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ADVOCATES AND SOLICITORS

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LIVING WITH COVID-19: The Impact on Commercial Properties

The Covid-19 crisis has not only affected individuals, but has also had a significant impact on all trades, businesses and professions, resulting in complete or partial non-observance and non-performance of work, duties and obligations. In fact, even the Government machinery has to a large extent come to a partial or complete stand still. However, the Government is making efforts to manage the unprecedented tragic situation we face, by issuing orders and directives from time to time, planning and preparing for the revival of the economy and ensuring that basic essentials are made available to the public.

We have received several queries from landlords/lessors and in particular, licensees/ lessees with respect to financial obligations arising from premises they have taken on lease/leave and license under registered agreements/deeds. The queries require an evaluation as to whether the licensees/lessees can legally invoke and/or enforce any term under their agreement/contract for a waiver/discount in license fees/rentals during this lockdown period, in particular the "Force Majeure" clause.

We find that the Covid 19 crisis has caused several hardships to the landlords/licensors as well as to the licensees/lessees resulting in non-observance and non-performance of their respective obligations including respective financial obligations to various third parties.

A. Force Majeure

"**Force Majeure**" literally translates from French as "superior force," but Black's Law Dictionary defines it as "An event or effect that can be neither anticipated nor controlled." A force majeure provides for eventualities in an agreement as a result of which performance of the terms and conditions by a party becomes impossible or impracticable leading to termination or suspension of the agreement and the consequences follow as provided in the agreement.

Most Force Majeure clauses in agreements/contracts in India, provide for occurrences like wars, riots, natural calamities like earthquakes and floods, and such unforeseen events resulting without human intervention, that lead to non-performance of the terms and conditions of the agreement.

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 event as provided for in the agreement.

Most licensees/lessees have been invoking the clause of "Force Majeure" for this lockdown period seeking a waiver and/or discount in the rental/license fees from the landlords/licensors. In some cases, licensors/landlords have voluntarily waived off/discounted the rental/ license fees for the lockdown period.

Whether a party to the agreement can invoke and enforce a "Force Majeure" clause for Covid-19 is questionable and debateable. One needs to review and examine the provisions and terms of the agreement as the applicability would largely depend on the language of the clause and legal interpretation. Parties should review the precise language of the force majeure clause, as the language will determine what events are covered by the clause, the procedure that the parties must follow in order to invoke the clause to excuse its contractual performance and the steps they must take to overcome the Force Majeure event. Whilst reading the clause one needs to be vigilant with reference to certain words like "use and occupation" and "damage", "destruction' caused to the premises.

There may be situations where the expression, "unforeseen event" has been incorporated under the Force Majeure clause, wherein the "unforeseen event" may render performance impossible only during the limited time period during which the unforeseen event is in operation, with the likelihood that the parties can resume normal contractual obligations after the unforeseen event ceases. The present Covid –

19 situation can be treated as an unforeseen event following which, once the situation is under control, the parties can perform their contractual obligations.

The Ministry of Finance, India, in Office Memorandum dated 19th February, 2020, has referred to the expression 'Force Majeure Clause' and stated that the coronavirus should be considered a natural calamity where force majeure may be invoked, wherever considered appropriate, as stated therein. It also provides that a Force Majeure clause does not excuse or release a party from performing its obligations entirely, but only suspends it for the duration of the Force Majeure.

Global private equity investors who are owners of various commercial/IT parks across India have categorically stated that "Force Majeure" is not applicable to their licensees/lessees for 2 (two) main reasons, (i) the premises have not been permanently damaged or destructed and (ii) most of the licensee/ lessees, although not in use and occupation of the premises, have their database servers and equipment, etc. in the premises, which are operational and functional, as a result of which their employees, consultants, etc. can function and work from home.

B. Indian Contract Act, 1872

Section 32 and 56 of the Indian Contract Act, 1872 provides circumstances under which performance of a contract becomes impossible or unlawful. However, judgements of the Court, including the Supreme Court of India, has upheld that section 56 of the Indian Contract Act, 1872 is not applicable to immovable properties, i.e. lease and leave and license agreements. [This Note is limited to agreements/contracts relating to immovable properties, in particular, lease and leave and license agreements.]

