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FORCE MAJEURE AND ITS APPLICABILITY DURING COVID-19 CRISIS IN THE INDIAN CONTEXT

- Debajyoti Panda

Since the Great Depression of the 1930s, COVID-19 is the only catastrophic event that has caused the broadest and deepest health and economic impacts of any single non-war event. The sudden and unprecedented onset of the Covid-19 pandemic has been a humanitarian as well as an economic crisis for the whole world. Like others, India too has been seriously impacted by the COVID-19 especially in the areas of cross-border trade, the real estate market, specifically the developers, the home-buyers, and the commercial lease arrangements. It has also impacted the party’s ability to meet their contractual obligations due to restriction in movement, stoppage of production, increase in costs due to scarcity of raw materials components, labor shortages, shortage of funds, disruption in the supply chains.

As a result of such restrictions, it has raised some serious doubts on the ability of parties to perform their obligations under contracts when these are not ordinarily classified as ‘essential services’. Uncertainty as to the performance of contracts has led to parties envisaging breaches of contract and assessing their rights and remedies concerning the same. The Doctrine of Force Majeure and the frustration of contract are the two common defences that have been used frequently vide the hardships faced by the parties due to this pandemic. But, one issue that has quickly arisen is that whether the COVID-19 event constitutes a force majeure under national or international law or not. The following article will try to put some light to this pertaining issue by analysing the recent judgements that were passed amid this lockdown.

FORCE MAJEURE

Force majeure is a common clause in contracts that essentially frees both parties from liability or obligation when an extraordinary event or circumstance beyond the control of the parties, such as war, strike, riot, crime, epidemic or an event described by the legal term act of God, prevents one or both parties from fulfilling their obligations under the contract.

The Indian contract act does not specifically define what the term force majeure means but its reference can be found under Section 32 of the Indian Contract Act.
A force majeure clause in a contract provides temporary relief to the party bound to perform his obligations under such a contract when a force majeure event occurs. A force majeure in a contract states under what circumstances or events will such clause apply to a contract and what would be the consequences when such an event happens. The circumstances or the events recorded must be beyond the control of either party and the parties will be required to demonstrate that they have made attempts to mitigate the impact of such force majeure event. In practice, most force majeure clauses do not excuse a party's non-performance entirely, but only suspend it for the duration of the force majeure.

If a contract does not include a force majeure clause, the parties resort to the defence of frustration of contract. The common law principle of frustration of contracts which is embodied in Section 56 of the Indian Contract Act 1872.

A frustrated contract is a contract that, subsequent to its formation, and without fault of either party, becomes impossible to perform in the manner that was contemplated by the parties to the contract. In other words, ‘frustration of contract’ occurs whenever, without default of either party, a contractual obligation becomes incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract.

**THE INDIAN SCENARIO AMID THE COVID-19 OUTBREAK:**

The Covid-19 pandemic is unprecedented in its global reach and impact. The havoc of COVID 19 is such that it has put all the nations globally into a state of public health emergency. This brought about an adverse impact on the global economy and on performance of contracts.

The first case of COVID-19 in India was reported on 30 January 2020, when a university student from Wuhan, China travelled back to Kerala. As a preventive measure against the spread of the pandemic in India the Government of India ordered a nationwide complete lockdown for 21 days on 24 March, 2020 which extended for almost 4 months and unlocked phase wise till today.

During this lockdown period, all transport services such as road, air and rail, educational institutions, industrial establishments and hospitality services stand suspended, with exceptions for transportation of essential goods, fire, police and emergency services, food shops, banks and ATMs, petrol pumps, other essentials and their manufacturing. With
disruption in supply chains, domestic and international travel, and business operations, many individuals and businesses are unable to fulfill their existing contractual obligations.

The pandemic and the consequent lockdown has created a major impact in the areas of loans, government contracts as well as private contracts, lease agreements and other agreements such as employment, service and retainer to name a few.

1. LOANS

To ease impact of lockdown, a series of measures were announced by the Reserve Bank of India (RBI) in the Monetary Policy Committee (MPC) meeting held on 27 March 2020. The RBI has imposed a 3 month moratorium/temporary halt on all term loans (on home, personal, agriculture, auto, crop loans) outstanding as on 1 March 2020 and allowed banks to defer payment of installments on loans including EMI, credit card dues, principal or interest payments, bullet payments, until 31 May 2020, as part of the measures. Thus resulting in the extending the tenure of such loans by 3 months after the moratorium. However, interest shall continue to accrue on outstanding portion of the term loan during the moratorium period i.e. at the end of three months, the interest will be added to the outstanding term loan and will have to be paid.

Additionally, the repo rate and reverse repo rates have been reduced, cash reserve ratio (CRR) of banks and marginal standing facility have also been reduced apart from long term repo auctions to inject liquidity of 3.74 lakh crore into the system.

