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FAQ on Force Majeure and Frustration of Contracts

What is the meaning of the term "Force Majeure"?

Oxford dictionary defines force majeure as an unexpected circumstance, such as war, that can be used as an excuse when they prevent somebody from doing something that is written in a contract.

Parties sometimes contractually deal with future risk through force majeure clauses. These clauses provide for certain pre-agreed outcomes (e.g. excusing performance, delay or other measures) in certain pre-agreed situations.

Is outbreak of COVID-19 a force majeure situation?

Generally, force majeure clause in a contract will identify force majeure situations. Certain force majeure clauses may cover epidemics and pandemics. Clearly, asserting coverage of Covid-19 will be more straightforward if the clause includes this reference and because the World Health Organization has labelled Covid-19 as a pandemic. If there is no such specific reference, then alternative coverage will need to be considered as summarized below

- References to "acts of God" have been interpreted in the past under Indian case law to cover events other than pandemics. Therefore, a party seeking to assert that Covid-19 coverage is as an "act of God" will need to consider how this is consistent with the principles that previous cases have set out. The position may well be similar in relation to the interpretation of "natural disasters".

- The use of the term "disaster" in itself (rather than "natural disaster") may create some scope for usage because of the broader statutory definition of this term in the Disaster Management Act 2005. However, this legislation relates to government policy on dealing with disasters, so the context is different to a contractually negotiated bargain. This definition remains to be tested in the context of illnesses and the interpretation of this term under contract law may potentially be narrower in practice.

- Some force majeure clauses include a catch all phrase or residual provisions, on other potential uncontrollable events. However, these are likely to be interpreted by a court, by reference to the earlier list of events in the clause itself (the so called "ejusdem generis" principle), and if so, such residual clauses may be of limited use.

- Alternatively, if government shutdowns are listed as force majeure events, then these could open up another avenue to assert force majeure.

If the force majeure clause in the contract list epidemics, pandemics and government orders as force majeure events, can one invoke the force majeure clause?

Even if an event is covered in the list of force majeure events, parties will need to consider how the force majeure clause is drafted. In particular, the aspects that will need consideration are:

- Is the occurrence of the force majeure event referred to, preventing performance or delaying performance or affecting performance in some way? And,
- What is the outcome that is contractually defined after invoking the same, that is, does this permit a delay or suspension in performance, or does it act as a carve-out to liability or does it confer a termination right?

Ultimately, the ability of a party to apply Covid-19 as a way out will depend on the drafting of the relevant provisions.

Are there any notification requirements prior to invoking a force majeure clause?

The force majeure clause in your contract may also require you to notify your counterparty within a reasonable time of the impediment arising and affecting your performance of the contract. In the present case, the triggering event need not necessarily be the initial outbreak of COVID-19 in December 2019 and may constitute a particular stage in the advancement of COVID-19 or, a particular governmental decision in this regard. Please make sure to note when the triggering event occurred, and ensure compliance with the procedure in your contract, while maintaining correspondence with the counter party and highlighting the nature of disruption.

Does the party invoking force majeure have a duty to mitigate?

Force majeure clauses often require mitigation action on the part of the party seeking to assert it. Further, even if not explicit, and if a "catch all" phrase in the definition of the force majeure clause is drafted, by reference to other circumstances beyond the parties' "control", this limb may also imply a duty to mitigate the outcome on the party seeking to assert the force majeure provision.

Is there any other remedy available if the contract does not contain a force majeure clause?

If your contract does not contain an express provision on force-majeure, one can still examine if the necessary ingredients of Section 56 of the Indian Contract Act, 1872 are otherwise made out, and whether the doctrine of *frustration* or *impossibility* to perform are made out in this regard. This is a statutory provision available for all Indian law governed contracts. Frustration of contract being a Common Law doctrine, it will also be available in common law governed countries which may have statutory provisions similar to Section 56 embedded in their domestic laws.

The force majeure clause in the contract does not list epidemics, pandemics and government orders as force majeure events. Can we take the benefit of Section 56 of the Contract Act, 1872?

The contractual concepts of force majeure and frustration in India operate in mutually exclusive spheres. When a contract contains a force majeure clause which on construction by Court is held attracted to facts of the case, Section 56 of the Contract Act, 1972 becomes inapplicable.

What are the consequences if our claim of force majeure or impossibility of performance is subsequently held to be wrong?

If unsuccessful, the party claiming force majeure or frustration of contract would be considered to be in breach of the contract. The affected party may sue the breaching party for damages, specific performance or injunctive reliefs.

Are there any other relevant considerations which one should keep in mind while invoking a force majeure clause?

Force majeure is a question of fact and the burden of proof in force majeure claims lies with the person claiming relief. As such, it is necessary that due diligence is conducted before putting up the claim and it would be ideal to identify the disruptions and the indulgence being sought from the counter party.

