

## **Force Majeure**



Amidst the outbreak of the Covid-19 pandemic, one of the widely discussed topics is the applicability of *Force Majeure* clause, particularly concerning the commercial contracts. The term *Force Majeure* is a French term derived from the Latin expression, 'vis major', though, the French term is known to have a wider meaning than the Latin expression. While a contract between parties is in force, some situations may arise beyond the reasonable control of the parties.

These situations can be general, referring to events that are beyond the reasonable control of the parties such as flood, war, fire or similar events or combination of both which sometimes tend the performance of the contract, impossible. Such events are *Force Majeure* events. However, the meaning and its applicability depend on the contract, and the language used. Two sections that are relevant under the Indian Contract Act, 1872 ("Act") are as follows: Which Legal Principles used To Invoke *Force Majeure*?

1. In the event of an express or implied clause in a contract, agreements are governed under Section 32[1].
2. *Force Majeure* events occurring outside the purview of the agreements are dealt with under Section 56 (popularly referred to as Frustration of Contract).

The extracts of the sections are set out herein:

*"32. Enforcement of Contracts contingent on an event happening - Contingent contracts to do or not to do anything if an uncertain future event happens, cannot be enforced by law unless and until that event has happened. If the event becomes impossible, such contracts become void.*

*56. Agreement to do impossible act - An agreement to do an act impossible in itself is void.*

*Contract to do act afterwards becoming impossible or unlawful. A contract to do an act which, after the contract made, becomes impossible or, by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.*

*Compensation for loss through non-performance of act known to be impossible or unlawful. Where one person has promised to do something which he knew or, with reasonable diligence, might have known, and which the promisee did not know, to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-*

*performance of the promise."*

Per section 32, a party to a contract which contains a *Force Majeure* clause must prove the following:

*(a) that the event which caused non-performance must be included in the force majeure clause; (b) the non-performance was caused due to the said event; (c) the non-performance was beyond the party's control and (d) that there existed no alternative mode of performance.*

For invoking Section 56, there needs to be a valid contract, the performance of the contract has not been completed or must have been partially completed, the said performance becomes impossible by way of facts or law[2], the subsequent event is beyond the control of the party who intends to claim frustration and no reasonable steps could mitigate subsequent events.

#### Judicial Precedents

In India, the entire jurisprudence pertaining to Force Majeure has been summarised by Justice RF Nariman of the Supreme Court in the case of *Energy Watchdog vs. CERC (2017)*[3]. *While reiterating that doctrine of frustration cannot apply to the cases as the fundamental basis of the contract remains unaltered, the Court held that "an unexpected price rise will not absolve the generating companies from performing their part of the contract for the very good reason that when they submitted their bids, this was a risk they knowingly took.*

*We are of the view that the mere fact that the bid may be non-escalable does not mean that the respondents are precluded from raising the plea of frustration, if otherwise it is available in law and can be pleaded by them...When a contract contains a force majeure clause which on construction by the Court is held attracted to the facts of the case, Section 56 can have no application".*

The Court went on and detailed the jurisprudence on this subject matter. It is significant to reproduce the extracts[4] herein below:

"Prior to the decision in *Taylor vs. Caldwell*[5], the law in England was extremely rigid. A contract had to be performed, notwithstanding the fact that it had become impossible of performance, owing to some unforeseen event, after it was made, which was not the fault of either of the parties to the contract.

This rigidity of the common law in which the absolute sanctity of contract was upheld was loosened somewhat by the decision in *Taylor vs. Caldwell* in which it was held that if some unforeseen event occurs during the performance of a contract which makes it impossible of performance, in the sense that the fundamental basis of the contract goes, it need not be further performed, as insisting upon such performance would be unjust.

'Impossibility' under S.56 doesn't mean literal impossibility to perform (owing to strikes, commercial hardships, etc.) but refers to those cases where a supervening event beyond the contemplation and control of the parties (like the change of circumstances) destroys the very foundation upon which the contract rests, thereby rendering the contract 'impracticable' to perform, and substantially 'useless' in view of the object and purpose which the parties intended to achieve through the contract.

Satyabrata Ghose v. Mugneeram Bangur & Co[6]. The second paragraph of Section 56 has been adverted to, and it was stated that this is exhaustive of the law as it stands in India. What was held was that the word "impossible" has not been used in the Section in the sense of physical or

literal impossibility. The performance of an act may not be literally impossible but it may be impracticable and useless from the point of view of the object and purpose of the parties.