2. GOVERNMENT CONTRACTS:

The Ministry of Finance has by way of an office memorandum (O.M. No. 18/4/2020-PPD) issued on February 20, 2020, clarified that the disruption of the supply chains due to the spread of coronavirus in China or any other country should be considered as a case of natural calamity and “force majeure clause” may be invoked, wherever considered appropriate, following the due procedure. However, such clarification has been provided only concerning the disruption of the supply chains and as indicated above, the invocation of force majeure provisions in light of COVID-19 will have to be assessed on a case-to-case basis depending on the terms of the contract entered into between the parties.

Para 9.7.7 of the Manual of Procurement of Goods, 2017 inter alia states that a force majeure event does not excuse a party’s non-performance entirely, but suspends it for the duration of
the force majeure event. The clause requires a party to give notice of the force majeure event as soon as it occurs and cannot be claimed ex post facto/with retrospective effect.

However, government notifications are only restrictive. The bottom line as to whether a party can have the benefit of force majeure or not shall depend on the contractual provisions. The events constituting force majeure event stipulated in the contract shall be considered to determine whether the performance of the contract may be suspended or will stand frustrated.

3. PRIVATE CONTRACTS

In case of private contracts, if the contract has an express or implied Force Majeure Clause, the obligation of the parties will be determined by the consequences specified in the force majeure clause. In such a case, the terms of the contract would have to be examined to determine what events enable parties to invoke the Force Majeure clause and whether outbreak of a pandemic constitutes a force majeure event, subject to compliance of requirements of notice etc., if any, as specified under the contract.

But if there is no force majeure clause in a contract, or on occurrence of an event dehors the contract (for eg., the outbreak of Covid-19) the common law principle of ‘frustration of contracts’ which is embodied in Section 56 of the Indian Contract Act 1872 shall govern the contract.

Therefore in determining whether a contract is frustrated, an assessment of all relevant factors is necessary. They are the terms of the contract; factual background to the contract; party’s knowledge and expectations about risk when entering into the contract; the parties ability to perform the contract in the circumstances which are said to have frustrated the contract.

4. LEASE AGREEMENTS

It is the Lease Agreement that governs the relationship between a Lessor and Lessee are governed. But when the force majeure clause is absent in the Lease Agreement, such agreement will be governed by the general law of Contract and Transfer of Property.

Courts in India have generally taken the view that Section 56 of the Contract Act is not applicable when the rights and obligations of the parties arise under a transfer of property under a lease. Under a lease agreement, there is a transfer of right to enjoy that land/property. If any material part of the property be wholly destroyed or rendered substantially and permanently unfit for the purpose for which it was let out, because of fire, tempest, flood, violence of an army or a mob, or other irresistible force, the lease may, at the option of the
lessee, be avoided. This rule is incorporated in Section 108(e) of the Transfer of Property Act and applies to leases of land, to which the Transfer of Property Act applies, and the principle thereof to agricultural leases and to leases in areas where, the Transfer of Property Act is not extended. Where the property leased is not destroyed or substantially and permanently unfit, the lessee cannot avoid the lease because he does not or is unable to use the land for purposes for which it is let out to him.

The possession of the leased premises by the lessee is the fundamental basis of a lease agreement. So in the present scenario the question whether the outbreak of Covid-19 can be said to fall within the expression ‘or other irresistible force’ in Section 108(e) is a question to be determined the courts. But, presently, even though an unforeseen event not in contemplation of the parties has occurred i.e. the outbreak of Covid-19, the event being temporary and transitory in nature, till the time it is not shown that the fundamental basis of the contract i.e. the possession of premises of the Lessor, is destroyed, or the leased premises has become permanently unfit for use, the contract cannot be said to be frustrated and the Lessee is bound to pay rent in terms of the Lease Agreement.

5. EMPLOYMENT/SERVICE/RETAINER AGREEMENTS

In case of employment agreements, in order to determine whether the doctrine of frustration of contracts as embodied in section 56 of Indian Contract Act would apply, in absence of an express or implied clause in the agreement, what has to be considered is whether at the time of entering into the contract, the parties could have reasonably anticipated the occurrence of the force majeure event i.e. in the present scenario- outbreak of Covid-19. Whether, such event is beyond the affected contracting party’s control and whether performance of the contract/service/job becomes ‘impossible’ or ‘unlawful’ due to the occurrence of the event.

Subject to the intention of the parties, term/duration of the employment agreement and the fundamental basis/ foundation of the agreement, the outbreak of Covid-19, being temporary and transitory in nature, is a temporary alteration of circumstances in which the contract was made and even though it may be financially unfavorable or impractical or lead to leading to monetary hardship for the employer it will not amount to frustration of a contract of long term employment.
JUDICIAL TRENDS

In the case of Satyabrata Ghosh vs. Mugneeram Bangur & Co., the Supreme Court laid down the enforceability of the doctrine of frustration under section 56 of the Contract Act. The apex court held that “the doctrine of frustration is really an aspect or part of the law of discharge of contract by reason of supervening impossibility or illegality of the act agreed to be done and hence comes within the purview of Section 56 of the Indian Contract Act. It would be incorrect to say that Section 56 of the Contract Act applies only to cases of physical impossibility and that where this section is not applicable, recourse can be had to the principles of English law on the subject of frustration. It must be held also, that to the extent that the Indian Contract Act deals with a particular subject, it is exhaustive upon the same and it is permissible to import the principles of English law de hors these statutory provisions. The decisions of the English Courts possess only a persuasive value and may be helpful in showing how the Courts in England have decided cases under circumstances similar to those which have come before our Courts.”

