

“Doctrine of Frustration of Contract”

Ayush Goyal
DES's Shri Navalmal Firodia Law College,
Pune

I. INTRODUCTION:

Black's Law Dictionary defines the term 'contract'¹: An agreement between two or more parties, creating obligations that are enforceable or otherwise recognizable at law. Contracts are voluntary agreements reached between individuals which have benefit for both the parties. The contract happens through a communicative process between the individuals. In almost all the cases, an agreement is formed when one person makes an offer, and the other accepts it. Contract law is based on the principle that parties bargain to form agreements to exchange goods and services and, in the case of a dispute; the courts have to give effect to it. The contract makes provision for the discharge of a contract only where, after its formation, a change of circumstances makes contractual performance illegal or impossible. In English law, such a situation is provided for by the doctrine of frustration². Originally this term was confined to the discharge of maritime contracts by the 'frustration of the adventure', but now it has been extended to cover all cases where an agreement has been terminated by supervening events beyond the control of either party.

II. MEANING AND DEFINITION

Black's Law Dictionary defines the term 'frustration'³: the prevention or hindering of the attainment of a goal, such as contractual performance. A valid contract becomes void if it subsequently becomes illegal or its performance becomes impossible due to change in subsequent events. The impossibility could be due to flood, fire, natural disaster, epidemics, strike, riot, civil war, etc. The contract is said to be frustrated. It has accumulated a lot of deadwood, particularly in the cross-referencing between Indian Law and Common Law. The Indian courts have extensively referred to the common law judgments on impossibility.

¹ Garner Black's Law Dictionary, 9th Edition, p. 365.

² See generally, Treitel, Frustration and Force Majeure (1994).

³ Garner Black's Law Dictionary, 9th Edition, p. 740.

A contract may be frustrated when something occurs after the formation of the contract which renders it physically or commercially impossible to fulfill the contract or transforms the obligation to perform a radically different obligation from that undertaken to perform while executing the contract.

Force Majeure Clause:

Black's Law Dictionary defines *Force Majeure Clause*⁴: A contractual provision allocating the risk of loss if performance becomes impossible or impracticable, especially as a result of an event or effect that the parties could not have anticipated or controlled. The development in relation to frustration of contracts made the contracting parties mindful in stipulating terms that could prevent frustration of the contract. The modality was to make express provisions on all things which could frustrate a contract, like war, floods, and other natural calamities. Once an express provision was made, the express provision would apply. However to require a person to do something impossible or near impossible, even if expressly agreed, would be struck down by the courts as void. The clause on impossibility in standard terms of the contract is called *force majeure* clause. The stipulation makes it possible for the party to extend the performance of contract as well as retain the option of terminating the contract.

III. DEVELOPMENT OF THE DOCTRINE IN THE ENGLISH LAW

Before 1863, it was a general rule of the law of contract that a person was absolutely bound to perform any obligation which had been undertaken, and could not be excused by the mere fact that performance had subsequently become impossible. The classic decision on the rule as to absolute contracts first was highlighted in *Paradine v. Jane*. Where a lessee who was sued for arrears of rent pleaded that he had been evicted and kept out of possession by an alien enemy; such an event was beyond his control, and had deprived him of the profits of the land from which he expected to receive the money to pay the rent. He was nevertheless held liable on the ground that, "*where the law creates a duty or charge and the party is disabled to perform it and hath no remedy over, there the law will excuse him... but when the party of his own contract creates a duty or charge upon himself, he is bound to make it good, if he may, notwithstanding any accident by inevitable necessity, because he might have provided against it by his contract.*"⁵

⁴ Garner Black's Law Dictionary, 9th Edition, p. 746

⁵ (1646) *Aleyn 26*, available at <https://saifdingankar.wordpress.com/>

However this approach proved too strict and potentially unjust even for the 19th century courts. Who were in many respect strong supporters of the concept of freedom of contract, taking the view that it was not for the court to interfere to remedy perceived injustice resulting from a freely negotiated bargain.

