



KOCHHAR & Co.
ADVOCATES & LEGAL CONSULTANTS



COVID 19 : IMPACT OF FORCE MAJEURE IN INDIAN COMMERCIAL CONTRACTS

Authors – Preetam D'Souza (preetam.dsouza@bgl.kochhar.com) Ranjit Mahishi (ranjit.mahishi@bgl.kochhar.com)

1. Force Majeure – meaning.

The term 'force majeure' translates literally from French as *superior force*. It is also generally defined in the Merriam Webster dictionary as 'an event or effect that cannot be reasonably anticipated or controlled'. The reference to "force majeure" is meant to describe events beyond the reasonable control of contracting parties and could include uncontrollable events (such as war, labour stoppages, or extreme weather) that are not the fault of any party and that make it difficult or impossible to carry out normal business.

A provision of force majeure in a contract is intended to absolve a party or waive its obligations absolutely or suspend it temporarily for reasons which cannot be construed to be a breach of contract by the defaulting party.

2. Section 56 and 32.

In India, the law on force majeure is embodied under sections 32 and 56 of the Indian Contract Act, 1872 ("**Contract Act**"). Section 32 of the Contract Act provides that '*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.*' Section 56 of the Contract Act enshrines the 'doctrine of impossibility', which provides that '*a contract to do an act which, after the contract is made, becomes impossible or unlawful or, by reason of some event which the promisor could not prevent, becomes void when the act becomes impossible or unlawful.*'

Under the aforesaid provisions, contracting parties can plead impossibility of performance and consequently frustration of a contract on account of a particular event, unforeseen previously and beyond the control of the parties.

3. Contract.

Commercial contracts almost always include a *force majeure* clause. The circumstances in which the provision may be invoked are generally limited to common events which may be construed to be 'Acts of God' and are usually not negotiated vigorously, except for specific situations such as 'strikes, lock outs, shortage of material, etc', which are the parties anticipate are likely to occur and have a direct bearing on the performance of the contract.

In certain instances, the provision may be triggered by an 'Act of God' and may not specifically enumerate the specific situations, such as the current pandemic. Most commercial contracts nevertheless include certain catch-all provisions having language such as – 'any other cause whatsoever beyond the control of the respective party'.

4. Section 56 of the Contract Act.

Doctrine of frustration - Impossibility

Prior to the Common Law 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 on the 'doctrine of frustration' has been laid down in India by the Supreme Court in the seminal decision of *Satyabrata Ghose v. Mugneeram Bangur & Co.* [1954 SCR 310]. The word "impossible" has not been used in the section [Section 56 of the Contract Act] in the sense of a 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 Contract Act. If, however, frustration is to take place *de hors* the contract, it will be governed by Section 56 of the Contract Act.

In *M/s Alopi Parshad & Sons Ltd. v. Union of India* [1960 (2) SCR 793], the Supreme Court, after setting out section 56 of the Contract Act, held that the statute 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* [1968 (1) SCR 821], the Supreme 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, the 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* [1961 (2) All ER 179], 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.

Non application if contract provides for force majeure which applies

As has been held in particular, in the *Satyabrata Ghose* case, 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 of the Contract Act can have no application.

The Supreme Court in its latest judgment in *Energy Watchdog vs. Central Electricity Regulatory Commission and Others* [(2017) 14 SCC 80] dated April 11, 2017 laid down the guidelines with respect to applicability of sections 32 and 56 of Contract Act to a contract. In the said judgment, the Supreme Court also made references to previous landmark judgments of the Supreme Court of India and also drew references from common law judgments and held that in so far as it is relatable to an express or implied clause in a contract, it is governed by Chapter III dealing with contingent contracts and more particularly, Section 32 thereof. 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 Act.

5. Covid 19 – Force Majeure event.

Contract –application.

Force majeure clauses in commercial contracts generally set forth limited circumstances under which a party may terminate or be excused of performance without liability due to the occurrence of an unforeseen event.

If the definition of *force majeure* specifically includes an ‘epidemic’, ‘pandemic’, ‘disease outbreak’, or even ‘public health crisis’, the current situation relating to COVID-19 may fit within that clause. The provision may also still include a reference to government action as a *force majeure* event, including ‘acts, orders, regulations, or laws of any government’, or ‘government order or regulation’.

Where such clauses are present, regulations and executive orders regulating, among other things, the size of gatherings or mandating the closure of certain establishments issued by the local government or the authorities, may qualify as *force majeure* events.

