

Construction Contracts and Force Majeure Events

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Abstract:

The growth of Construction and Infrastructures sector has seen its all-time high in the recent years and has immensely contributed towards overall growth and development of country in terms of its GDP and pushing its progression towards a developed nation in the near future. With such streamlined developmental goals and financing to back up the same, India has witnessed a smooth yet fast transition towards development of construction and infrastructure projects through engagement of best in-class practices and techniques to enhance the quality standards and pace of development.

In the recent years, the construction sector has basically fumbled upon the intricacies and developments relating to force majeure clauses that have played a significant role, owing to the sudden outbreak of COVID-19 and its aftermath. With a sudden stop of the overall economy, the contractors, stakeholders and concessionaires working in the construction sector were greatly hit to be able to conquer and recover from the losses incurred by them during such corona outbreak. The force majeure clause with the contracts/agreements played a vital role in safeguarding and recovering losses incurred during the pandemic era, and also opened floodgates of legal issues and intricacies pertaining to its interpretation in the post-pandemic years.

All of such challenges, also forced a dilemma with the Government to enhance and develop the force majeure clause within the construction contracts/agreements to be able to tackle similar situation if faced in the future.

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Introduction

India's construction and infrastructure sector accounts for almost 9% of the total FDI inflow and contributes majorly to the country's Gross Domestic Product (GDP). As per the press release dated July 28, 2022, published by the Ministry of Commerce and Industry, the construction sector occupied one of the top five slots with 5.52% of the FDI equity inflow during FY 2021 – 22.¹

In fact, the sector's importance has been realized and recognized in the Union Budget 2023-24, where investment in infrastructure occupied a significant position among the seven priorities laid down by the Hon'ble Minister of Finance. In line with such a vital stand in the country, any dispute obstructing the construction of a structure/building relevant to the public domain may be considered to be against the public interest.

In recent years, a popular reason for these construction sector disputes/conflicts causing factors were natural and man-made calamities and adversities, wherein, the latest were a series of flash floods which plagued North and North Eastern regions of the country and were caused by rising water levels from unprecedented rains. Owing to these floods, there were many reports of destruction of buildings, bridges, highways, and other infrastructural landmarks.

In addition to acting as a wake-up call for inculcating sustainable values to prevent global warming, this calamity also worked in forcing the Concessionaires and Authorities to revisit their construction contracts towards strengthening their rights and liabilities, while simultaneously preventing the loss of public revenue.

Force Majeure Clauses and Natural Disasters

Delays and destructions caused in the construction sector due to natural calamities are often covered by the Force Majeure clauses of contracts. Force Majeure events are those which are unprecedented and unforeseeable by both the parties to a contract, and cannot be avoided despite taking reasonable care or caution, and are henceforth, not attributable to any party's default and cannot be controlled thereof. In common parlance, a Force Majeure clause is invoked when an extraordinary event occurs that is beyond human intervention. Often also referred to as 'acts of god', these events are understood as unforeseen, uncontrollable instances which can have several adverse impacts ranging from a simple delay to a completely weakened possibility of project completion.

As per the official notification dated February 19, 2020, passed by the Government of India, Force Majeure events have been defined to include "*extraordinary events or circumstance beyond human control*" such as an event described as an act of God (like a natural calamity) or events such as a war, strike, riots, crimes, that explicitly does not include negligence or wrongdoing, predictable/ seasonal rain and any other events specifically excluded within the provided Force Majeure clause or agreement.

A Force Majeure clause in the contract absolves both parties to a contract from contractual liability or obligation provided therein. This ensures that both parties, who are unwillingly prevented from fulfilling their part of the contract due to the occurrence of an unforeseen or

¹ "Singapore (27.01%), USA (17.94%), Mauritius (15.98%), Netherland (7.86%) and Switzerland (7.31%) emerge as top 5 countries for FDI equity inflows into India FY 2021-22", July 28, 2023, PIB Delhi, <https://pib.gov.in/PressReleasePage.aspx?PRID=1845719>.

inevitable incident/event are absolved from their liability under the contract. However, a Force Majeure clause usually does not excuse a party's non-performance entirely but only suspends it for the duration of occurrence of such an unforeseen event.