The modern law has developed from the classic decision in *Taylor v. Caldwell*⁶. Where the facts were that the defendants had agreed to permit the plaintiffs to use a music-hall for concerts on four specified nights. After the contract was made, but before the first night arrived, the hall was destroyed by fire. Blackburn J., held that the defendants were not liable for damages since the doctrine of the sanctity of contracts applied only to a promise which was positive and absolute, and not subject to any condition express or implied. It was held that, “*as subject to an implied condition that the parties shall be excused in case, before the breach, performance becomes impossible from the perishing of the thing, without default of the contractor... the principle seems to us to be that, in contracts in which the performance depends on the continued existence of a given person or thing, a condition is implied that the impossibility of performance arising from the perishing of the person or thing shall excuse the performance. In none of these cases is the promise other than positive, nor is there any express stipulation that the destruction of the person or thing shall excuse the performance; but that excuse is by law implied.*”

IV. SCOPE OF FRUSTRATION

The doctrine of frustration currently operates within rather narrow confines. This is so for two principle reasons. The first is that the courts do not wish to allow a party to appeal to the doctrine of frustration in an effort to escape from what has proved to be a bad bargain. As per a prominent case⁷ ‘The frustration is not lightly to be invoked to relieve contracting parties of the normal consequences of imprudent commercial bargains’.

The second is that parties to commercial contracts commonly make provision within their contract for the impact which various possible catastrophic events may have on their contractual obligations. Thus, force majeure clauses, hardship and intervener clauses are frequently inserted into the commercial contracts. The effect of these clauses is to reduce the practical significance of the doctrine of frustration because; where express provision has been

⁶ (1863) 3 B. & S.826, available at <https://saifdingankar.wordpress.com>

⁷ Pioneer Shipping Ltd v B.T.P. Tioxide Ltd. (The Nema) (1982) A.C. 724,752.

made in the contract itself for the vent which has actually occurred, then the contract is not frustrated.⁸ Therefore the wider the ambit of contractual clauses, the narrower is the practical scope of the doctrine of frustration.

V. THE THEORETICAL BASIS OF DOCTRINE OF FRUSTRATION

Considerable judicial attention has been paid to the theoretical basis on which the doctrine of discharge of a contract by frustration rests. This is because of a perceived need to explain why a finding of frustration does not constitute a reallocation of risks nor permit an escape from a bad bargain.⁹

The House of Lords in successive pronouncements have set forth a number of learned, but often contradictory, opinions concerning this issue. A number of theories have been put forward at various times. There is no general agreement on the appropriate test to be applied. There are only briefly four principal tests or theories which have been advanced.¹⁰

(i) **Implied Term:**

The preponderance of judicial opinion at one time favored the view that frustration of a contract depends upon the implication of a term. But this does not explain discharge where the performance of the contract is made legally impossible by a change in the law or its operations.¹¹

A contract would therefore be frustrated if a term could be implied that, in the events that subsequently happened, the contract would come to an end. The expression ‘an implied term’ is ambiguous. It may be used in a subjective sense. It may mean a term which the court reads into the contract in order to give effect to what it regards as the parties real intention at the time of contracting. The number of objections may be raised to such an implied term. Particularly, it is difficult to see how the parties could be taken, even impliedly, to have provided for something which never occurred to them¹². Lord Wright said¹³, “*It is not possible, to my mind, to say that if they had thought of it, they would have said: ‘Well, if that*

⁸ Joseph Constantine SS. Line Ltd. v. Imperial Smelting Corp. Ltd. (1942) A.C. 154, 163.

⁹ Pacific Phostates co. Ltd. v. Empire transport (1920) LLR 189 at p 190.

¹⁰ In National carriers Ltd v. Panalpina (Northern) Ltd. (1981) A.C. 675.

¹¹ In the heyday of the implied contract theory legal impossibility was sometimes said to differ from other categories of frustration: Joseph Constantine SS. Line Ltd. v. Imperial Smelting Corp. Ltd. (1942) A.C. 154, 163.

¹² Davis Contractors Ltd v. Fareham U.D.C (1956) A.C. 696.

¹³ Denny, Mott & Dickson Ltd. v. Fraser (James B.) & Co. Ltd. (1944) A.C. 265.

happens, all is over between us'. On the contrary, they would almost certainly on the one side or the other have sought to introduce reservations or qualifications or compensations."

The widespread use of *force majeure* clauses which specify what is to happen on the occurrence of an event which affects one or both parties' performance.

However, the implied term test has been subject to considerable criticism and was later finally laid to rest in *National Carriers Ltd v Panalpina (Northern) Ltd*¹⁴. It was observed that test was artificial since there could be a genuine common intention to terminate the contract upon the occurrence of the event. Therefore, it was accepted that the meaning of the contract must be taken to be, not what the parties did intend, but that which the parties, as fair and reasonable men, would presumably have agreed upon if, having such possibility in view, and they had made express provision as to their several rights and liabilities in the event of its occurrence.

