

THE CORONA -
CONTRACTS COROLLARY

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I. INTRODUCTION

The rise of COVID-19, the pathogen causing coronavirus which started in the Wuhan region of China has resulted in dramatic consequences with thousands of deaths and complete lockdown in various countries across the world. The fast-growing number of cases and the inability to contain the same has rendered various ramifications on the economy as well. Moreover, the pandemic has various legal implications like handling of employment relations, insurance coverage of epidemic related damages, etc.¹ The economic implications include disruption and delay in performing and carrying out several contractual obligations. Many parties might seek to even terminate the contracts. Since the pandemic has made it impossible for certain contractual obligations to be performed, the principle of *Lex non cogit ad impossibilia* (law compels no one to do vain or impossible) is being used as a defense. Since the delay of performing contractual obligations or termination of the contracts cannot be attributable to either of the parties, legal experts are reviewing and assessing these provisions to find suitable rights and obligations.

The *Force Majeure* or *Vis Major clause* can be found in almost all the commercial contracts. According to Webster, Force Majeure simply translates to “*a superior force*”. The principle of Force Majeure simply means that a party cannot perform certain contractual obligation(s) due to an unforeseen or unavoidable circumstance which is beyond the control of the party. Thus, concerning the current situation of the COVID-19 pandemic, such Force Majeure clauses must be carefully reviewed. It should be cautiously seen whether the current pandemic falls under the Force Majeure clause or not and what are the legal ramifications of the same.

¹ Deloitte Germany, The coronavirus and its consequences, <https://www2.deloitte.com/in/en/pages/risk/articles/legal-consequences-coronavirus-deloitte-germany.html#>

II. WHAT IS COVID-19?

Coronavirus disease popularly known as *COVID-19* (Coronavirus Disease of 2019) is an infectious disease that can affect your lung and airways caused by a newly discovered SARS virus. The COVID-19 virus emerged first in Wuhan, China in December 2019. Scientist Leo Poon who first decoded the virus thinks it most likely started in an animal and spread to humans.² Many scientists believe that it spread through bats to humans. There is no specific treatment for coronavirus yet. Patients are being treated according to the symptoms they show.³ Washing hands, using sanitizers, avoiding direct contact with others are the only ways through which the spread of coronavirus can be prevented. With the World Health Organisation (WHO) declaring the disease as a pandemic⁴, immediate measures have been taken by various countries, one of them being imposing lockdown all over the country.

III. IMPACT OF COVID -19 ON CONTRACTS WORLDWIDE

The virus, despite causing severe harm to life and health, has expanded the damage to other realms as well, one such target is the contracts entered into by companies, industries, and individuals before the outbreak.

Due to massive loss of life, a myriad of people rendered infected, quarantined and lock-down protocols, the world economy has taken a severe hit, which has caused a seismic shock for the domestic markets as well. The response to the aforementioned stimulus was a disorder in the supply chain, business revenues,

² <https://www.cnn.com/2020/01/20/health/what-is-coronavirus-explained/index.htm>

³ <https://www.nbcnews.com/health/health-news/what-new-coronavirus-n1119081>

⁴ <https://www.cnbc.com/2020/03/11/who-declares-the-coronavirus-outbreak-a-global-pandemic.html>

and contractual performance. From construction contracts to manufacturing and supply agreements, if deemed appropriate, the variety of contracts that are likely to be affected by the spread of COVID-19 is undoubtedly humongous. Additionally, this new impossibility brings out challenges against land acquisition, financing of big projects and delay in engineering and technological research and advancements. Many counterparties like the suppliers and professional service lenders (e.g. Independent Consultants & Accountants), may seek to avoid immediate performance, by citing delay or non-performance borne out of an unexpected event. Parties may cite this pandemic as a ground for opting for renegotiation of price and terms of the contract.⁵ To have a better understanding, the topic is been further divided into two parts where the effect of COVID-19 can be seen on International Commercial Contracts and the Indian Contracts.

(A) EFFECT OF COVID-19 ON INTERNATIONAL COMMERCIAL CONTRACTS:

The COVID-19 pandemic has severely impacted contractual performance across the globe, because of this many businesses are confronted with serious commercial consequences. These are the consequences of pandemic other than mortality rate. The pandemic has led to supply chain disruption, series of lockdowns across the world, fear-induced aversion to the workplace and other public gatherings, governments transferring capital to another sector.

