

## Saudi Supreme Court's Decision Regarding the Covid-19 Pandemic Impact on Contracts



Khalid AlArfaj  
[Khalid@ArfajLaw.com](mailto:Khalid@ArfajLaw.com)

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Alya AlEssa  
[Alya.AlEssa@ArfajLaw.com](mailto:Alya.AlEssa@ArfajLaw.com)

The World Health Organization declared the COVID-19 as a 'pandemic' on March 11, 2020 (the "Pandemic"). Saudi Arabia and many other countries around the world implemented a series of precautionary measures to limit the spread of the Pandemic. Since then, many contracts governed by Saudi law have been impacted by the Pandemic and the related governmental measures.

Contracts in Saudi Arabia are governed by the principles of Islamic Law (Sharia). Under these principles, parties to a contract must abide by their contractual terms unless these terms are excused for a legitimate reason under Sharia or found to be inconsistent to Sharia principles and public policy or enacted legislation. To clarify the relevant judicial principles to be applied to contracts affected by the Pandemic, the General Authority of the Saudi Arabian Supreme Court (the "Court") has issued its Decision Number (45/M) on 08/05/1442H (December 23, 2020). The decision stated that the Pandemic will fall under:

- the **exceptional circumstances** category if a contract cannot be performed without an unusual loss; and
- the **force majeure** category if it causes the performance of a contract to be impossible.

### Conditions for Application

The Court set the following conditions to apply what is stated in the decision on contracts affected by the Pandemic:

- 1) The contract was concluded prior to the Pandemic's precautionary measures, and its implementation continues after the occurrence of the measures.
- 2) The impact of the Pandemic on the contract is direct and unavoidable.
- 3) The impact of the Pandemic on the contract is independent of any other cause.
- 4) The party affected by the Pandemic has not waived nor settled its rights.
- 5) The impact of the Pandemic was not addressed by a specific law or under a decision of a competent authority.

The Court also stated that the impact of the Pandemic on the contract should be severe and unusual. When assessing the impact, the contract's activity and timeframe should be considered, and the assessment of the harm should not exceed the period in which the impact of the Pandemic appeared on the contract. One or more experts should do the assessment.

### Modification of Contractual Obligations

The decision stipulated that courts, upon the request of the aggrieved party, and after balancing between the parties and considering the surrounding circumstances, may amend a contract impacted by the Pandemic as follows:

1) Property and movable assets lease contracts:

- a. If it was impossible to use the leased property fully or partially due to the Pandemic, a court will reduce the rent to the extent that the normal intended use of the property was diminished.
- b. The lessor does not have the right to terminate the contract if the tenant was late in paying the rent for the period during which it was impossible to use the property fully or partially due to the Pandemic.

2) Construction and supply contracts:

- a. If the Pandemic leads to an increase in the cost of materials, labor wages or operations, etc., a court will increase the value of the contract for the obligor (contractor or supplier), to the extent of usual reasonable increase. The obligee (owner or customer) has the right to seek termination of the contract due to the price increase.
- b. If the materials' cost increase due to the Pandemic is temporary, a court will temporarily suspend the implementation of the contract.
- c. If the Pandemic causes a shortage of materials in the market, a court will reduce the quantity to the extent it deems sufficient to protect the obligor from the unusual harm.
- d. If the shortage of materials due to the Pandemic is temporary, a court will temporarily suspend the implementation, if the obligee is not seriously harmed by this suspension. If the obligee is harmed, the obligee may request termination of the contract.
- e. If shortage of materials due to the Pandemic is permanent, which make it impossible to implement all or some of the contractual obligations, a court, at the request of one of the contracting parties, will annul the clauses that are impossible to implement.
- f. If it is impossible to implement the obligation to perform the work under a construction contract due to the Pandemic, a court will suspend the implementation of that obligation for a temporary period. If the obligee is seriously harmed by this suspension, it may request termination of the contract.

### Restrictions on Hearing COVID-19-Impacted Contract Cases

The Court stipulated that a court considering cases of contracts affected by the Pandemic must adhere to the following:

- 1) Decline to enforce liquidated damages or other penalties or termination provisions included in the contract if the Pandemic was the reason for delaying the implementation of the obligation.
- 2) Cancel the effect of any condition included in the contract that exempts a party from liability in the event of exceptional circumstances or force majeure.
- 3) The burden of proof that the Pandemic has caused any breach of any obligation is on the party that breached the obligation.

### Conclusion

The Court's decision will clearly be relevant to cases involving contracts affected by the Pandemic. Parties to contracts affected by the Pandemic should be aware that the terms of their contracts may be modified by this decision. They should carefully consider the effect of this decision on their rights and obligations related to these contracts and plan to take the appropriate actions.