Can we invoke force majeure or Section 56 of the Contract Act, 1872 in lease deeds?

With respect to leases, the provisions of the Contract Act do not apply, as the special law governing leases is the Transfer of Property Act, 1882 (TOP Act). Therefore, the protection available under Section 56 of the Contract Act relating to frustration of a contract would not apply in case of a lease.

Section 108 of the TOP Act only covers a situation when the property is destroyed or is rendered substantially and permanently unfit for the purposes for which it was let on account of fire, tempest or floor, or violent of any army or of a mob or other irresistible force. In such an event, the lease is terminable at the option of the lessee. The parties however are at liberty to mutually agree in their respective lease deeds the events or conditions which would be regarded as a force majeure event and the consequences thereof.

Therefore, if a lease deed envisages a force majeure event, then the parties would be confined to the scope of the definition of force majeure as provided in their lease deeds. It may not be open to parties to import additional events or seek protection which Section 108 of the TOP Act provides.

Hence, it is important to review each and every lease deed to ascertain (i) whether there is a force majeure clause; and the (ii) consequences on occurrence of a force majeure event, whether such force majeure clause envisages a termination or suspension of rights and obligations.

In the event a lease deed is completely silent on force majeure or consequences of the lessee being unable to use the premises for the purpose of which it is let out, then the Parties would have to examine if they fall within the four corners of Section 108 of the TOP Act.

If our contract is not governed by Indian law? Can we still invoke the force majeure clause or claim frustration of contract under Section 56 of the Contract Act, 1872?

If the contract is not governed by Indian law, it is advisable to seek expert opinion of a lawyer who is entitled to practice the law of the country, which governs the contract. For example, if the contract is governed by the laws of France, you should seek opinion of a lawyer practicing French law in relation to scope and applicability of force majeure clause to your contract.

The Ministry of Finance in its memorandum dated 19 February 2020 has clarified that *"disruption of the supply chains due to spread of corona virus in China or any other country will be covered in the Force Majeure Clause (FMC)"*. Is this clarification applicable to all contracts?

The memorandum issued by the Ministry of Finance applies only to procurement of goods, works or services by Ministry or Department of the Central Government or subordinate offices of the government. It does not apply to all contracts, but the memorandum would definitely carry persuasive value for contracts not covered by the memorandum dated 19 February 2020.

Can the principal employer claim 'force majeure' regarding engagement of contract workers through a manpower service provider?

Principal employers should review the manpower services agreement executed with vendors / contractors. If there is no force majeure clause covering situations of epidemic, the provisions of the Indian Contract Act 1872 will apply. As regards COVID-19, the answer to the question of claiming force majeure is not a definitive one – several factors including the local situation, the purpose of engagement of contract workers, the possible means of fulfilment of the terms of contract etc. will have to be assessed.

Can an employer declare the period of lockdown as 'leave without pay'?

As regards the category of workmen, leave without pay would be difficult to implement in view of the provisions of Industrial Disputes Act, 1947. As for managerial employees, management must strategize a plan for payment of their salaries keeping in view the state advisories that have been released to urge employers to not deduct employees' salaries during the initial closure period.

Can a company defer / cancel the employment of new joinees (who have not yet joined the services), in view of the outbreak and the local restrictions on operations?

Companies should review the terms of the appointment letters issued to new joinees. In general, if the appointment letter stipulates a specific date on which the employee is required to report to work, the same should be considered as the effective date of commencement of employment relationship, unless there is any other stipulation indicating the contrary. The company may, in such case, either delay the joining or revoke the offer of employment prior to the specified date of joining. Ultimately, it must be determined on a case-to-case basis as to when the employment relationship would really commence and whether the company has any flexibility to either delay the joining or revoke the offer at any time prior to such commencement.

The contract does not contain force majeure clause. Because of the pandemic, there would be substantial delays in the performance of the contract. Would substantial delays frustrate the contract?

If there is definite time limit agreed to by the parties within which a particular task is to be finished, in such cases delay for an indefinite period would make the performance of the contract impossible within the specified time and this would seriously affect the object and purpose of the venture. But when there is no time limit whatsoever in the contract, nor even an understanding between the parties on that point, then it would be difficult to bring the situation within the ambit of frustration.

Whether Section 32 or Section 56 applies to a contract that has become void because the event has become impossible?

Where the contract itself contains impliedly or expressly a term according to which it would stand discharged on the happening of certain circumstances, the question of dissolution of the contract according to its terms falls to be determined under section 32 of the Contract Act. The doctrine of discharge by frustration is not available where the contract makes full and complete provision, so intended, for a given contingency.

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Khaitan & Co have also established an internal working group of lawyers to advise clients on COVID-19 issues, and also aid the firm in assessing our preparedness to deal with contingencies and eventualities to ensure business continuity. For any queries please contact any of the authors.