This has led to the non-performance of contracts and resulting in huge economic damages. Most of the International Commercial Contracts is between the government of one state and a private party of another state, as the government's

⁵ India: Impact Of COVID-19 on Indian Commercial Contracts:
<http://www.mondaq.com/india/Coronavirus-Covid-19/912876/Impact-Of-COVID-19-On-Indian-Commercial-Contracts>

main policy is now to cope up with the deadly virus, this has incurred millions of dollars to health sectors and due to obstruction of revenue, the government is having a huge capital shortage. To cope up with this, the government will be happy to suspend all contracts to save up capital. Due to lockdown all “*sale and purchase contract*”, “*agency and distribution contracts*” are in a standstill. To protect themselves from turmoil most companies are invoking the “*Force Majeure Clause*”, but the application of this clause to a particular contract would have to be looked individually all over against the stage of litigation and arbitration.

(B) UNDERSTANDING FORCE MAJEURE IN INDIAN SCENARIO:

The main principle involved in the difficulty of the performance of contracts is the doctrine of ‘*Force Majeure*.’ Force Majeure, or ‘*Superior force*’ entails an absolution in performing contractual obligations in case of occurrence of an unforeseen, and uncontrollable event such as Act of God, War, Terrorism, Earthquake, Hurricane, Act of the Government, Explosions, Fire, Plague Epidemics, etc. These events are an entirely natural phenomenon and thus reach beyond the grasp of human control. The performance of a contract in these conditions may be deemed unreasonable. Meaning that in case of any such event happening, that cannot be estimated, and on which there no human control, in such circumstances contractual duty is foregone.

The word ‘*Force Majeure*’ doesn’t find a place in the Indian Contracts Act, rather the principle finds a place in Section 56 of the Act⁶ which contains the doctrine of impossibility. Section 56 of the Indian Contracts Act states that “*An agreement to do an act impossible in itself is void.*” Furthermore, it also states “*A contract to do an act which, after the contract is made, becomes impossible, or, because*

⁶ The Indian Contracts Act, 1872

of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.”

The aforementioned Section is based on the concept of ‘*Doctrine of Frustration*’ which entails two grounds upon which even a legal contract can be termed ‘*frustrated*’ thus absolving performance. The two grounds can be seen as follows:

- (1) performance of a contract is physically impossible, and
- (2) the object of the contract has failed.”

The aforementioned principle may apply to the current scenario as the spread of the virus is both unforeseen and uncontrollable.

A COVID-19 pandemic could make it more difficult for parties to perform their contractual obligations. There are two possible instances, which may suggest that a force majeure clause covers a pandemic:

- (a) if the contractual definition of a force majeure event expressly includes a pandemic. Inclusion of pandemic to the list of force majeure events will provide clarity as to whether the COVID-19 outbreak would trigger a force majeure clause in a contract; or
- (b) if the force majeure, clause covers extraordinary events or circumstances beyond the reasonable control of the parties. Such general, catch-all wording may be invoked if it is determined that the factual circumstances caused by the pandemic are beyond the reasonable control of the affected party.

Having said that, whether a party can be excused from a contract on account of COVID-19 being declared a pandemic is a fact-specific determination that will

depend on the nature of the party's obligations and the specific terms of the contract.⁷

IV. IMPACT OF FORCE MAJEURE CLAUSE ON INSURANCE SECTOR

Force Majeure clause applies otherwise to every sub-category within the insurance sector. For example, just in case of travel insurance. The Insurance Regulator and Development Authority of India (IRDAI) has, in COVID-19 connected directions issued to insurance corporations, same that the policyholders might presently get associate possibility from insurers to increase their travel insurance policy dates while not paying further charges to confirm that the impact of the coronavirus pandemic on their travel plans and finances is pillowed. The choice to increase dates while not further charges could be a relief for those policyholders United Nations agency has or can currently have to be compelled to schedule their air price tag bookings because of the strict imprisonment measures proclaimed by the govt. to contain the unfold of the wide community spreading coronavirus (COVID 19).⁸

In case of life assurance, the Life Insurance Council of India has proclaimed that each one life insurance company, each public and personal, can method all coronavirus-related death claims, at the earliest. In step with an announcement from the life assurance Council, *"The Council additionally confirmed that the clause of 'Force Majeure' won't apply just in case of COVID-19 death claims. The step was taken to reassure customers United Nations agency had reached*