One of the basic essential/preliminary conditions to claim and absolve liability by invoking a Force Majeure clause is by serving a notice, stating the occurrence of such an inevitable incident, to the other party. It is pertinent to intimate the event to the other party as soon as the event occurs, as the process for an ex-post facto claim may become much more complicated if claimed otherwise. This step is necessary to ensure and maintain effectual and timely communication and is seen as an elementary yet principal step towards continued association, project development and claim management in the future.

In many instances, there may be a Force Majeure situation affecting only one side/party to a contract such as the purchase organisation. In such a situation, the purchase organisation is to communicate with the supplier along similar lines as above for further necessary action. If the performance in whole or in part or any obligation under this contract is prevented or delayed by any reason of occurrence of Force Majeure event “for a period exceeding 90 (Ninety) days, either party may at its option terminate the contract without any financial repercussion on either side.”²

In the case of ***Energy Watchdog vs. Central Electricity Regulatory Commission & Ors.***³, the Hon’ble Supreme Court observed that,

“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.

It has also been held that applying the doctrine of frustration must always be within narrow limits.”

Subsequently, in the case of ***MEP Infrastructure Developers vs. South Delhi Municipal Corporation & Ors.***⁴, the Hon’ble High Court of Delhi, had observed that,

“It is the settled position in law that a Force Majeure clause is to be interpreted narrowly and not broadly. Parties ought to be compelled to adhere to contractual terms and conditions and excusing non-performance would be only in exceptional situations. As observed in Energy Watchdog (supra) it is not in the domain of Courts to absolve parties from performing their part of the contract. It is also not the duty of Courts to provide a shelter for justifying non-performance. There has to be a “real reason” and a “real justification” that the Court would consider to invoke a Force Majeure clause”.

According to the contemporary idea, a Force Majeure clause has always formed an essential part of any construction contract. Even though its importance has only increased over the years, there has been a drastic evolution as to how and where these clauses are inserted and how are they exercised in accordance with the reformed legalities in present times. As per the current

²Force Majeure, Department of Expenditure <https://doe.gov.in/sites/default/files/Force%20Majeure%20Clause-%20FMC%20.pdf> (last visited Oct 10, 2023).

³ Energy Watchdog v. Central Electricity Regulatory Commission and Ors., (2017) 14 SCC 80.

⁴ MEP Infrastructure Developers v. South Delhi Municipal Corporation & Ors., W.P. (C) 2241/2020 before the High Court of Delhi.

scenario, the Force Majeure clause has been increasingly used to dissolve the entire liability/obligation of one or both parties to a contract rather than delaying and postponing one's duty/obligation, depending upon individual circumstances of different construction disputes.

In the post-COVID era, Force Majeure clauses were majorly invoked to dissolve the complete liability of parties due to the impossibility of completing the project on time. However, there has been a greater debate to understand circumstances/events where the Force Majeure clause can be used to absolve complete liability as opposed to cases where obligation/timeline is further pushed or allowed to permit delay in the execution of construction projects, owing to no penalty at all.

The significance and relevance of Force Majeure clauses in contractual arrangements were recognized by parties and stakeholders of the construction industry, majorly in the post-COVID era. In line with such confusion and the possibility of delivering obligations in the pandemic era becoming debatable, the Government of India gave effectual refuge to the stakeholders through acceptance and relevance of the Force Majeure clause used within the curated contractual arrangements. Subsequently, as an immediate relief to the Indian citizens towards stopping businesses around the world, many official notifications were issued by the Indian Government towards accepting and relieving liability owing to the Force Majeure events and acceptance of COVID as one of the factors that can be used to invoke Force Majeure clause in contractual arrangements.

The Ministry of Finance, via a notification dated 19th February 2020, exclusively accepted and notified 'coronavirus' as a Force Majeure event and included it within the definition of a 'natural calamity', stating that the clause can be invoked by following the 'due process of law'. In pursuance of the official notification, many other reliefs were granted especially to contractors, including that of 'extension of time and concession period with no cost'⁵.

The Delhi Court through its judgment in *M/s Halliburton Offshore Services Inc vs Vedanta Limited*⁶ stated that "The countrywide lockdown, which came into place on 24th March 2020 was, in my opinion, prima facie in the nature of Force Majeure. Such a lockdown is unprecedented, and was incapable of having been predicted either by the respondent or by the petitioner" and successfully granted injunction regarding invocation or encashment of eight bank guarantees owing to the outbreak of the pandemic.