(ii) Just And Reasonable Result:

The discharge of a contract by frustration occurs not because of the actual or imputed will of the parties but by operation of law. The doctrine of frustration is, as Lord Summer pointed out, 'a device, by which the rules as to absolute contracts are reconciled with a special exception which justice demands'.¹⁵ The court exercises a positive function as it releases the parties from further performance of obligations which they would otherwise be bound to perform by declaring a contract to have been frustrated. The recognition of these facts led certain of the judges to the conclusion that the basis of doctrine of frustration was the desire of the courts to reach a just and reasonable result.¹⁶

(iii) Disappearance Of The Foundation Of The Contract:

The doctrine of frustration has also been based upon a theory of the disappearance of the 'basis or the foundation of the contract'. There was requirement of some test which would recognize that frustration did not depend on the intentions of the parties, but which would not permit contracts to be too easily discharged. The first such test to be formulated was that of the 'disappearance of the foundation of the contract'. The question to be asked was whether the events that had occurred were of a character and extent so sweeping as to cause the

¹⁴ (1981) A.C. 675, 693.

¹⁵ *Hirji Mulji v. Cheong Yue S.S. Co. Ltd.* (1926) A.C. 497, at p. 510.

¹⁶ *Joseph Constantine SS. Line Ltd. v. Imperial Smelting Corp. Ltd.* (1942) A.C. 154, at p. 186.

foundation of the contract to disappear.¹⁷ The theory has been rejected by the House of Lords in *National Carriers Ltd v Panalpina (Northern) Ltd.*¹⁸

(iv) Radical Change In The Obligation:

There is now general agreement that the appropriate test to apply to determine whether a contract has been frustrated is that of a ‘radical change in the obligation’. In *Davis Contractors Ltd. v Fareham U.D.C.*, Lord Radcliffe said, “Frustration occurs whenever the law recognizes that without default of either party a contractual obligation has become 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. *Non haec in foedera veni*¹⁹. It was not this that I promised to do...there must be...such a change in the significance of the obligation that the thing undertaken would, if performed, be a different thing from that contracted for.²⁰”

This test has been adopted by the House of Lords in various cases and was reformulated by Lord Simon in *National Carriers Ltd v Panalpina (Northern) Ltd.*²¹

This approach has sometimes been called the ‘construction’ theory, because it requires court to construe the terms of contract in the light of its nature and the relevant surrounding circumstances when it was made to determine the original obligation undertaken by the parties. The court must then consider whether there would be radical change in that obligation if performance were enforced in the circumstances which have subsequently arisen. A mere rise in cost or expense will not suffice.

VI. THE TEST FOR FRUSTRATION

Although the existence of the doctrine of frustration is now firmly established, its juristic basis remains rather uncertain. However in *Lauritzen AS v Wijsmuller BV*²², Bringham L.J sets out five propositions which describe the essence of the doctrine of frustration. These propositions he stated were “established by the highest authority” and were “not open to questions.” The first proposition was that the doctrine of frustration has evolved “to mitigate

¹⁷ F.A. Tamplin Steamship Co. Ltd. v. Anglo-Mexican Petroleum Products Co. Ltd. (1916) 2 A.C. 397, at p 406.

¹⁸ (1981) A.C. 675.

¹⁹ It was not this, that I promised to do.

²⁰ (1956) A.C. 696 at p. 729. This statement was explicitly approved by the House of Lords in *In National carriers Ltd v. Panalpina (Northern) ltd.* (1981) A.C. 675.

²¹ (1981) A.C. 675.

²² (1990) 1 Lloyd’s Rep. 1.

the rigour of the common law’s insistence on literal performance of absolute promises.” And that its object was “to give effect to the demands of justice, to achieve a just and reasonable result”. Secondly, Frustration operates to “kill the contract and discharge the parties from further liability under it” and therefore it cannot be “lightly invoked” but must be kept within “Very narrow limits and ought not to be extended.” Thirdly, Frustration brings a contract to an end “forthwith, without more and automatically”. Fourthly, the essence of frustration is that it should not be due to the act or election of the party seeking to rely on it. Finally, Frustrating event must take place “without blame or fault on the side of the party seeking to reply to it.”

