Force Majeure – Frustrate or not?

- An analysis on how the legal term works

Force majeure clause won't apply to coronavirus death claims in life insurance policies

"The Economic Times"

Force Majeure takes centre stage during Covid-19

"The India Legal"

With lockdowns and restricted movements within and across countries, COVID-19, continues to unleash its impact on business and commerce in the country and worldwide. Today, with production units remaining vacant, considerable workforce connecting remotely, sales figures taking a plunge, the business goes through one of the toughest times since 2008. These disrupted operations demand the need to revisit contracts, their performance and obligations. This calls for the discussion, the term 'Force Majeure', its dimensions in the background of COVID-19.

Typically, mining contracts, contracts like supply agreements, contain a Force majeure clause to control the consequences in case of default in performance owing to certain circumstances or events. Because of the different interpretations of force majeure across legal systems, it is common for contracts to include specific definitions of force majeure, particularly at the international level.

An impact of Force majeure event may take the form of a notice from a customer that he does not require the goods or services, the corporate tenant refusing to pay rents, suppliers forcing delivery of goods or services though no/decrease in demand for the business's goods or services, delay and increased cost of delivery of goods or services to customers etc. So what is a Force Majeure clause?

Force Majeure is a French phrase meaning "a superior force". A Force Majeure clause is a contract provision that allows a party to suspend or terminate the performance of its obligations when certain circumstances beyond their control arise. Such circumstances may render performance inadvisable, commercially impracticable, illegal, or impossible. The provision may state that the contract is temporarily suspended, or that it is terminated if the event of force majeure continues for a prescribed period of time.

The list of events to be covered under Force Majeure is a matter of negotiation between the parties.

A typical Force Majeure clause may be read as follows:

"Neither party shall be held liable or responsible to the other party nor be deemed to have defaulted under or breached this Agreement for failure or delay in fulfilling or performing any obligation under this Agreement when such failure or delay is caused by or results from causes beyond the reasonable control of the affected party, including but not limited to **fire, floods, embargoes, war, acts of war (whether war is declared or not), insurrections, riots, civil commotions, strikes, lockouts or other labor disturbances, acts of God or acts, omissions or delays in acting by any governmental authority;** provided, however, that the party so affected shall use reasonable commercial efforts to avoid or remove such causes of nonperformance, and shall continue performance hereunder with reasonable dispatch whenever such causes are removed. Either party shall provide the other party with prompt written notice of any delay or failure to perform that occurs by reason of force majeure. The parties shall mutually seek a resolution of the delay or the failure to perform as noted above."

So, for example, a flood occurred that shut down a port, the seller planning to ship its goods through that port would not be liable for late delivery of the goods.

As such, the following elements should be addressed in a force majeure clause:

- Definition of force majeure events
- What happens when an event occurs
- Who can suspend performance; and
- What happens if the force majeure event continues for more than a specified period of time

In countries like China, France, the concept of Force Majeure is codified under law. Whereas in countries like India, UK, the concept of Force Majeure is not codified but introduced in the contracts by way of an agreement between parties.

Force majeure" is governed by the Indian Contract Act, 1872. In so far as it is relatable to an express or implied clause in a contract, it is governed by Chapter III dealing with the contingent contracts, and more particularly, Section 32 thereof.

Section 32 provides for **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.

Where an agreement does not provide for Force Majeure or one does not fall within the Force Majeure clause, the parties may have to look beyond the clause. For example:

"In the event either party is unable to perform its obligations under the terms of this Agreement because of **acts of God or damage reasonably beyond its control, or other causes reasonably beyond its control**, such party shall not be liable for damages to the other for any damages resulting from such failure to perform or otherwise from such causes"

The above clause does not provide a list of Force Majeure events instead uses a generic language throughout. In such a situation one may consider invoking Section 56. In so far as a force majeure event occurs de hors the contract, it is dealt with by a rule of positive law under Section 56 of the Contract.

Section 56 of Indian Contract Act 1872, otherwise termed as the **“Doctrine of Frustration”** reads as follows: Agreement to do impossible act - An agreement to do an act impossible in itself is void.

1. Contract to do act afterwards becoming impossible or unlawful. A contract to do an act which, after the contract is 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.

   i.e. At the time of entering into contract, the performance of an act was possible and lawful but afterwards such performance becomes impossible or unlawful due to some event which the promisor could not prevent. Then in such cases, the contract becomes void.

2. 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.”

   i.e. Where a person promised to do something which he knew or with reasonable diligence, might have known that it was impossible or unlawful to do but which the promisee did not know, then such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-performance of the promise.

Prior to the decision in Taylor vs. Caldwell, (1861-73) All ER Rep 24, 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.

The law in India has been laid down in the seminal decision of Satyabrata Ghose v. Mugneeram Bangur & Co., 1954 SCR 310. 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. It 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."

The word "impossible as mentioned in Section 56 doesn't mean literal impossibility to perform (like strikes, commercial hardships, etc.) but refers to those cases where a supervening event beyond the control of the parties (like the change of circumstances) destroys the very foundation upon which the contract rests. This would render the contract 'impracticable' to perform, and substantially 'useless' in view of object and purpose which the parties intended to achieve through the contract.

"In cases, therefore, where the court gathers as a matter of construction that the contract itself contained impliedly or expressly a term, according to which it would stand discharged on the happening of certain circumstances the dissolution on of the contract would take place under the terms of the contract itself and such cases would be outside the purview of section 56 altogether. Although in English law these cases are treated as cases of frustration, in India they would be dealt with under section 32 of the Indian Contract Act which deals with contingent contracts or similar other provisions contained in the Act."