If the contract does not have specific language detailing the specific force majeure scenarios mentioned above, but has general catch all language referring to events outside the control

of the performing party, the courts generally interpret *force majeure* clauses narrowly and typically do not interpret a general catch-all provision to cover specific circumstances, which upon analysis may be construed to be beyond the agreed scope of the contract agreed between the parties. In such an event, if litigated, a party may have to prove that the clause, when drafted, was intended to cover a similar situation (a public health crisis as opposed to a natural disaster).

If the *force majeure* clause covers only 'Acts of God', the current pandemic may be outside its scope, as apart from triggering the applicability of Section 56 of the Contract Act and consequently impossibility of performance as above, the party claiming waiver of obligations under the provision will need to substantiate the intent of the parties to assume inclusion of the pandemic as an 'Act of God'. It is however important to note that assessing applicability and enforceability of such clauses by the relevant court will be dependent on a highly fact-specific analysis.

Finance and renewable energy ministry orders on force majeure.

The Ministry of Finance recently issued an office memorandum dated February 19, 2020 ("OM") which states that the force majeure clause can be invoked in Government contracts under the Manual for Procurement of Goods, 2017 if there is a "*disruption in supply chain due to spread of corona virus in China or any other country*". The OM further states that it should be considered as a case of "*natural calamity*".

Pursuant to the aforesaid memorandum, the Ministry of New & Renewable Energy issued an Office Memorandum dated March 20, 2020 which directed all renewable energy implementing agencies of the Ministry of New & Renewable Energy (MNRE) to treat delay on account of disruption of the supply chains due to spread of coronavirus in China or any other country, as force majeure.

In case of a litigation, where the contractual provisions are not specific or have general language, such as 'events beyond the control of the performing party', the above mentioned Government memorandums may help in supporting the interpretation that the situation amounts to a force majeure event. Further, it could be covered under 'natural calamity' (as stated in OM) if the clause does not use the words 'epidemic' or 'pandemic'.

6. Standard of performance.

Contract – termination, suspension of obligations

The consequence of a force majeure event under a contract may vary. Certain commercial contracts may require an 'impossible' standard for termination of the contract where a party may be allowed to terminate the contract only if the obligations are impossible to be performed. In certain other cases, the provisions may allow for the parties to suspend certain obligations during the pendency of the situation or allow for suspension in case of situations where although the performance may be possible, it may nevertheless be impractical or commercially non feasible.

7. Government orders.

Where the contracting party seeks to rely on orders of a regulatory authority or legislations issued in order to regulate the movement of persons or conduct of business on account of

the pandemic, it will be necessary for the contracting party to review the restrictions carefully to confirm that the same tantamount to the standards of performance as set out in the contract or under law (as applicable). For eg., where the relevant order provides for a prohibition of all commercial activities, but allows for certain business to procure passes for its employees to travel to their work places, it may be argued that the contract is not frustrated on account of the allowance; or that the non performing party is not restrained from fulfilling its obligations on account of events beyond its control.

Although the specific language in the contract may not set out an 'impossible' standard for invocation, the courts nevertheless are known to read into the said Government orders and restraints relied upon by the party take a narrow view of such circumstances to determine the parties claim for waiver of obligations under the contract.

8. Notice.

In addition to the rights accruing to the non performing party under the contract, specific attention will also need to be paid to the timing and manner in which the notice will need to be issued under the contract.

Most commercial contracts allow for issuance of a written notice by registered post, courier and/or email. In the event the parties have not agreed to multiple modes for issuance of the notice and the prevailing circumstance make it almost impossible for the notice to be issued by modes agreed to in the contract (such as post or by courier), the non performing party will need to consider a mode, whereupon, a notice issued and receipt thereof may be legally and validly substantiated in case of enforcement.

The non performing party will also need to consider the timing for the issuance of the notice in line with the requirements of the contract. Most commercial contracts provide for the period of suspension or right to terminate to be triggered upon issuance/receipt of the notice. Even where the contract does not specifically provide for such a trigger, it is advisable for the party seeking waiver or suspension of obligations to issue the notice at the earliest upon becoming aware of the event or upon realization of its inability to perform its obligation under the contract.

Conclusion – The concept of 'one size fits all' would be anathema in the invocation of the force majeure provision under Indian law or under the relevant contract. The local practices, usage, orders by the statutory bodies, the specific language of the contract, facts in relation to the pandemic affecting the parties, etc have a bearing on the analysis of applicability and enforceability of the provisions of the contract.
