

Coronavirus Pandemic (COVID-19): Invoking Force Majeure and Doctrine of Frustration: An Analysis From an Indian Law Perspective

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INTRODUCTION

The on-going global Coronavirus disease (“COVID-19”) pandemic, has affected a countless number of people around the world, businesses, and the global economies alike and is certainly nothing short of a ticking time bomb. On March 11, 2020, the World Health Organization declared COVID-19 a pandemic after noting that COVID-19 has increased 13-fold in countries other than China. A few state governments in India have also termed COVID-19 as an epidemic.² In testing times like these, India, currently amidst an unprecedented nationwide lock-down, which has subsequently been extended until May 3, 2020 and has resulted in a temporary or partial shutdown of most business(es)-in India—whether they be small, medium or big business houses, with the exception of only a list of services notified by the relevant governmental authorities which have been deemed to be and are categorized as ‘essential services’³ and allowing functioning of select additional activities (*such as allowing manufacturing activities in certain sectors to take place*), which have also only been permitted to start from April 20, 2020⁴.

With this, the Indian business community has certainly had to witness some of its biggest challenges in the recent past.⁵ This article examines some of them in more detail below.

DEMAND-SIDE IMPACT

Tourism, Hospitality and Aviation are among the worst affected sectors that are facing the maximum brunt of the present crisis.⁶ Closing of cinema theaters and declining foot traffic in shopping complexes have affected the retail sector by impacting consumption of both essential and discretionary items. Consumption is also getting impacted due to job losses and a decline in income levels of people, particularly daily wage earners. This is due to slowing activity in several sectors including retail, construction, and entertainment. With growing fear and anxiety now increasing, the overall confidence level of consumers has dropped significantly, leading to the

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² Honorable Supreme Court of India in: ‘RE: CONTAGION OF COVID 19 VIRUS IN PRISONS’ – order dated April 26, 2020; Writ Petition (Civil) No.1/2020.

³ In line with the order of the Central Government of India, dated March 24, 2020 (“**Order**”) r/w the addendum to the Order dated March 25, 2020, ‘essential services’ has allowed that certain services deemed important and critical for economy, which includes items and services falling under the ambit of the services, including but not limited to the following list of services: (i) healthcare; (ii) pharmaceutical; (iii) FMCG; (iv) agriculture and food processing.

⁴ Refer to order No. 40-3/2020-DM-I-(A) dated April 15, 2020, issued by the Ministry of Home Affairs, Government Of India.

⁵ Refer to study paper issued by Federation of Indian Chambers of Commerce and Industry (“FICCI”), entitled “Impact of Covid-19 on Indian Industry” dated March 23, 2020 and the subsequent addendums, available at: <http://ficci.in/spdocument/23221/Industry-Feedback-MHA-Circular-15-April.pdf>.

⁶ Refer to article, available at: <http://ficci.in/ficci-in-news-page.asp?nid=21078>, last visited on April 06,2020.

postponement of their purchasing decisions. Travel restrictions have severely impacted the transport sector.⁷ Such large-scale issues have definitely led to a demand impact of various industries.

SUPPLY CHAIN DISRUPTION

Many projects depend on a just-in-time supply chain. Delay in contractual obligations due to logistical challenges such as the failed distribution or delay in the distribution of goods and components (particularly from China) cause enormous problems for the companies that rely on these materials. Many Indian companies rely heavily on the import of critical components from China. Delay in procuring these essential components will have an impact on the timelines and delivery of Indian products or projects.

FINANCIAL DIFFICULTIES ARISING -OR LIKELY TO ARISE BECAUSE OF SUPPLY CHAIN DISRUPTION

Due to the COVID-related lockdown, financial difficulties and obligations for companies are likely to emerge and may also lead to delays in the payments cycle. This in turn will undoubtedly lead to financial difficulties throughout Indian industries, especially, in the foreseeable future. A classic example of this is the defaults by the electricity distribution companies (“DISCOM”), in releasing payments to private companies.⁸

LIQUIDITY CRISIS: DELAY IN PAYMENTS OR PARTIAL PAYMENTS BY RELEVANT GOVERNMENTAL AUTHORITIES AND CUSTOMERS TO POWER-PRODUCING COMPANIES

Even though COVID-19 has hit India relatively later than other nations, its effects are already being felt by private companies, especially those in the power-producing sector. This is because a few of the relevant governmental authorities, and customers alike, have delayed clearing current and past-due accounts, leaving a collective debt often running into several hundred crores.⁹

Further, owing to many economic factors, a few of which have been discussed above, there is serious doubt about the performance obligations of the parties. This article seeks to examine whether parties can seek relief and construe COVID-19 to be a *force majeure* event and invoke the legal principle of the ‘Doctrine of Frustration.’

