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The Effect of Outbreak of COVID-19 on Force Majeure Clause in Commercial Contracts: An Indian Perspective

AMBICA BATAS¹ AND MEET SHAH²

ABSTRACT

The recent outbreak of COVID-19 has a devastating impact on mankind and countries globally, its outreach has also affected the trade, business and commerce of the nations. The rapid spread of the pandemic has made the Governments take eminent and vital steps to save the community along with saving the economy of the country. Amidst such policies, India took a decisive move of complete lockdown of the country which has led to disruption and closure of industries and businesses. Consequently, it has impacted the performance of contracts and obligations entered by the parties. This has endeavored to demystify the concept of Force Majeure in the commercial contracts. The current Research Paper analyses the applicability of 'Force majeure' clause incorporated in commercial contracts during the current pandemic outbreak of COVID-19. It further evaluates the contracts which do not have such clause and the consequences on the business transactions thereof. Lastly, the extent of limitation period of a contract is also critically analyzed.

Keywords: Contracts, Force Majeure, COVID-19, Limitation period

I. INTRODUCTION

Who in this era of scientific and swift commercial transformation would have thought that a sub-microscopic virus could bring the world to a standstill. The recent outbreak of the COVID-19 i.e. Coronavirus Disease has made this period of time as the most crucial testing times of the human generation. COVID-19 is defined as a global health crisis of this generation which through its spread has affected the lives on every country of each continent. Countries are racing to slow the spread of the disease by testing and treating patients, carrying out contact tracing, limiting travel, quarantining citizens, and cancelling large gatherings such as sporting events, concerts, and schools. The pandemic is moving like a wave, one that may yet crash on

¹ Author is Teaching and Research Associate at Gujarat National Law University, India.

² Co- Author is an Advocate, practicing in Gujarat, India.

those least able to cope.³

With the advent of civilization and industrialisation in the human life, there has always been an interactions and aspiration of financial and economic growth of individual. Every individual is striving for professional growth. This need of profit making and monetary interaction has given rise to establishment of business activities. People carry out their business with one another in the form of sale and purchase which may be either for goods or services. In order to maintain cordial relations amongst themselves and ensuring smooth functioning of their business, parties often enter into contracts which bind them on agreed mutual terms and conditions.⁴ Such commercial contracts often contain a disused clause called *Force Majeure*.

The virus has affected all walks of life and collapsed the economy and market of majority countries. The Governments are struggling to keep the economical graph from crumbling and are introducing numerous policies and benefits for the industry and business organizations. Countries like India have taken a major step of complete lockdown to reduce the spread of Coronavirus. A Barclays research estimates India's loss of economic activity could be as high as \$234 billion in the lockdown period, resulting in zero per cent GDP growth this fiscal year.⁵ Consequent to lockdown, the industries and the businesses have been gravely impacted and so has been the enforcement of the commercial agreements and contracts which were entered by the parties. There has been disruption in the supply chains leading to the closure or interruption in manufacturing of several products and services globally. Hence, the much obliterated *Force Majeure* clause has now come into scrutiny under the existing commercial contracts. Therefore, it is the ripe time to study the effect of outbreak of COVID-19 on the *Force Majeure* clause in commercial contracts.

II. STATUS OF COVID-19

On 11th March 2020, the Director-General of World Health Organization (“WHO”) informed through media briefing that COVID-19 is characterized as a **pandemic**.⁶ A pandemic is defined by WHO as a worldwide spread of a new disease.⁷ Similarly, the Dictionary of Epidemiology

³ UNDP, *Coronavirus disease COVID-19 pandemic | UNDP*, (Apr. 15, 2020, 10:05 AM), <https://www.undp.org/content/undp/en/home/coronavirus.html>.

⁴ S.S. Rana & Co. Advocates, *India: Force Majeure clauses in Contracts*, (Apr. 15, 2020, 10:30 AM), <https://www.mondaq.com/india/government-contracts-procurement-ppp/737524/force-majeure-clauses-in-contracts>.

⁵ Nirbhay Kumar, *Lockdown 2.0: How it impacts ailing economy*, India Today, April 16, 2020, at <https://www.indiatoday.in/mail-today/story/lockdown-2-0-how-it-impacts-ailing-economy-1667426-2020-04-16>.