For the sake of reference, we have reproduced section 32 and 56 of the Indian Contract Act, 1872 as under:

> ***32. 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.*

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.

Compensation for loss through non-performance of act known to be impossible or unlawful: Where one person has promised to do something which he knew or, with reasonable diligence, might have known, and which the promisee did not know to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-performance of the promise.

There are several judgements relating to sections 32 and 56 of the Indian Contract Act, 1872, which set out the facts under which performance of the contract by a party becomes absolutely impossible and the contract comes to an end automatically from the date of happening of such event. One needs to assess and ascertain if the occurrence of such an event has resulted in the destruction of the main object and purpose of the contract, or has made a significant impact on the obligations of the parties, which had not been anticipated and in the way the contract now stands, far beyond the contemplation of the parties.

In **Sushila Devi vs. Hari Singh AIR (1971) 2 SCC 288**, the matter was relating to a lease of a property, which went to Pakistan after partition. The Supreme Court determined that the impossibility contemplated by Section 56 of the Indian Contract Act, 1872 is not confined to something which is not humanly possible. If the performance, of a contract becomes impracticable or useless with regard to the object and purpose the parties had in view, then it must be held that the performance of the contract has become impossible. The Court observed, holding the lease agreement as frustrated. Furthermore, the Court concluded that a contract is not frustrated merely because the circumstances in which it was made are altered.

The Courts have no general power to absolve a party from the performance of its part of the contract merely because its performance has become onerous on account of an unforeseen turn of events.

In **Raja Dhruv Dev Chand v. Raja Harmohinder Singh AIR 1968 SC 1024**, the three-Judge Bench of Supreme Court held 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.

In a recent judgement, the High Court of Delhi in the matter between **Airports Authority of India Vs Leela Venture Ltd.** on 15th July 2016, has clarified that it is a well settled law that Section 56 of the Indian Contract Act, 1872 is not applicable to leases. It is also a well settled proposition of law that a party to an agreement cannot refuse to perform his obligations under an agreement merely because their performance has become more onerous.

In even assuming Section 56 applies to leases, it cannot be invoked in the case of commercial hardship. Frustration cannot be used as a device to avoid a bad bargain. The contract between the parties was for a period of 30 years and it was all but natural and foreseeable by both parties that there would be various economic turmoils over a period of 30 years. The principle of frustration is not applicable when the event is foreseeable but not foreseen.

The doctrine of frustration embodied in Section 56 of the Indian Contract Act, 1872 which renders a contract void by reason of the impossibility, would not apply in the case of a lease.

Section 56 of the Indian Contract Act, 1872 refers to the stage when the contract becomes impossible or unlawful and frustrated within the meaning of that Act; the contract is thereby discharged.

C. Transfer of Property Act 1882

Sections 108(e) of the Transfer of Property Act, 1882 is a special law and it excludes the general law i.e. Section 56 of the Indian Contract Act, 1872.

Section 108(e) of the Transfer of Property Act does not use the words 'when the contract becomes impossible', but really gives certain instances of it. It begins with certain instances where the lease becomes impossible of further performance and those instances are destruction by 'fire, tempest, flood, violence of an army or of a mob'; and after citing specific instances, it continues to use a rather general clause 'other irresistible force'.

Section 108(e) is based on the principle of frustration of contract, and was enacted to safeguard the rights of the tenant in case of the total destruction of the property leased to him/her. It gives him/her the right to escape his/her liability as a tenant by declaring the lease void. However, if the tenant does not exercise the option under clause (e) that is, does not invoke the doctrine of frustration, the lease shall continue for the benefit of both the parties. It is the general rule that the rent continues to be payable notwithstanding that, in the case of a dwelling-house or flat, it is at the time of letting, or subsequently becomes, unfit for habitation; or in the case of land near the seashore, that it is of no value; or in the case of agricultural land, that it is unsuitable for the intended use; or that the premises are subsequently destroyed by fire, or carried away by a flood, or inundated by fresh water; or destroyed by enemy action; the premises have become useless to the tenant. It would thus appear that in case of the destruction of the leased accommodation, though due to no fault of the landlord, the tenant can avoid payment of rent only if he declares the lease void under Section 108(e) of the Transfer of Property Act, however; if he fails to do so, the lease will subsist for the benefit of both parties and the landlord is entitled to claim rent.