COVID-19 AND INVOKING THE *FORCE MAJEURE* CLAUSE UNDER INDIAN LAW

The Cambridge Dictionary has defined the term of *force majeure*, as follows: “an unexpected event such as a war, crime, or an earthquake which prevents someone from doing something that is written in a legal agreement.”¹⁰ The concept of ‘force majeure,’ *per se*, however, is not codified under the applicable provisions of the Indian law. The closest interpretation of the concept can be traced to Section 32, and to an extent under Section 56 of the Indian Contract Act, 1872 (“Act”). Section 32 of the Act, details how ‘contingent contracts,’¹¹ cannot be enforced under the law unless and until there is the occurrence of a particular event, and upon the occurrence of such an event, should the performance of the contract become unenforceable then, such a contract would become void. Additionally, Section 56 of the Act, discusses how an agreement to do an impossible act in itself is void. The ‘Doctrine of Frustration’ under Indian law finds its authority from the provisions of Section 56 of the Act.

⁷ Supra.

⁸ <https://www.livemint.com/news/india/centre-cracks-the-whip-on-discoms-to-discourage-delayed-paymentsto-utilities1561733209305.html>

⁹ A crore denotes ten million (10,000,000 or 10⁷ in scientific notation) and is equal to **100 lakh** in the Indian numbering system. In this case, it refers to the official Indian currency, rupees.

¹⁰ Refer to definition provided at: <https://dictionary.cambridge.org/dictionary/english/force-majeure>

¹¹ ‘Contingent Contracts’ are contracts which depend on event of ‘Contingency.’ Refer to definition of ‘Contingency’ provided at: <https://dictionary.thelaw.com/contingency>, wherein ‘contingency’ has been defined as a contract provision that states that something in a provision requires something to happen or not to happen.

The courts in India have usually given a relatively wide interpretation of the term *force majeure*. As seen in the case of *Dhanrajamal Gobindram vs. Shamji Kalidas and Co.*,¹² the Honorable Supreme Court of India had observed:

“The expression “force majeure” is not a mere French version of the Latin expression “vis major”. It is undoubtedly a term of wider import. Difficulties have arisen in the past as to what could legitimately be included in “force majeure”. Judges have agreed that strikes, breakdown of machinery, which, though normally not included in “vis major” are included in “force majeure”. An analysis of rulings on the subject into which it is not necessary in this case to go, shows that where reference is made to “force majeure”, the intention is to save the performing party from the consequences of anything over which he has no control. This is the widest meaning that can be given to “force majeure”.”

A force majeure clause essentially relieves one party or all the parties from liability to perform contract obligations when performance is prevented by an event or circumstances beyond the parties’ control.¹³ Should the force majeure clause be invoked, the parties are not liable for the breach of contract caused due to such superior forces against which their skill and care cannot possibly provide for.¹⁴

In light of the above, the critical question is whether COVID-19 would constitute a force majeure event. For this, each contract would need to be examined and the wording in each contract would need to be examined carefully, especially the force majeure clause contained in the particular contract. Also, each contract would need to be examined and reviewed on a case-to-case basis. Further, the mechanism stipulated in the particular contract (or any other ancillary documentation signed in furtherance to the contract), would need to be followed. If there is no specific force majeure clause drawn in the contract, then the terms of the contract would need to be examined and further read with provisions of Section 56 of the Act.¹⁵

A party claiming relief under provisions of Section 56 of the Act, would need to establish whether the current situation or a particular event has become such that post entering into the contract it has become impossible or unlawful to perform. If so, the contract will be rendered void automatically.¹⁶ In such an event, the parties to the contract would not be held liable for their performance obligations, starting from the time the ‘Doctrine Of Frustration’ is invoked. The onus in both cases would lie on the party seeking relief under the force majeure clause or wishes to invoke the Doctrine of Frustration. That party would be obligated to prove that the situation has become such that the performance of the contract has become impossible to perform.

The Indian courts have time and again upheld the principle of sanctity of contracts,¹⁷ which means that any situation that prevents performance of a contract must be such that it affects the fundamental nature of the contractual relationship. When the contract is voided, both contracting parties would be discharged of their subsequent obligations, and neither party would have the right to sue the other party for breach of the contract.

Following a similar approach, the Ministry of Finance¹⁸ has recently clarified that in line with the definition of force majeure detailed under the “Manual For Procurement Of Goods, 2017”¹⁹ the disruption of a supply chain caused by the spread of the COVID-19 in China or any other country would constitute a ‘natural calamity’ and hence, the force

¹² MANU/SC/0362/1961.

¹³ See, e.g. <https://www.natlawreview.com/article/boilerplate-contract-language-coming-to-forefront-force-majeure-clauses-and-covid-19>.

¹⁴ Id.

¹⁵ Section 56 of the Act, lays down the legal principle of ‘Doctrine of Principle’ wherein it has been mentioned that an agreement to do an impossible act would be held to be void.