⁶ WHO, *WHO Director-General's opening remarks at the media briefing on COVID-19 - 11 March 2020*, (Apr. 16, 2020, 1:00 PM), <https://www.who.int/dg/speeches/detail/who-director-general-s-opening-remarks-at-the-media-briefing-on-covid-19---11-march-2020>.

⁷ WHO, *What is a pandemic?*, (Apr. 16, 2020, 1:00 PM), https://www.who.int/csr/disease/swineflu/frequently_asked_questions/pandemic/en/.

describes a pandemic as “*an epidemic occurring worldwide, or over a very wide area, crossing international boundaries and usually affecting a large number of people*”⁸. It is imperative to be cognizant of the threat posed by COVID-19 in order to determine its status thereof. In a nutshell, the Director-General of WHO stated that on one hand, we have never witnessed in the history of mankind a pandemic caused by Coronavirus and on the other hand, the pandemics experienced by us were never successfully controlled.⁹ In *toto*, COVID-19 is declared as a never experienced and life threatening pandemic rapidly spreading across the world by infecting thousands of humans on a daily basis.

III. FORCE MAJEURE CLAUSE IN A COMMERCIAL CONTRACT

Black’s Law Dictionary defines ‘*Force Majeure*’ as “*an event or effect that can be neither anticipated nor controlled, is unexpected and which prevents someone from doing or completing something that he or she had agreed or officially planned to do*”¹⁰. In contractual terms, a *Force Majeure* denotes the occurrence / happening of an unforeseeable event that prevents the parties to perform the contract. Parties to a contract are at liberty to incorporate a *Force Majeure* clause in their contract. The Indian law mandates that a *Force Majeure* clause shall be expressly provided in the contract to avail its protection thereof; and parties cannot invoke an implied *Force Majeure* clause howsoever.

Parties to a contract may mutually decide the list of events to be categorized under the clause. It is common to find a boilerplate *Force Majeure* language in commercial contracts. The *Force Majeure* clause may be exhaustive or inclusive. Exhaustive *Force Majeure* typically includes events like acts of God, war, terrorism, acts of Government, strikes at national level etc. In an inclusive *Force Majeure* clause, parties agree to the events constituting *Force Majeure* and thereafter add phrases such as ‘and other similar events’, ‘and such other acts’ etc. However, it is to be noted that whether a particular event falls within the ambit of *Force Majeure* essentially is a fact-based inquiry depending upon the interpretation of the clause as provided in a contract. Successful invocation of a *Force Majeure* clause in a contract allows the parties to terminate their contractual obligations. However, it is noteworthy that the Indian Courts have strictly interpreted *Force Majeure* clauses in a contract and are not inclined to frustrate the contract on minimal and trifling grounds. The burden is on the party invoking the *Force Majeure* clause to

⁸ JM LAST, A DICTIONARY OF EPIDEMIOLOGY(4 Ed., 2001).

⁹ WHO, *WHO Director-General's opening remarks at the media briefing on COVID-19 - 11 March 2020*, (Apr. 16, 2020, 1:00 PM), <https://www.who.int/dg/speeches/detail/who-director-general-s-opening-remarks-at-the-media-briefing-on-covid-19---11-march-2020>.

¹⁰ Black’s Law Dictionary, 10th ed., 2014.

prove that the event in question falls within the four corners of the clause. Further, as the definition says, the party also needs to satisfy the Indian Courts that the event alleged to be *Force Majeure* was not foreseeable and / or controllable.

IV. LEGAL CONTRACTS WITH *FORCE MAJEURE* CLAUSE

It is rare that any contract may have expressly referred COVID-19 as a *Force Majeure* event owing to the fact that the global community has never witnessed such an outbreak. Though the impact of COVID-19 is still unfolding day by day, there are various reasons that COVID-19 will be considered as a *Force Majeure* event by the Indian Courts in near future. The various reasons supporting the invocation of *Force Majeure* clause due to the outbreak of COVID-19 are succinctly discussed below.