In the case of Alopi Parshad & Sons Ltd. v. Union of India, the Supreme Court held that the courts have no general power to absolve a party from the performance of his part of the contract merely because its performance has become onerous on account of an unforeseen turn of events. Commercial hardship will not by itself support frustration and excuse performance.

In the case of Dhanrajmal Gobindram v. Shamji Kalidas & Co., the SC held that wherein a contract, the reference is made to force majeure, the parties intend to save the performing party from the consequences of anything over which it has no control. If this is the underlying meaning that comes out from the specified contractual provision, that condition about force majeure cannot be considered vague. Even if there lies some vagueness in such a clause, it is capable of being made certain and definite based on the dealings of the parties in the ordinary course of business and other related proofs.

In the case of Energy Watchdog vs. Central Electricity Regulatory Commission and Anr., the Supreme Court stated that “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. The

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1 1954 SCR 310(12)
2 AIR 1960 SC 588
3 AIR 1961 SC 1285
4 (2017) 14 SCC 80
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."

THE PRESENT SCENARIO

As highlighted above, the spread of the COVID-19 pandemic and lockdowns imposed by several nations have made performance of contracts challenging and/or impossible. India was until recently, under a complete lockdown since 25th March 2020. All commercial activities saving a few ‘essential services’ were suspended. Resultantly, Indian courts have started witnessing the onslaught of contractual disputes inter-alia revolving around the doctrine of frustration. The initial approach of the Indian Courts has varied from case to case as can be seen from the recent Orders of the Bombay High Court and the Delhi High Court.

In the case of Rural Fairprice Wholesale Ltd. & Anr. vs IDBI Trusteeship Services Ltd. & Ors the Bombay High Court recognized the market situation pursuant to the COVID-19 and observed that the share market had collapsed due to COVID-19, therefore, it was a fit case to restrain the bank from acting upon the sale notices and a direction to withdraw any pending sale orders for the pledged shares.

But in the case of Standard Retail Pvt. Ltd vs Gs Global Corp and Ors the Bombay HC departed from its previous order and refused to grant interim measures to the Petitioner observing that the commodity in question was an essential item and lockdown is only for a limited period. Consequently, Petitioner cannot resile from its contractual obligation of making payments to the Respondents.

In the case of Halliburton Offshore Services Inc. vs Vedanta Ltd. and Anr the case pertained to restrain on invocation of bank guarantees. However, the Delhi High Court observed that even in cases where 'irretrievable or irreparable injury' or 'special equities' existed, the invocation of bank guarantee may be stayed. The Court, after due consideration, took a liberal view and granted an ad-interim injunction in favor of Halliburton Offshore Services Inc. noting that COVID-19 pandemic and lockdown were prima facie Force Majeure events, beyond the comprehension of any party. Therefore, it could be said that special equities do exist, as would justify grant of the prayer, to injunct invocation of the bank guarantees.

5 Order passed on 3rd April 2020
6 Order passed on 8th April 2020
7 O.M.P. (I) (COMM) & I.A. 3697/2020
In the case of **Indirajth Power Private Limited v. UOI & Ors** the Petitioner sought interdiction of the Bank Guarantee inter-alia on account of the lockdown in the country due to spread of COVID-19 pandemic, which could drive the Petitioner towards being declared an NPA. The Court while observing the Petitioner’s conduct i.e. despite the extension of 12 months, could not fulfil its obligation under the Contract, refused to grant relief to the Petitioner. The Court observed that Petitioner’s position under the contract was unaffected by the imposition of the lockdown.

Therefore, the exemption of Force Majeure indeed depends on case to case. While a Court can grant equitable reliefs such as temporary injunctions, the threshold for meeting Force Majeure and frustration criteria is generally high.

**CONCLUSION**

In the events of impossibility Force Majeure has always been regarded as one of the exceptional defenses. Even though the quality of proof is very high, the Courts will decide its implacability on a case by case basis. It is however, best left for the parties to draft proper Force Majeure clauses to include events precluding them from performing contracts. Hence, a surge in the number of commercial contracts incorporating Force Majeure clauses is very likely – to specifically cover situations such as Government imposed lockdowns, epidemics and pandemics, apart from traditional events such as Act of God, natural calamities, etc.

It can be positively state that contracts are impacted by the pandemic and also by the current lock-down situation. However, within the times to return, we shall also be witnessing varied interpretation of clauses, terms, and parameters of performance of contracts under these unforeseen circumstances as well as notifications and directives by the govt. during this respect. The law relating to Force Majeure is will be massively amended in the view of this current pandemic.

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8 Order passed on 28th April 2020