VII. RISKS AND ITS INCIDENCE

Black’s Law Dictionary defines the term ‘risk’²³: the uncertainty of a result, happening, or loss, the chance of injury, damage or loss. The doctrine of frustration is principally concerned with the incidence of risk – who must take risk of the happening of the supervening event? The application of the doctrine must not cause a reallocation of risks; the object of the application is to find a satisfactory way of allocating the risk of supervening events. It is the duty of the courts to determine whether the contract, on its true construction, has made provision for that risk.

(a) Express Provision:

Where the contract makes provision (that is full and complete provision, so intended) for a given contingency, this will preclude the court from holding that the contract is frustrated.²⁴

(b) Foreseen Events:

The question is whether events which were foreseen by the parties at the time of contracting can be relied upon to establish frustration. It may be argued that the parties must be taken to have assumed the risk of an event which was present in their minds at the time of contracting. It is however depends upon the construction of contract, whether there is any express provision in the contract that will be binding in case of happening of foreseen events, or whether, in the absence of any express provision, the issue is left open so as to allow incidence of risk to be determine by the law relating to frustration. For example in the case of

²³ Garner Black’s Law Dictionary, 9th Edition, p. 1442.

²⁴ Bank Line Ltd. v. Capel (A) & Co. (1919) A.C. 435 at p. 455; Joseph Constantine SS. Line Ltd. v. Imperial Smelting Corp. Ltd. (1942) A.C. 154, at p. 163.

W.J. Tatem Ltd v. Gamboa,²⁵ the fact that seizure of the ship was within the contemplation of the parties did not preclude the operation of frustration since the contract made no express provision for the contingency.

(c) Prevention Of Performance In Manner Intended By One Party:

The question is whether a contract will be frustrated by an event which prevents performance in a manner intended by one party alone. In *Blackburn Bobbin Co. Ltd. v. Allen (T.W.) & Sons Ltd.*²⁶

A agreed to sell and deliver to B.B. at Hull a quantity of Finnish birch timber. A found it impossible to fulfill his contract because the outbreak of war cut off its source of supply from Finland. B.B. was unaware of the fact that timber from Finland was normally shipped directly from a Finnish port to England, and that timber merchant did not, in practice, hold stocks of it in England.

The court of Appeal held that there was no frustration. The event that has happened was merely that an event had occurred which rendered it practically impossible for defendants to deliver and it had not been provided for in the contract. To free A from the liability, it would have been shown that the continuance of the normal mode of shipping the timber from Finland was a matter which both parties contemplated as necessary for the fulfillment of the contract. Since this is not the case. A bore the risk.

(d) Delay:

Frequently, we have seen that, delay is caused due to happening of a subsequent event in the performance of contract. Such delay brings financial loss to one of the parties. In commercial transactions, one has to accept the risk of delay. The delay must be such as to render the adventure absolutely nugatory.²⁷ Delay must be such that it puts an end in a commercial sense to the undertaking. On this point, Lord Roskill, in *Pioneer Shipping Ltd. v. B.T.P. Tioxide Ltd.*,²⁸ has provided guidance, “*It is often necessary to wait upon events in order to see whether the delay already suffered and the prospects of further delay from that cause will make any ultimate performance of the relevant contractual obligations ‘radically different’...from that which was undertaken by the contract. But, as has often been said,*

²⁵ (1939) 1 K.B. 132.

²⁶ (1918) 2 K.B. 467.

²⁷ *Bensaude & Co. v. Thames and Mersey Marine Insurance Co.* (1897) 1 Q.B. 29, per Lord Esher at p. 31.

²⁸ (1982) A.C. 724 at p. 752.

businessmen must not be required to await events too long. They are entitled to know where they stand. Whether or not the delay is such as to bring about frustration must be a question to be determined by an informed judgment based upon all the evidence of what has occurred and what is likely thereafter to occur.”

It is for the tribunal to decide whether or not the contract has been frustrated. Even where delay is prima facie sufficient, where both the parties are responsible for it, the rule that reliance cannot be placed on a self-induced frustration will preclude discharge.²⁹

VIII. EFFECTS OF FRUSTRATION

(i) Common Law

(a) Contract generally determined automatically:

Generally the contract is not merely dischargeable at the option of one or other of the parties. The contract is brought to an end forthwith and automatically held in *Hirji Mulji v Cheong Yue Steamship Co. Ltd.*³⁰

(b) Future obligations discharged:

The effect of frustration at common law is to release both parties from any further performance of contract. All obligations falling due for performance after the frustrating event occurred are discharged held in *Appleby v Myers*.³¹

(c) Accrued obligations remain:

Legal rights or obligations already accrued and due, before the frustrating event occurred, are left undisturbed held in *Chandler v Webster*.³²

(ii) Law Reform (Frustrated Contracts) Act, 1943

(a) Underlying principle:

It has been stated that the fundamental principle underlying the Act is prevention of the unjust enrichment of either party to the contract at the other's expense and not the apportionment of the loss caused by the frustrating event between the parties.³³

(b) Expense incurred by payee:

²⁹ Paal Wilson & Co. A/S v. Partenreederei Hannah Blumenthal (1983) 1 A.C. 854.