If an untoward event or change of circumstance totally upsets the very foundation upon which the parties entered their agreement, it can be said that the promisor finds it impossible to do the act which he had promised to do. It was further held that where the Court finds that the contract itself either impliedly or expressly contains a term, according to which performance would stand discharged under certain circumstances, the dissolution of the contract would take place under the terms of the contract itself and such cases would be dealt with under Section 32 of the Act. If, however, frustration is to take place de hors the contract, it will be governed by Section 56.

In M/s Alopi Parshad & Sons Ltd. v. Union of India[7], this Court, after setting out Section 56 of the Contract Act, held that the Act does not enable a party to a contract to ignore the express covenants thereof and to claim payment of consideration, for performance of the contract at rates different from the stipulated rates, on a vague plea of equity. Parties to an executable contract are often faced, in the course of carrying it out, with a turn of events which they did not at all anticipate, for example, a wholly abnormal rise or fall in prices which is an unexpected obstacle to execution. This does not in itself get rid of the bargain they have made. It is only when a consideration of the terms of the contract, in the light of the circumstances existing when it was made, showed that they never agreed to be bound in a fundamentally different situation which had unexpectedly emerged, that the contract ceases to bind. It was further held that the performance of a contract is never discharged merely because it may become onerous to one of the parties.

Similarly, in Naihati Jute Mills Ltd. v. Hyaliram Jagannath[8], this Court went into the English law on frustration in some detail, and then cited the celebrated judgment of Satyabrata Ghose v. Mugneeram Bangur & Co. Ultimately, this Court concluded that a contract is not frustrated merely because the circumstances in which it was made are altered. The Courts have no general power to absolve a party from the performance of its part of the contract merely because its performance has become onerous on account of an unforeseen turn of events.

It has also been held that applying the doctrine of frustration must always be within narrow limits. In an instructive English judgment namely, Tsakiroglou & Co. Ltd. v. Noblee Thorl GmbH[9], despite the closure of the Suez canal, and despite the fact that the customary route for shipping the goods was only through the Suez canal, it was held that the contract of sale of groundnuts in that case was not frustrated, even though it would have to be performed by an alternative mode of performance which was much more expensive, namely, that the ship would now have to go around the Cape of Good Hope, which is three times the distance from Hamburg to Port Sudan.

The freight for such journey was also double. Despite this, the House of Lords held that even though the contract had become more onerous to perform, it was not fundamentally altered. Where performance is otherwise possible, it is clear that a mere rise in freight price would not allow one of the parties to say that the contract was discharged by impossibility of performance.

This view of the law has been echoed in 'Chitty on Contracts', 31st edition.

In paragraph 14-151 a rise in cost or expense has been stated not to frustrate a contract. Similarly, in 'Treitel on Frustration and Force Majeure', 3rd edition, the learned author has opined, at paragraph 12-034, that the cases provide many illustrations of the principle that a force majeure clause will not normally be construed to apply where the contract provides for an alternative mode of performance.

It is clear that a more onerous method of performance by itself would not amount to a frustrating event. The same learned author also states that a mere rise in price rendering the contract more expensive to perform does not constitute frustration. (See paragraph 15-158)

Indeed, in England, in the celebrated *Sea Angel* case<sup>[10]</sup>, the modern approach to frustration is well put, and the same reads as under: In my judgment, the application of the doctrine of frustration requires a multi-factorial approach.

Among the factors which have to be considered are the terms of the contract itself, its matrix or context, the parties' knowledge, expectations, assumptions and contemplations, in particular as to risk, as at the time of the contract, at any rate so far as these can be ascribed mutually and objectively, and then the nature of the supervening event, and the parties' reasonable and objectively ascertainable calculations as to the possibilities of future performance in the new circumstances.

Since the subject matter of the doctrine of frustration is contract, and contracts are about the allocation of risk, and since the allocation and assumption of risk is not simply a matter of express or implied provision but may also depend on less easily defined matters such as "the contemplation of the parties", the application of the doctrine can often be a difficult one. In such circumstances, the test of "radically different" is important: it tells us that the doctrine is not to be lightly invoked; that mere incidence of expense or delay or onerousness is not sufficient; and that there has to be as it were a break in identity between the contract as provided for and contemplated and its performance in the new circumstances."