The law of frustration in England developed, as is well known, under the guise of reading implied terms into contracts. The court implies a term or exception and treats that as part of the contract. However, Indian Law treats the two subjects of study completely different u/s 32 and 56. Therefore, where a Court in India while interpreting the contract, is convinced about the existence of an implied (S.9) or express term in the contract, that the contract shall be discharged upon happening of certain event, the matter will be dealt u/s 32 and will be completely outside the purview of S.56.

"In the large majority of cases however the doctrine of frustration is applied not on the ground that the parties themselves agreed to an implied term which operated to release them from the performance of the contract. The relief is given by the court on the ground of subsequent impossibility when it finds that the whole purpose or basis of a contract was frustrated by the intrusion or occurrence of an unexpected event or change of circumstances which was beyond what was contemplated by the parties at the time when they entered into the agreement. Here there is no question of finding out an implied term agreed to by the parties embodying a provision for discharge, because the parties did not think about the matter at all nor could possibly have any intention regarding it. When such an event or change of (a) circumstance occurs which is so fundamental as to be regarded by law as striking at the root of the contract as a whole, it is the court which can pronounce the contract to be frustrated and at an end. The court undoubtedly has to examine the contract and the circumstances under which it was made"

The relief is given by the courts on the ground of supervening impossibility or illegality when it finds that the whole purpose of the contract was frustrated by the intrusion or occurrence of an unexpected event which was beyond what was contemplated by the parties at the time of entering into the contract. When such an event occurs, which is so fundamental as to be regarded by law as striking at the root of the contract as a whole, then it is the court which pronounce the contract to be frustrated at the end.

Thus the Court concluded that a contract is not frustrated merely because the circumstances in which it was made are altered but the occurrence of an event which strikes at the root of the contract causing impossibility/impracticability of performance. 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.

Force Majeure – what next?

While deciding on a contract, it is important to comprehend the nature of the clause, the type of events covered, whether the terms could be extended to cover impact of COVID-19, if not whether relief can be taken under Doctrine of Frustration. Force Majeure event generally includes Acts of God, hence if the clause contains the term ‘Acts of God’ it could be extended to cover epidemic or pandemic. States like Haryana, Bihar, Karnataka have already declared COVID 19 as epidemic. The Government of India has issued a clarification declaring COVID 19 as a “notified disaster”. Whether the ability to perform obligations under a contract on account of COVID 19 be covered as Force Majeure event would be subject to argument.

The following points are to be noted in the review/drafting of commercial contracts.

1. Re-examine the key contracts as to whether these contain a Force majeure clause, if so, the nature of events included i.e. determine if it is a general clause or a specific clause.
2. Assess the parties’ rights and obligations, including with respect to termination and dispute resolution
3. Comply the procedure for notifying the other party
4. Understand the impact of COVID-19 on the performance obligations
5. Check for any alternative method of performance
6. In case of non-performance of the obligation, ensure proper evidences are in place to enforce the Force majeure event

In the case of Dhanrajamal Gobindram vs. Shamji Kalidas & Co. AIR 1961 SC 1285, the Supreme Court observed that force majeure as a term is not simply the French adaptation of vis major. The sum and substance of this term, in the opinion of the court, is of an extensive nature.

The onus of proving that the specifications of the contract would have been carried out was it not for the COVID-19 pandemic would lie on the party taking its plea (Classic Maritime v. Limburgan Makmur SDN BHD and Another, [2019] EWA Civ. 1102).

In the case of Satyabrata Ghose v. Mugneeram Bangur & Co., 1954 SCR 310, the court pointed out that the cases where the contract would stand suspended on the “happening of certain circumstances”, expressly or impliedly mentioned in the contract, would be independent of the ambit of section 56 of the act.

The court further, in the case of Energy Watchdog vs. CERC (2017) 14 SCC 80 while referring to the above judgment clarified that cases of such nature will be dealt under the arrangements of Section 32. The force majeure events that have been left out of the contract deliberately cannot be relied upon at a later stage. It was also held in this case that a force majeure clause will lose its pertinence if there exists an alternative method of performance of conditions, as laid down in the contract.

In the case of Tsakiroglou & Co. Ltd. v Noblee Thorl, GmbH, 1961 (2) All ER 179 it was noted that the fact that alternative route was longer than the original one, doesn't discharge the party from his obligations arising under the contract.

Going forward, while drafting contracts, due care has to be taken to ensure the Force Majeure clause is exhaustive and the language used does not call for a dispute concerning its scope. Counterparties may also attempt to invoke other contractual clauses like price adjustment clauses, material adverse change (MAC) clauses, limitation or exclusion clauses, to limit or exclude liability for non-performance. The ability to invoke such other grounds will depend on the wording of the relevant clause, and how the clause is construed by courts.

Conclusion

A force majeure clause cannot be implied under Indian law. It must be expressly provided for under the contract and protection afforded will depend on the language of the clause. In the event of a dispute as to the scope of the clause, the courts are likely to apply the usual principles of contractual interpretation.

In the absence of a force majeure clause, parties to a contract are left to the mercy of the narrow common contract law doctrines of "impracticability" and "frustration of purpose," which rarely result in excuse of performance.

What awaits would be, a time that demands clear understanding of language of the contract, a strong knowledge of principles of contractual interpretation, an ability to apprehend the scope of the clause, an informed decision making in the best interests and thereby conclude whether to frustrate or not.