulletin, we examined the use of *force majeure* and material adverse change clauses following the US/Israeli strikes on Iran.

The development of these events – including Qatar's warning – prompt a pressing question for commercial parties – particularly those operating in the Middle East: when do geopolitical shocks move beyond *force majeure* and actually frustrate a contract under English law?

Frustration – The High Bar Under English Law

Frustration is a common law doctrine that automatically discharges a contract for both parties when:

- A supervening event occurs after formation
- Neither party is at fault
- Performance becomes impossible, illegal or fundamentally different from what the parties originally agreed

Key principles include:

- **Frustration is exceptional** – Hardship, delay, inconvenience or increased cost are insufficient. Courts have refused frustration where an alternative route was merely longer (e.g., the Suez closure – see *Tsakiroglou & Co Ltd v. Noblee Thorl GmbH* [1962] AC 93 (HL)) or where lengthy delays did not change the nature of the bargain. For example, if a charterparty permits a vessel to load cargo at a location outside the Persian Gulf, it becomes very difficult to claim that closure of the Strait of Hormuz would frustrate the agreement.
- **No clause may provide for the event** – If the contract already provides for how to deal with the supervening event (such as through demurrage or a *force majeure* clause), courts are far more likely to apply the agreed mechanism than allow the parties to walk away. Yet, even then, a charterparty may still be found to have been terminated for other reasons. For example, in *MSC Mediterranean Shipping Company S.A. v. Cottonex Anstalt* [2016] EWCA Civ 789, the Court of Appeal found that a party was not entitled to keep a charterparty "alive" for the purposes of claiming demurrage when the defaulting party was unable to perform its obligations, as the "commercial purpose" of the venture had become frustrated.
- **A frustrating event cannot be self-induced** – If the event arises from a deliberate action or choice of one of the parties, that party cannot rely on the doctrine of frustration. A party cannot invoke frustration where the event making further performance impossible is the result of their own breach or negligence.
- **Only three categories usually apply:**
  - Impossibility
  - Illegality
  - A radical shift in the nature of the obligation

The event must impact the core purpose of the contract; foreseeable or incremental risks do not typically meet the test.

- **The effect is automatic discharge** – Once frustration occurs, all future obligations fall away with no judicial discretion to amend the contract. This "all-or-nothing" consequence makes courts cautious. For example, if a vessel under a time charter was part-way through its service when a supervening event permanently prevented it from continuing, such as the vessel being destroyed or irretrievably seized, any remaining obligation to complete the charter period or continue trading would fall away automatically.

Conflict-driven Events – Do They Satisfy the Frustration Threshold?

Physical Destruction or Unavailability of the Subject Matter

Frustration may arise if war destroys or permanently removes the subject matter of the contract.

In the current Iranian conflict, disruption has largely involved airspace closures, shipping delays and market volatility, rather than the widescale destruction of essential facilities. Unless a party can show that critical infrastructure (e.g. a port, refinery or project site) has been eliminated, frustration may be hard to prove. Nonetheless, given the recent warning that Gulf states may begin declaring *force majeure* under their contracts, and that it may take "weeks to months" to return to normal cycles – frustration may well arise due to delay, rather than physical destruction.

Moreover, while financial loss would not in itself cause a charter to be frustrated, case law suggests an exception to this rule when a vessel is damaged during a voyage.

The exception applies where the cost of carrying out only those repairs necessary to let the ship finish the voyage, even if the repairs are temporary, would exceed the vessel's post-repair value, meaning that no reasonable owner would undertake them. In such circumstances, the situation is treated as equivalent to one where repair is physically impossible, and it is now regarded as a form of frustration (as in *Bunge SA v. Kyla Shipping Company Limited (The "Kyla")* [2012] EWHC 3522 (Comm)).

This exception may not apply if the charter requires the owners to maintain hull insurance at a specified level, and the repair costs fall within the insured amount. In that scenario, the owners may not be able to argue that they could not reasonably be expected to fund the repairs, because the insurance proceeds would cover them.

Illegality Arising From Sanctions or Government Measures

Performance may become illegal if new sanctions, export controls or emergency governmental restrictions prohibit contractual obligations. The courts recognise such supervening illegality as a typical category of frustration.

The current disruptions we are seeing as a result of the Iranian conflict, such as insurance withdrawals, higher freight costs or increased risk premiums, do not themselves amount to illegality.

However, given the rapidly evolving dynamics, future Iran-related sanctions could make certain contracts illegal to perform (for example, prohibiting supplies to specified counterparties). If that occurs, frustration may become viable.