³⁰ (1926) A.C. 497.

³¹ (1867) L.R. 2 C.P. 651.

³² (1904) 1 K.B. 493.

³³ B.P. Exploration (Libya) Co. Ltd v. Hunt (No. 2) (1979) 1 W.L.R. 783.

This Act gives to the court a discretionary power to allow the payee to set off against the sum so paid or payable a sum not exceeding the value of any expenses which the payee has incurred in or for the purpose of performing the contract before the frustration.³⁴

(c) Arbitration:

There are very few reported decisions on the interpretation of the 1943 Act: most disputes simply concern the amount of each party's liability, and are referred to arbitration.³⁵

IX. DEVELOPMENT OF THE LAW IN INDIA

The Indian contract act was written down in 1872. By that time, *Taylor v. Caldwell*³⁶ case was decided introducing the doctrine of frustration on the grounds of impossibility. The principle that a contract which had become opposed to the law could not be enforced had always existed. The two formed the basis for the following formulation of the principle in the Indian contract act, 1872. Section 56 provides:

56. Agreement to do impossible act – An agreement to do an act impossible in itself is void.

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.

This section provides for three situations. The initial impossibility is that an agreement to do an impossible act is void. It applies to the case where the act was impossible at the time of making of the agreement. The second situation relates to a contract that was lawful when made. However, a subsequent changes in the law or events makes it unlawful to perform the contract. The laws made by the state take precedence over contractual obligations. The third situation is after a contract is made, the changes in the situation make it impossible to perform the contract.

This provision codified the common law principle. However, the difference was this: once the principle became a statutory provision, the Indian courts did not have to introduce the conceptual basis of law. In contrast, the common law courts, based on the system of precedence, could not escape from justifying the principle. The Indian courts had all along

³⁴ *Gamerco S.A. v. I.C.M. / Fair Warning (Agency) Ltd.* (1995) 1 W.L.R. 1226.

³⁵ *Pioneer Shipping Ltd v. B.T.P. Tioxide Ltd.* (1982) A.C. 724.

³⁶ (1863) 3 B. & S.826.

insisted that section 56 has provided a positive law, and thus the Indian courts, unlike the British courts, need not go into intention of the parties. As the Supreme Court noted in *Naihati Jute Mills Limited v. Khyaliram Jagannath*³⁷, “*The necessity of evolving one or the other theory was due to the common law rule that courts have no power to absolve a party to the contract from his obligation. On the one hand, they were anxious to preserve the sanctity of contract while on the other the courts could not shut their eyes to the harshness of the situation in cases where performance became impossible by causes which could not have been foreseen and which beyond the control of the parties. Such a difficulty has, however not to be faced by the courts in this country... so far as the courts in this country are concerned they must look primarily to the law as embodied in section 32 and 56 of the Contract Act.*”

In fact, the common law cases displayed a wide array of approaches and conflicting theories. In no small measure, this made the Indian courts confine themselves to the statutory provisions. The Supreme Court, referring to the common law cases concluded that, “*These differences in the way of formulating legal theories really do not concern us so long as we have a statutory provision contained in the Contract Act. In deciding cases in India, the only doctrine that we have to go by is that of supervening impossibility or illegality as laid down in the section 56 of the Indian Contract Act, 1872 taking the ‘impossible’ in its practical and not literal sense. It must be borne in mind, however, that section 56 lays down a rule of positive law and does not leave the matter to be determined according to the intention of the parties.*”

X. CONCLUSION

Frustration occurs whenever the law recognizes that without default of the either party a contractual obligation has become 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 researcher is of the view that force majeure clauses help the parties to avoid or lessen their obligations in case of happening of a supervening event which is beyond their control. If force majeure clauses is not present in the contract then the concept of frustration of contract as present in the common law and recognized by section 56 of the Indian Contract Act, 1872 would operate to save the parties from any liability because of the non-performance of the contract.

³⁷ AIR 1968 SC 522.