⁷ <https://www.bloombergquint.com/coronavirus-outbreak/covid-19-coronavirus-force-majeure-and-impact-on-commercial-contracts>

⁸ Navneet Dubey, COVID 19 impact: IRDAI asks insurers to allow travel insurance policies' extension sans charges.

https://www.google.com/amp/s/m.economictimes.com/wealth/personal-finance-news/covid-19-impact-irdai-asks-insurers-to-allow-travel-insurance-policies-extension-sans-charges/amp_articleshow/74909336.cms

intent on individual life assurance corporations seeking clarity on this clause within their contract similarly on do away the confusing in the minds of voters. All life assurance corporations have additionally effectively communicated to their customers several during this regard."⁹ The CEOs and CFOs of life insurance corporations have expressly stated that death because of COVID-19 won't be enclosed beneath the life assurance policies.

V. COVID-19 AND FORCE MAJEURE

Law is a dynamic concept and it goes beyond explanation. The epidemic of coronavirus has affected world economies to a greater concept and it was nearly impossible for all the contracts entered prior when COVID-19 was declared as a “*Pandemic*” by the World Health Organisation on 11th March 2020.¹⁰ Given the supply chain disruption caused by the pandemic, it is likely that several contractual obligations are obstructed by this pandemic. The premise of this part of the article revolves around the concept that due to this epidemic where the performance of the contract has become nearly impossible how does the force majeure clauses operate and what reliefs are available to the parties. Will the clause Force majeure operate as a blanket provision for all these situations and what happens in the situation when the agreement does not contain such clauses?

The concept of *Force Majeure* translates from a French word meaning *Superior Force*. It's a common clause in legal contracts that allows either party to limit their liability in the face of some unforeseeable or an extraordinary event. Force majeure means extraordinary events or circumstances beyond the control of

⁹ Navneet Dubey., “Are deaths due to corona virus covered under life insurance policies” https://www.google.com/amp/s/m.economictimes.com/wealth/insure/life-insurance/are-deaths-due-to-coronavirus-covered-by-life-insurance-policies/amp_articles/74687234.cms

¹⁰ <https://time.com/5791661/who-coronavirus-pandemic-declaration/>

parties to a contract and typically includes events described such as an act of God or natural disasters, war or war-like situations, labor unrest or strikes, epidemics or pandemics, etc. The intention of a Force Majeure clause in a contractual agreement is there to rescue the performing party from consequences of something over which it has no control. Generally, on the activation of the Force Majeure clause in the contract, it absolves both parties from contractual liability or obligation under the contract. Force majeure is, therefore, an exception to what would ordinarily otherwise amount to a breach of contract.

When the entire world is at standstill the major issue which is raised: - What happens to the contracts which are impossible to be performed due to the COVID-19 outbreak?

When the change in circumstance occurs after the parties have entered into the contract and render the contract physically impossible to perform, such a contract is said to be frustrated. Not just the physical impossibility but even when the object of the contract loses its significance it would fall under the doctrine of frustration.

The law about Force Majeure in India is governed by the Indian Contract Act, 1872.¹¹ In so far as it relates to express or an implied clause in a contract, it will be governed by Section 32 of the Indian Contract Act.¹² However, where a force majeure event occurs other than a contract, it is dealt with by Section 56 of the Indian Contract Act.¹³

¹¹ The Indian Contract Act, 1872

¹² Section 32 of Indian Contract Act, 1872: Enforcement of contracts contingent on an event happening—Contingent contracts to do or not to do anything if an uncertain future event happens, cannot be enforced by law unless and until that event has happened. —Contingent contracts to do or not to do anything if an uncertain future event happens, cannot be enforced by law unless and until that event has happened." If the event becomes impossible, such contracts become void.

¹³ Section 56 of the Indian Contract Act, 1872: Agreement to do impossible act - An agreement to do an act impossible in itself is void.

The law of Force Majeure in India has been laid down in the decision of *Satyabrata Ghose vs Mugneeram Bangur & Co.*¹⁴ In this case, the Supreme Court or the Apex Court of India held that the word "impossible" has not been used in Section 56 in the sense of physical or literal impossibility. The performance of an act may not be impossible, but it may be impractical and useless from the object and purpose of the contractual arrangement between the parties. If an untoward event or change of circumstance upsets the very foundation upon which the parties entered their agreement, it can be said that the promisor finds it impossible to do the act which he had promised to do. It was further held that where the court finds that the contract itself either impliedly or expressly contains a term, according to which performance would stand discharged under certain circumstances, the dissolution of the contract would take place under the terms of the contract itself and such cases would be dealt with under Section 32 of the Contract Act. If, however, frustration is to take place de hors the contract, it will be governed by Section 56 of the Contract Act.