Section 108(e) of the Transfer of Property Act, 1882 refers to "destroyed wholly or rendered substantially and permanently unfit", but Section 56 of the Indian Contract Act, 1872 refers to "an act becoming unlawful or impossible".

Section 108(e) of the Transfer of Property Act, 1882 refers to instances of destruction and damage to the property as a result of which the lessee is unable to use and occupy the property, however, the section does not cover instances/ events as a result of which although the property has not been destructed and/or damaged but the accessibility to the property is restricted (for reasons not attributable to the lessor) and it is completely impossible and impractical for the lessee to use and enjoy the property in terms of the lease deed.

When the parties have entered into commercial contracts with their eyes open, there cannot be a variation to the terms of a concluded contract which has already been acted upon. The parties are estopped from challenging the terms and conditions of the contract. If a person of his own accord accepts or contracts on certain terms and works out the contract, he cannot be allowed to adhere to and abide by some of the terms of the contract which proved advantageous to him and repudiate the other terms of the same contract which might be disadvantageous to him. In **State Bank of Haryana v. Jage Ram (1980) 3 SCC 599** the Supreme Court held that the Licensee cannot challenge the terms of the licence on the ground that he is finding it commercially inexpedient to conduct his business. In **C.J. International Hotels Ltd. v. N.D.M.C.,**

AIR 2001 Del 435, this Court held that the licensee cannot challenge the conditions of the licence if he finds it commercially unviable to conduct his business.

Assuming that Section 56 of the Indian Contract Act, 1872 is applicable to a lease, a lessee would be required to surrender the leased property and settle all liabilities including financial obligations upto the date of surrender under section 65 of the Indian Contract Act, 1872 if the lease is deemed to be frustrated and void, assuming the improbable applicability of section 56 of the Indian Contract Act 1872 on leases.

Conclusion

In view of the law and the aforementioned judgements, as it stands today, it is well settled that Section 56 of the Indian Contract, 1872 would not apply to leases and leave and license agreements for immovable properties.

In the situation we face, a crucial aspect which could lead to disputes or concerns would be with respect to entities/establishments, which are licensees/lessees, covered under the category of "essential services". These services/industries are permitted to remain operational and functional during this crisis, however some entities do not have the minimum/ requisite manpower/resources to operate and conduct their business and function and hence, unable to pay and/or fulfil their financial obligations with the landlords/ licensors.

As explained, one needs to carefully examine and review all the terms and conditions of the agreement/deed, since, both the landlords/licensors as well as the licensees/lessees are required to abide and comply with the rules and regulations of the Government during this crisis, which is an unprecedented event beyond the control of both the parties. It is not a voluntary act on the part of the licensee/lessee to close their premises, but they are mandatorily required to do so as per the directives of the Government.

In the given circumstances, both parties need to re-evaluate their commercials in the interest of their respective businesses and try to resolve the dispute amicably to the best extent possible, renegotiate and avoid litigation, which could be a costly and time consuming process.

We at ALMT Legal will be happy to guide you during these challenging times. Should you need any assistance, please write to us at **litmumbai@almtlegal.com.**

Disclaimers:

a) *Our views expressed herein are based on limited details, information and facts available with us with respect to commercial properties. Our views may differ depending on the facts and circumstances of each case.*

b) *Our views are based on our personal interpretation of the applicable Indian laws and regulations and no assurance is given that Courts or regulators in India will agree with the same.*

c) *Other than as expressly stated herein, we express no view on any other related or other issue.*

d) This Note should not be transmitted to anyone else nor is it to be relied upon by anyone else or for any other purposes or quoted or referred to in any public document or filed with anyone without our express prior written consent.