India: Frustration Of Contract – When Does It Arise

by Kunal Tandon

In the wake of the current corona virus outbreak, most businesses are looking out to re-align themselves with the economic disparity that is likely to arise. In fact, even the Union of India through Ministry of Finance (Department of Expenditure Procurement Policy Division) has recently issued a clarification that corona virus will be considered as a case of natural calamity and as such covered under the *force majeure* clause available to be invoked wherever necessary and applicable.

What is *'force majeure' or 'vis major'?* It means 'superior force' or 'chance occurrence/unavoidable accident'. As the term and its meaning suggests, it is an event that the contracting parties could not have contemplated at the time of acceptance of contra cts. In India, primarily Section 56 of the Indian Contract Act deals with this situation. Though some say that Section 32 is also a facet of frustration, as any contingency becoming impossible to perform results in dissolution of the contract. However, this is outside the purview of strict frustration or *force majeure* condition in India, while an event of this nature under English law would lead to invocation of a *force majeure* clause.

This article deals with the distinction between the English and Indian law a little later, however, we straighta way come to 2nd part of Section 56, which reads 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.'*

The doctrine of frustration with its limited applicability was developed in *Taylor Vs. Caldwell* (1863) 3 B&S 826 in the year 1863 for the first time, wherein Justice Blackburn reasoned that the rule of absolute liability only applied to positive, definite contracts, not to those in which there was an express or implied condition underlying the contract.

As far as Indian law is concerned, Section 56 of the Indian Contract Act, 1872 is absolutely clear that an act, after the con tract is made, becomes impossible to perform or by reason of some event which a promisor/a party could not prevent becomes void and is not capable of performance. In this regard, the Supreme Court of India right from the Judgment in ***Satyabrata Ghose v. Mugneeram Bangur and Co. &Anr.*** reported in ***AIR 1954 SC 44, para 9*** to ***M/s. Dhanrajamal Gobindram v. M/s. Shamji Kalidasand Co.*** reported in ***AIR 1961 SC 1285*** and ***Smt. Sushila Devi &Anr. v. Hari Singh &Ors.*** reported in ***AIR 1971 SC 1756*** interpreted Section 56 to mean that an act must result in an impossibility of performance, or 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 which the parties had in view; and if an untoward event or change of circumstances totally upsets the very foundation upon which the parties rested their bargain, it can very well be said that the party finds it impossible to do the act which he promised to do. Further, the Supreme Court in *Sushila Devi* (supra) has held that since the law of frustration in India is different than under English law, recourse to English law may not be available to us. The interpretational process has developed various theories of frustration (i) implied term theory *i.e.* it is implied that the subject of the contract must survive for it to be performed; (ii) basis or foundation of the contract i.e. destruction / disappearance of the basis of the contract; (iii) just and reasonable solution i.e. if the termination is believed to be just and fair; (iv) radical change in obligation i.e. significant change in the nature of the contract.

From the above, it is clear that a *force majeure* event must lead to impossibility and any hardship, inconvenience or material loss (except if the termination can be shown to be just and fair) cannot be considered as a *force majeure* event. Hence, a change in policy by no means can be considered as a *force majeure* or an impossible event.

This brings us to the yet another facet of frustration, though not absolutely. Section 32 of the Indian Contracts Act charters what is known as internal frustration. First part of Section 32 of the Indian Contract Act suspends the performance of a contract until the uncertain future event (i.e. parties at the time of entering into the contract were aware of this uncertainty) happens, if that

future event is contained in the contract itself, thereby making a contract a contingent contract. If this future event becomes impossible to perform, the contract itself becomes void i.e. not capable of being performed.

Difference between English law and Indian Law

The Supreme Court in ***Satyabrata Ghose v. Mugneeram Bangur andCo. & Anr.*** reported in ***AIR 1954 SC 44*** *analyzed the situation under the English law and Indian Law and put it succinctly as under*:

16. In the latest decision of the House of Lords referred to above, the Lord Chancellor puts the whole doctrine upon the principle of construction. But the question of construction may manifest itself in two totally different ways. In one class of cases the question may simply be, as to what the parties themselves had actually intended; and whether or not there was a condition in the contract itself, express or implied, which operated, according to the agreement of the parties themselves, to release them from their obligations; this would be a question of construction pure and simple and the ordinary rules of construction would have to be applied to find out what the real intention of the parties was. According to the Indian Contract Act, a promise may be express or implied (Vide Section 9) . *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 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*. 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 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 belief, knowledge and intention of the parties are evidence, but evidence only on which the court has to form its own conclusion whether the changed circumstances destroyed altogether the basis of the adventure and its underlying object (Vide *Morgan* v. *Manser*, 1947 AER Vol. II, p. 666) . This may be called a rule of construction by English Judges but it is certainly not a principle of giving effect to the intention of the parties which underlies all rules of construction. This is really a rule of positive law and as such comes within the purview of Section 56 of the Indian Contract Act.

Hence, concluding this Article, it would be relevant for me to note that the law of frustration or rather *force majeure* is applicable in following circumstances:

1. If the act becomes impossible to perform- this may include impracticability, physical and commercial impossibility including impossibility in view of the object and purpose of the contract in mind at the time of execution. It, however, will not include hardships, material loss or inconvenience. For e.g. a contract is executed for supply of rice, and at the time of the contract, rice from Country X is cheap but later country X stops supplying rice making availability of rice more expensive. The promisor cannot seek shelter of Section 56.
2. The event which the promisor could not prevent- like an epidemic or pandemic, there should not be any negligence or malfeasance of the promisor in creating that event.
3. The parties ought not to have contemplated such supervening event at the time of execution of the contract.
4. The doctrine of frustration results in killing the contract, thereby discharging the contract and hence, it should not be lightly invoked.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.