In *Alopi Parshad & Sons. Ltd. vs Union of India*¹⁵, the Supreme Court held that the Contract Act does not enable a party to a contract to ignore the express covenants thereto, and to claim payment of consideration for the performance of the contract at rates different from the stipulated rates, on a vague plea of equity this is a remedy under Quantum Meruit which is restitutory. The concept of Quantum Meruit can be seen under Section 70¹⁶ of the Indian Contracts Act, 1872. Parties to an executable contract are often faced, in the course of carrying it out, with a turn of events which they did not at all anticipate; for instance, a

¹⁴ *Satyabrata Ghose vs Mugneeram Bangur & Co.*, AIR 1954 SC 44

¹⁵ *Alopi Parshad & Sons. Ltd. vs Union of India*, AIR 1960 SC 588

¹⁶ Section 70 of the Indian Contracts Act, 1872: Obligation of person enjoying benefit of non-gratuitous act.—Where a person lawfully does anything for another person, or delivers anything to him, not intending to do so gratuitously, and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered.

wholly abnormal rise or fall in prices which is an unexpected obstacle to execution. This does not in itself get rid of the bargain they have made. It is only when a consideration of the terms of the contract, in light of the circumstances existing when it was made, showed that they never agreed to be bound in a fundamentally different situation which had unexpectedly emerged, that the contract ceases to bind. It was further held that the performance of a contract is never discharged merely because it may become onerous to one of the parties.

In *Energy Watchdog vs CERC*¹⁷, the Supreme Court held that force majeure clauses are to be narrowly construed. The court opined that in the force majeure clause contained in the contract in question, "*hindrance*" could mean an event wholly or partly preventing performance. However, a mere increase in prices would not amount to a hindrance. It was held that since the force majeure specifically excluded the rise in fuel cost from force majeure, the fundamental basis of the contract was never dislodged. Since alternative modes of performance were available even though the same were at a higher price, a force majeure situation did not arise. The Court further held that since there was a specific clause addressing force majeure in the contract in question, Section 56 of the Contract Act would not have any application.

In a recent case titled as *Prabhat Steel traders Pvt. Ltd vs M/s Hyundai Corporation & Ors.*,¹⁸ a petition was filed in Bombay High Court to enforce the force majeure clause in an agreement between two parties regarding the purchase of certain steel products to dissolve the liability of making payment for the purchase. The petitioners (buyers) pleaded that the doctrine of frustration comes

¹⁷ *Energy Watchdog vs CERC*, (2017) 14 SCC 80

¹⁸ *Prabhat Steel traders Pvt. Ltd vs M/s Hyundai Corporation & Ors.*, Commercial Arbitration Petition No. 407 of 2020 (Bombay High Court, 08/04/2020)

<https://bombayhighcourt.nic.in/generatenewauth.php?bhcpair=cGF0aD0uL3dyaXRlcmVhZGRhdGEvZGF0YS9vcmlnaW5hbC8yMDIwLyZmbmFtZT1DQVJCUDQwNDIwMDgwNDIwLnBkZiZzbWZsYWc9TiZyanVkZGF0ZT0mdXBsb2FkZHQ9MDkvMDQvMjAyMCZzcGZzc3BocmFzZT0xMzA0MjAxMjMjc=>

into picture due to the current coronavirus situation. The Hon'ble High Court rejected the plea of the petitioner holding that firstly the force majeure clause that is available in the contract is available to the sellers and not the buyers and secondly that according to the government notifications, the distribution of steel is declared as an essential service. The Court further held that the lockdown is for a certain limited period and that being so the petitioner could not get out of its liability to the respondents to make payments for the purchase.¹⁹

In light of the COVID-19 Coronavirus, the China Council for the Promotion of International Trade on 17th February 2020, issued over One Thousand Six Hundred '*Force Majeure Certificates*' to firms in thirty sectors, covering the contracts worth over and around USD 15 Billion.²⁰ Similarly, in India, the Department of Expenditure (Procurement Policy Division) of the Ministry of Finance by way of an Office Memorandum (O. M. No. 18/4/2020-PPD) concerning the '*Manual for Procurement of Goods, 2017*'²¹ issued on 20th February 2020 clarified that disruptions of supply chains, due to the Coronavirus should be considered as a case of natural calamity and "*force majeure clause*" may be invoked. This clause is to be assessed on a case to case basis depending on the terms of the contract entered into between the parties, the intent of the parties and steps to mitigate.