At this juncture, reference may be drawn to two significant decisions rendered in light of the pandemic situation. First is the decision of the Bombay High Court in *Merwanji Mancherji Cama v. Syed Sirdar Ali Khan*.<sup>[11]</sup> In the said case, the defendant was obliged to vacate the premises under notices from the plague authorities.

In the suit for arrears of rent, the defendant pleaded that he was not liable for rent for the period he was out of possession due to the notice of plague authorities as his enjoyment of the leased property was interfered with. Fulton, J. held that when under the provisions of the Epidemic Act 1897, it became unlawful for the tenant to occupy the premises in the manner contemplated by the lease, there was no breach of the lessor's contract for quiet enjoyment by the lessee.

*Li Ching Wing v Xuan Yi Xiong*<sup>[12]</sup> suggests prospects in arguing that agreements are frustrated by closures caused by Covid-19. In the said case, a residence was leased for a 2-year fixed term. Due to the SARS outbreak, an isolation order was issued due to which the tenant has to move out. Later the tenant issued a letter to terminate the lease and the landlord accepted his termination.

Relying upon UK House of Lords decision in *National Carriers v Panalpina*<sup>[13]</sup> which had approved the prior decision of *Cricklewood Property and Investment*

Trust v Leightons Investment Trusts[14], the Court has refused to accept the tenants contention that the contract was frustrated. In the former case, Lord Simon of Glaisdale had defined frustration as:

*"Frustration of a contract takes place when there supervenes an event (without default of either party and for which the contract makes no sufficient provision) which so significantly changes the nature (not merely the expense or onerousness) of the outstanding contractual rights and/or obligations from what the parties could reasonably have contemplated at the time of its execution that it would be unjust to hold them to the literal sense of its stipulations in the new circumstances; in such case the law declares both parties to be discharged from further performance. (at 700F)"* Importantly, Judge Lok said that *"an event which causes an interruption in the expected use of the premises by the lessee will not frustrate the lease, unless the interruption is expected to last for the unexpired term of the lease, or, at least, for a long period of that unexpired term. Therefore, emphasis was placed on the length (both qualitative and quantitative) of the supervening event vis a vis the remainder of the lease term"*.

Though, the jurisprudence pertaining to the lease agreements will have to be considered in light of the Transfer of Property Act, 1882, the aforementioned cases will be discussed and considered by the courts in India while arriving decisions involving commercial agreements.

Finally, the High Court of Bombay[15] recently dismissed a plea invoking the Force Majeure exemption, in a contract involving steel importers. While dismissing, it observed that the distribution of steel has been declared as an essential service, and there have been no significant restrictions on the movement of vehicles and manpower in the context of the steel industry, or operations of container freight stations and warehouses for steel.

It further noted that the lockdown would be for a limited period and the lockdown cannot come to the rescue of the petitioners so as to resile from its contractual obligations to the respondent of making payments.

#### Conclusion

It must be borne in mind that applicability of Force Majeure will be examined on a case to case basis. However, the law on this subject matter has been laid down in the Energy Watchdog vs. CERC case which mandates high threshold conditions. While interpreting, the courts are expected to narrowly construe the applicability of the Force Majeure events; ascertain if the fundamental basis of the contract dislodged and scrutinise alternative modes of performance if available while arriving at the decisions.

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[1] Satyabrata Ghose v. Mugneeram Bangur & Co

[2] Industrial Finance Corp. of India Ltd. v. Cannanore Spg. and Wvg. Mills Ltd., (2002) 5 SCC 54 at page 78

[3] Civil Appeal Nos.5399-5400 of 2016 <https://indiankanoon.org/doc/29719380/>

[4] Para 33 to 41 of the judgement

[5] (1861-73) All ER Rep 24

[6] 1954 SCR 310

[7] 1960 (2) SCR 793,

[8] 1968 (1) SCR 821,

[9] 1961 (2) All ER 179,

[10] 2013 (1) Lloyds Law Report 569,

[11] (1899) ILR 23 Bom 510 cited in Ardesir Bejonji Surti vs Syed Sirdar Ali Khan And Ors. on 13 October, 1908

[12] [2004] 1 HKC 353

[13] [1981] AC 675, [1981] 1 All ER 161, [1980] UKHL 8

[14] [1945] AC 221

[15] Standard Retail Pvt. Ltd. v. M/s G.S. Global Corp & Ors., Commercial Arbitration Petition (L) No. 404 of 2020.

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