¹⁶ High Court of Andhra Pradesh in the case of *Alluri Narayana Murthy Raju vs. Dist. Collector and Ors.* (MANU/AP/0514/2008).

¹⁷ Allahabad High Court in the case of *Ganga Singh And Ors. vs Santosh Kumar And Ors* (AIR/1963/All 201).

¹⁸ Refer to Office Memorandum, No: F.18/4/2020-PPD- dated February 19, 2020, issued by Ministry of Finance, Department of Expenditure, Procurement Policy Division, Government of India.

¹⁹ https://doe.gov.in/sites/default/files/Manual%20for%20Procurement%20of%20Goods%202017_0_0.pdf

majeure clause may be invoked, wherever considered appropriate, by following the set-procedure specified in the said notification.²⁰ The notification further clarifies that: (i) by invoking the force majeure clause, it does not free the contractual obligations of the parties entirely but only suspends it for the duration of the non-performance obligation; and (ii) additionally, in the event a force majeure clause is invoked for a period of more than 90 (ninety) days, then in such an event, either party to a contract may have the right to terminate the said agreement.²¹

Not all governmental agencies, however, seem to be following this approach. For instance, a few relevant government authorities such as the state-run Solar Energy Corporation of India, has recently stated in a letter addressed to the Government of Uttar Pradesh that the claim of the Uttar Pradesh Distribution Companies invoking the force majeure clause and wanting to seek relief in light of the ongoing COVID-19 pandemic, is not valid grounds for seeking relief from its performance obligations enlisted under the said contract.²²

CONCLUSION

In light of the above, it is evident that to claim relief under a force majeure event and/or under the Doctrine of Frustration, a party to a contract would need to establish that given the present situation in the COVID-19 pandemic, the obligations to perform have become such that its performance obligations as provided under the contract have become impossible to perform, in light of the on-going economic and business scenario. Additionally, in light of the on-going COVID-19 pandemic, the following key-takeaways, should be kept in mind by the parties to a contract:

The impact of a force majeure event cannot be generalized, and the nature of a force majeure event will vary depending on each contract and transaction. In the event a party to a contract wishes to seek relief under the force majeure clause (if contained in a contract), then it would most definitely be critical to examine the wording of each contract individually and separately, and on a case-to-case basis. Each contract would need to be examined and should be carefully studied to see whether relief can be achieved under the provisions of the force majeure clause provided in the particular contract. Further, an analysis should be made whether the clause has been drafted in a way to include an event such as COVID-19 under the head of a pandemic and what relief has been provided under the contract.

In the event of a dispute, it would be interesting to see how the courts interpret disputes involving unforeseen circumstances such as on the ongoing COVID-19 pandemic. Will they interpret each contract based on the language and devise a test enlisting a list of conditions? In contract cases where force majeure may come into play, parties should seek legal advice and form strategies for renegotiation of existing contracts. At present, under the applicable provisions of the Indian law, there is no set of judicial precedents which detail and discuss on whether COVID-19 would constitute to be a 'pandemic' or not.

Faced with the present set of circumstances and the unique challenges brought about by the global pandemic, companies should review their ongoing contracts and undertake a thorough risk analysis regarding the performance obligations of the contracts. Very soon, the relevant authorities from the Government of India are also likely to come out with further clarification, enabling stakeholders to obtain more clarity and find their way forward. This is especially true for those entities dealing with governmental agencies, and when circumstances are such that invoking the force majeure clause in government contracts may seem like a useful path forward.

In light of the COVID-19 pandemic, parties that are presently negotiating contracts should consider whether the lockdown conditions and a potential resurfacing of the virus could amount to a force majeure event for their contracts. Contracting parties should also try to anticipate how such occurrences could affect the performance of their obligations and what measures and alternatives can be resorted to under such circumstances, and if possible, they should make suitable amendments to their existing contracts. For example, COVID-19 will most likely have

²⁰ See Office Memorandum, *supra* at note 18.

²¹ *Id.*

²² <https://www.financialexpress.com/industry/renewable-energy-seci-says-up-discoms-force-majeureclaim-notvalid/1914091/>

an impact on commercial leases and other acquisitions in the real estate sector as many companies have already started feeling the financial impact of COVID-19. The number of these companies is only expected to rise in the near future. It would be prudent to review the wording of each contract independently and review the wording of each clause independently. In fact, there are already reports where various parties are seeking to invoke force majeure clauses to obtain relief for the payment of rents to building contractors and mall owners.

In sum, and in light of the current ongoing COVID-19 pandemic, parties should carefully evaluate the wording of each contract being entered into. They should clarify within the agreement in itself the relief mechanism should a party be unable to perform its obligations or a part of its obligations), which include but are not limited to the following: (i) 'force majeure and frustration'; (ii) 'events of default', (iii) 'material adverse effect'; (iv) 'suspension of performance/termination'; and (v) 'payment and guarantee terms'.