¹⁹ <https://www.livelaw.in/amp/news-updates/bombay-hc-refuses-force-majeure-exemption-steel-importers-steel-declared-essential-service-during-lockdown-155083>
https://www.livelaw.in/pdf_upload/pdf_upload-372942.pdf
<https://www.barandbench.com/news/litigation/lockdown-cannot-rescue-steel-importer-from-its-contractual-obligations-to-make-payment-bombay-hc>

²⁰ Dalila Ouerghi, China issues record number of force majeure certs to coronavirus-hit businesses, FASTMARKETS MB (March 02, 2020, 3:48 PM), <https://www.metalbulletin.com/Article/3921083/China-issues-record-number-of-force-majeure-certs-to-coronavirus-hit-businesses.html>

²¹ Office Memorandum issued by Government Of India, Ministry Of Finance dated February 19, 2020
<https://doe.gov.in/sites/default/files/Force%20Majeure%20Clause%20-FMC.pdf>

Some delay or some hardship is very common in all human affairs and it cannot be supposed that any agreement entered will contain all the suitable conditions of non-applicability of event. The courts have been very cautious in discharging the parties to the obligation and no universal formula has been drafted as to what happens to the contractual obligations in the current scenario. However, the detailed precedents as discussed above and forthwith suggests the circumstances which will operate as frustration of contract: -

- Destruction of subject matter
- When circumstances arise, which makes the performance of the contract impossible and in the manner as contemplated.
- The epidemic has destroyed human life worldwide and therefore death or incapacity of the party would also operate as a clause to the frustration of contract.
- The national and state governments have been implementing strict lockdown which has reduced human movement restricted only to essential items and in the scenario of such government, intervention would operate as frustration.

However, the courts in India are sentinels of justice and they had made adequate provisions for the relieves of the parties under section 65 of the Indian contract act. After strict interpretation even when the contract stands frustrated the party who is having any benefit to such frustration has to compensate the party at loss. When the coronavirus operates as a force majeure clause then it is imperative that the law would operate as a whole to provide the remedies too.

VI. CONCLUSION

Thus, there exists a vast difference between the doctrine of frustration and the doctrine of force majeure.

Force Majeure gives a temporary reprieve to a party from performing its obligations under the contract upon the occurrence of a force majeure event, which is an event unforeseeable and uncontrollable, with no human causation, which may result in deferment in performance. It does not excuse the parties from performing their obligations.

The doctrine of Frustration, on the other hand, enumerates the inability of performance of the agreed act due to the occurrence of an event that renders performance impossible. The frustration of a contract is defined in Section 56 of the Indian Contract Act as, “*the performance of an act becomes impossible due to an event in which the party undertaking the performance could not prevent, then such a contract becomes void.*” Consequences of Frustration of a contract is restitution as set out in Section 65 of the Indian Contract Act.

This difference in the principles is crucial herein as one of them entails total absolution in contractual duty whereas another entails a temporary suspension of the same. Thus, the inherent postulates of the contract concerning the “*Unforeseen Situation*” portion must be analyzed thoroughly to determine the contractual liability of the parties involved as well as to determine the impact of the prevailing pandemic which may be classified as an ‘*unforeseen situation*’ on the same.

As part of planning for managing the impact of the COVID-19 crisis all businesses should consider carefully whether they or their counterparties will be able to continue to perform their contractual obligations. If performance may be significantly affected it is crucial to review the terms of your contracts so you understand your rights and obligations and to allow you to scenario-plan accordingly.

We need to understand the starting point under the contract to put ourselves in the best possible position in any ongoing negotiations and to be ready to deal with any situations where agreement is not possible.

At this point, one does not know how this clause will be played in contracts where the threat from pandemics, epidemics, and quarantine is not mentioned. But just as we are learning some life-changing lessons, the legal fraternity could see this clause having major implications on how contract law is penned. This event could shape the law in ways we presently do not know.

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