The Hon'ble Supreme Court of India and various High Courts, while deciding and dealing with the extent of liability of contractors and concessionaires in various construction projects have also relied on and referenced the notifications issued by the National Highways Authority of India and Ministry of Roads, Transport and Highways (hereinafter referred to as "MoRTH"). To decide the extent of applicability of Force Majeure clauses in the post-pandemic era, regarding construction contractual arrangements, the Courts and Tribunals across the Nation, have increasingly relied on MoRTH circulars as precedents to extend necessary relief to road sector Companies and Concessionaires about the penalties on submission of bank

⁵ *Force Majeure*, Department of Expenditure, <https://doe.gov.in/sites/default/files/Force%20Majeure%20Clause-%20FMC%20.pdf> (last visited Oct 10, 2023).

⁶ *M/s Halliburton Offshore Services Inc v. Vedanta Limited*, 2020 SCC OnLine Del 542.

guarantees/performance guarantees, extension of time for completion, financial closures as well as for other similar benefits.

Compensation under the Force Majeure Clauses

The term 'Force Majeure' has been adopted from French law and had a limited scope of interpretation based on its usage within different civil law jurisdictions. Additionally, the legal concept of Force Majeure has been adopted by different countries in different forms according to the requirements and applicable legislations of their civil law. However, with the advent of the pandemic, the Force Majeure clause within the English law is progressively being interpreted more liberally to be able to provide compensation towards financial losses suffered by stakeholders during the COVID-19 times. English laws were flexible to the degree of allowing parties to invoke Force Majeure clauses regardless of contractual provisions/agreements.

Besides sudden changes in laws and regulations, delayed authority approvals, labour and workforce restrictions and supply chain disruptions, the stakeholders in the construction sector struggled with huge financial losses. The main concern that arose in the post-COVID times was the dilemma of recovering the financial losses incurred by contractors/stakeholders owing to the sudden closing of the economy despite the employment of labour and machinery to project sites. The courts were flooded with claims owing to the financial losses incurred and their timely resolution that further obstructed financial supply chains.

Within the English law, "Properly drafted, a Force Majeure clause governed by English Law should provide a sophisticated mechanism for dealing with the consequences of exceptional events that are beyond the control of the Parties" and will henceforth, help the Courts to interpret and understand the applicability of the phrased Force Majeure clauses in individual circumstances. The Court stated that due to evident 'ambiguity', every case would be decided based on individual phrasing and wording of Force Majeure clauses to understand the rights and obligations of parties within the defined Force Majeure clauses.

Invoking Force Majeure Clauses under FIDIC Conditions of Contract

Due to the inevitability of COVID-19, the majority of financial claims in the Court were made within Clause 19 of the Rainbow FIDIC suite of Contract, 1999 edition. The essentials to ascertain a Force Majeure event is considered when an event satisfies five conditions namely, "(a) an exceptional event or circumstance; (b) beyond the Party who has been affected by it; (c) against which such affected Party could not have reasonably provided against before entering into the Contract; (d) which having arisen such affected Party could not reasonably have avoided or overcome; and (e) it must not have been substantially attributable to the other Party".

Flash Floods and Force Majeure – A Need for Rethinking the Clause

It may be relevant to note that while the pandemic catalysed the publication of various circulars which sought to provide relief to the Concessionaires, the recent flash floods are yet to be compensated on these terms. Such compensation may, however, be considered to be necessary because while in the case of the former disaster, the construction was halted and not disturbed, the damage caused by the floods may have reversed the construction progress altogether. Even though the duration of the latter calamity may not have exceeded 90 days, the damage caused

and loss incurred may be greater than that in the pandemic, which further provides a need for an amendment to the definition. Henceforth, a mere perusal of the notifications and judgments may give a reasonable inference that while events like flash floods may not provide concessionaires with the option to terminate the contracts, pandemic-like situations, on the other hand, may render such reliefs.

Additionally, it is also relevant to note the ambiguity and acceptance of a certain event within the definition of 'Force Majeure event' or 'natural calamity' as prescribed within the Indian Contract Act, 1872. There is an immediate need to reform preliminary Force Majeure clauses included within the contractual arrangements of construction contracts, to safeguard and provide better clarity to the contractors, concessionaires and developers of any construction contract, whether in the private or public sector. There is an equal need to ensure effectual remedy and compensation to address the financial claims of contractors/stakeholders suffered during the COVID-19 times and to establish a definite mechanism to tackle and grant such claims at the earliest.