Radically Different Performance Due to Conflict Disruption

The question is not whether the conflict has made performance difficult, unprofitable or riskier, but whether the event has transformed the nature of the obligation so much that performing would constitute something fundamentally different.

Courts look at the contractual matrix, and in volatile regions like the Middle East, disruptions such as shipping delays or price spikes could be viewed as risks commercial parties should anticipate. In the context of delay, such as for a charter, the key question is whether the interruption is, or is likely to become, significant when compared with the remaining charter period. This assessment is to be made at the moment the delaying event takes effect. If the delay initially appears minor but later develops into one of excessive length, the contract may still be treated as frustrated once the true extent of the delay becomes apparent.

English law has consistently held that economic or logistical difficulty does not frustrate a contract. Since the strikes last weekend, traffic through the Strait of Hormuz sharply declined as insurers withdrew coverage and rerouting options were limited, creating major operational and financial strain. However, courts may view rerouting – even if expensive – as an increased burden rather than a radical transformation of the contractual obligation. Therefore, a war or a widespread strike might frustrate a voyage charter, while the same events may have no impact on a time charter that allows for a broader trading range. Yet, there are circumstances in which rerouting may amount to frustration. For example, where the contractual cargo is perishable, and could not endure an extended voyage, the requirement to deviate may arguably amount to frustration.

Frustration-focused Strategies and Key Questions

Despite the commercial fallout from the US-Israel-Iran conflict, most disruptions are unlikely to meet the stringent English law threshold for frustration. Nonetheless, as the conflict evolves and potential sanctions or targeted destruction emerge, certain contracts may well edge into frustration territory.

In the meantime, businesses should consider the following questions:

- Is it reasonable for me to expect to rely on *force majeure* or frustration?
  - **Depends** – Investigate whether a supervening event truly changes the nature of the obligation. Assess both the structural and economic impacts.
  - Analyse the parties' original risk allocation under the contact and the foreseeability of the event by reference to the time of contract. Courts will look closely at expectations in volatile regions.
  - Exercise caution before alleging frustration, as a failed assertion risks repudiatory breach.

Businesses should also consider *force majeure* – see our previous bulletin on force majeure and material adverse change.

- Can I rely on any other remedies?
  - **Maybe** – Check your contract carefully – it may contain separate provisions that provide relief.
- If I have a *force majeure* clause, should I provide notification?
  - **Yes** – Your contract may require you to provide notice of a *force majeure* event from the time when you (a) should have been aware of the event; and (b) realised an event may impact performance.
  - Irrespective of the notice requirements, it is always safer to give notice in advance of events that could impact your performance. Prompt notification will allow discussion and work on alternative arrangements to limit the impact of any potential disruption.
  - Any such notice should be given in accordance with the formality requirements of your contract.

- Should I prepare contingency plans?
  - **Yes** – You should take reasonable steps to avoid, limit and circumvent the frustrating event and its impact on your performance. This will be easier if alternative avenues for continuing performance are considered ahead of time for the most likely scenarios.
- Should I keep a record?
  - **Yes** – Businesses should gather contemporaneous evidence from the outset that can demonstrate impossibility or illegality. This can cover (a) the event; (b) the effects of the event; (c) the steps taken in mitigating the effects of the event; and (d) the costs of doing so.
  - For frustration, documentation of the fundamental nature of the disruption is critical.
- Should I initiate a dispute when I am entitled to rely on a *force majeure* clause and frustration, but my counterparty disagrees?
  - **No** – Initiating a dispute from the start is likely a premature step, and may entail avoidable costs. Instead, two things can be done at an early stage.
  - First, gather the necessary factual evidence to protect your position and establish your case. This includes reviewing and documenting alternative avenues for performance.
  - Second, aim to initiate dialogue with your counterparty, without waving any of your rights. Seek to agree and coordinate remedial action. Always do this with your in-house or external legal counsel.
- Will I bear my own losses incurred due to the frustrating event?
  - **Yes** – Because frustration is a remedy of last resort, its only consequence is the automatic discharge of all future rights and obligations under the contract. It does not provide compensation. Each party is therefore responsible for its own losses incurred as a result of the frustrating event.
  - However, past rights, obligations and liabilities will not automatically be discharged, and rights of recovery for past performance exist.
  - You should also consider insurance – see below.
- Should I contact my insurers?
  - **Yes** – Parties should keep their insurers up to date and notify them of any potential claims being made.
  - Parties should also review insurance documentation to understand whether the frustrating event is covered, and whether they have any obligation to minimise or avert any losses to preserve their rights.