- The Department of Expenditure (Ministry of Finance, Government of India) on 19th February 2020 *vide* Office Memorandum expressly clarified that COVID-19 is a natural calamity and thus, is covered in the *Force Majeure* clause provided in the Manual for Procurement of Goods, 2017. The said Memorandum further clarified that parties to the contract may terminate their contractual obligations / liabilities by following the due procedure to invoke the *Force Majeure* clause.
- Many a times a *Force Majeure* clause in a contract expressly incorporates epidemic and / or pandemic disease as one of its events. In such cases, it becomes crystal-clear that the COVID-19 will trigger the *Force-Majeure* clause agreed between the parties.
- It is observed that a typical *Force Majeure* clause in a contract includes ‘Governmental orders’, ‘change in law’ and / or ‘act of Government’ as one of the events to invoke the clause. The Government of India ordered a state of lockdown at national level for a period of 21 days with effect from 25th March 2020 *vide* Order¹¹ dated 24th March 2020 read with the Guidelines¹² and its addendums¹³. All commercial and private establishments were ordered to be closed barring a few essential services. One may successfully argue that the performance of contractual obligations of parties in a contract has not only become

¹¹ Ministry of Home Affairs, *Order No. 40-3/2020-DM-I(A)*, March 24, 2020, at https://www.mha.gov.in/sites/default/files/MHAorder%20copy_0.pdf.

¹² Ministry of Home Affairs, *Order No. 40-3/2020-D*, March 24, 2020, at https://www.mha.gov.in/sites/default/files/Guidelines_0.pdf.

¹³ Ministry of Home Affairs, *Order No. 40-3/2020-DM-I (A)*, March 25, 2020, At https://www.mha.gov.in/sites/default/files/MHA%20order%20with%20addendum%20to%20Guidelines%20Dated%2024.3.2020_0.pdf; read with Ministry of Home Affairs, *Order No. 40-3/2020-DM-I (A)*, March 27, 2020, At https://www.mha.gov.in/sites/default/files/PR_SecondAddendum_27032020_0.pdf; & Ministry of Home Affairs, *Order No. 40-3/2020-DM-I (A)*, April 2, 2020, At https://www.mha.gov.in/sites/default/files/3rd%20Addendum%20dated%202.4.2020%20to%20Lockdown%20measures_0.pdf.

impossible but also unlawful and against the order of the Government. Violation of the order attracts penalties to the fullest extent of law. The source of lockdown is the said Governmental order / act of Government and consequentially, there is also change in law wherein day-to-day business activities are suspended. Therefore, failure to perform contractual obligations fairly fall within the parameters of *Force Majeure*.

- In most contracts, a *Force Majeure* clause includes events like Acts of God that can neither be anticipated nor controlled by any of the parties and as a consequence, it prevents one or both of the parties from performing their contractual obligations. There is no doubt that COVID-19 was beyond any reasonable control of or anticipation by any of the parties to a contract. The media briefing of the WHO's Director-General on 2nd March 2020 further added that no one has before seen a respiratory pathogen that is capable of community transmission, but which can also be contained with the right measures.¹⁴ Further, the consequences of the outbreak have led the commercial market to a standstill / in a state of lockdown which has made it impossible as well as unlawful for the parties to perform their contractual obligations.
- Many a time a *Force Majeure* clause in a contract includes words like 'and other similar events'. In such cases, *Ejusdem Generis* rule may be applied to consider COVID-19 as a *Force Majeure* event. *Ejusdem Generis* is a rule of interpretation of contracts. The rule states that where specific words are followed by a general expression, the general expression is limited to the shared characteristics of the specific words. For example, a *Force Majeure* clause may include 'outbreak of disease such as Severe Acute Respiratory Syndrome (SARS), Middle East Respiratory Syndrome (MERS) or **any other similar contagious disease**'. In such a case, 'any other similar contagious disease' is a general expression prefixed by specific diseases. Thus, one may argue that outbreak of COVID-19 falls within the scope of the general expression.

V. LEGAL CONTRACTS WITHOUT *FORCE MAJEURE* CLAUSE

As stated above, incorporation of a *Force Majeure* clause in a commercial contract is not mandatory and there may be contracts without a such a clause. Naturally, in such cases, the affected party will not be able to invoke the principle of *Force Majeure*. However, the affected party will be at liberty to claim relief under the doctrine of frustration under section 56 of the

¹⁴ WHO, WHO Director-General's opening remarks at the media briefing on COVID-19 - 2 March 2020, (Apr. 19, 2020, 4:00 PM), <https://www.who.int/dg/speeches/detail/who-director-general-s-opening-remarks-at-the-media-briefing-on-covid-19---2-march-2020>.

Indian Contract Act, 1872. The second part of section 56 is reproduced below for easy reference.

“56. ...

Contract to do an 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.

...”

(Emphasis Supplied)

Impossibility arising subsequent to the formation of a contract which could be performed at the time when the contract was entered into is called a post-contractual or supervening impossibility. In such a case, the contract becomes void when the act becomes impossible or unlawful. It is to be noted that self-imposed impossibility of performance of a contract is no excuse for non-performance. However, parties are discharged from performance of their contractual obligations where the impossibility is caused by circumstances beyond the control of the parties.¹⁵ In the celebrated case of *Satyabrata Ghose v. Mugneeram Bangur & Co.*¹⁶, the Hon’ble Supreme Court observed that:

“... This much is clear that the word “impossible” has not been used here in the sense of 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 which the parties had in view and if an untoward event or change of circumstances totally upset the very foundation upon which the parties rested their bargain, it can very well be said that the promisor found it impossible to do the act which he promised to do...”

(Emphasis Supplied)

It is assumed that the performance of contractual obligations was possible prior to the outbreak of COVID-19. It is to be assessed whether the performance of a contract became impossible or impracticable after the outbreak of COVID-19 and if the answer is in affirmative, the principle of post-contractual or supervening impossibility incorporated under section 56 of the Indian Contract Act, 1872 will be attracted.

As observed by the Hon’ble Supreme Court, impossibility not only means physical or literal

¹⁵ N.D. KAPOOR, ELEMENTS OF MERCANTILE LAW, 125 (2012).

¹⁶ 1954 SCR 301

impossibility but also impracticability. It may be that there is a possibility of performance of contract but the performance will not achieve the desired objects and serve the purpose. It is noteworthy that the burden is on the affected party to prove that there exists a legal binding contract between the parties; the contractual obligations are yet to be performed; the performance of contract has become unlawful, impossible, impracticable or useless from the point of view of the object and purpose; and unlawfulness or impossibility is not self-imposed or due to any reason attributable to the promisor.

COVID-19 has not only made performance of contractual obligations impossible and / or impracticable but has also made it unlawful in certain cases. The state of lockdown has barred commercial transactions between parties. Hypothetically, a vendor has to transport goods (except essential items) to the purchaser under a contractual arrangement. The vendor cannot perform its contractual obligations since such a transport is restricted and any attempt may attract action to the fullest extent of law. Similarly, inter-State trade under any contract cannot take place legally. In other cases, wherein performance of contractual obligations may be remotely possible, the performance needs to be examined from the point of view of the object or purpose of the contract.

VI. LIMITATION PERIOD

Limitation period is the maximum period prescribed by law within which legal action can be initiated or a right can be enforced. Part II of Schedule to the Limitation Act, 1963 lays down the period of limitation for suits relating to contracts. Articles 6 to 53 provides the limitation period for specific contracts such as suit for wages, suit against a carrier, suit relating to negotiable instruments etc. Article 54 provides that the limitation period for the suit relating to specific performance of contract is three years from the date fixed for the performance or if no such date is fixed, when the plaintiff has notice that performance is refused. Similarly, article 55 provides that a suit for compensation for breach of contract not expressly provided in the aforementioned provisions shall be initiated within three years when the contract is broken or where there are successive breaches, when the breach in respect of which the suit is instituted occurs or where the breach is continuing, when it ceases.

It is noteworthy that the Hon'ble Supreme Court, *suo-moto*, took cognizance for extension of limitation period.¹⁷ Taking into account the situation arising from the outbreak of COVID-19 and the resultant difficulties faced by litigants across the country in filling suits, the Hon'ble Supreme Court extended the period of limitation for filling of suits with effect from 15th March

¹⁷ Suo Moto Writ Petition Civil No. 3/2020

2020 till further orders irrespective of the limitation prescribed under any law. The *suo-moto* order is binding on all the Indian Courts, tribunals and authorities.

VII. CONCLUSION

The current outbreak of the pandemic has posed us with challenges to analyze and interpret the *Force Majeure* provisions in the existing contractual arrangements. The interpretations and invocation of the *Force Majeure* clause incorporated in the existing contracts would depend on the construction and interpretation of the clause along with taking account of the circumstances of the case. However, *in toto*, there has been a disruption in supply or production of goods and services, due to which parties to the contract can according to provisions discussed in the Research Paper resort to the shield of the *Force Majeure* provision while enforcing the contract.