

Impact of the Movement Control Order on Contracts for Private Sectors Specifically on Timelines

The implementation of the Movement Control Order (“MCO”) since 18th March 2020 has created uncertainties with regard to the compliance of timelines for contracts. Whilst some contracts contain provisions such as the *force majeure* clause which allows the postponement or suspension of the obligations during the MCO, other contracts may not have envisaged such a circumstance.

What happens then, if your contract does not have a specific clause to address a MCO-type situation? The Frequently Asked Questions (FAQs) below may have given you the answers.

FAQ (1): What happens to contracts during MCO?

First and foremost, you will need to check if your contract contains provisions for the postponement or suspension of your contractual obligations, such as a *force majeure* clause.

“*Force majeure*” does not on its own carry a specific legal definition. It merely refers to an event that is beyond the control of the contracting parties. Contracts which address *force majeure* events would usually define a “*force majeure*”.

As such, if there is such clause in your contract, proceed to check whether the definition of “*force majeure*” includes the postponement or suspension of obligations due to pandemic / epidemic, quarantine restrictions or other public health restrictions or advisories or a catch all provision such as by the acts, restrictions, regulations, by-laws, prohibition or measure of any kind on the part of any governmental, parliamentary or local authority. There are commonly used terms in Malaysia that limit *force majeure* events to “man-made” calamities such as, wars or riots.

If the *force majeure* clause is sufficient to capture the MCO or the Covid-19 pandemic, then the time for performance of obligations for the parties concerned shall be extended to the extent that parties to the contract are prohibited to perform their respective obligations.

FAQ (2): What if your contract does not have a provision such as a *Force Majeure* clause?

If your contract does not contain a *force majeure* clause, either party to the contract may invoke the doctrine of frustration to terminate the contract. The Federal Court in **Goh Yew Chew & Anor v. Soh Kian Tee [1969] 1 MLJ 138** explained what amounts to frustration:

*“The doctrine of frustration is relevant when it is alleged that **a change of circumstances after the formation of the contract renders it physically or commercially impossible to fulfil the contract.** The doctrine is not concerned with initial impossibility to fulfil the contract. The doctrine is not concerned with initial impossibility which renders a contract void ab initio, as where a party to a contract undertakes to perform an act which, at the time the contract is made, is physically impossible according to existing scientific knowledge and achievement.” [our emphasis]*

Section 57 of the Contracts Act 1950 (“CA”) provides that:

- “(1) An agreement to do an act impossible in itself is void.*
- (2) 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.”*

What then amounts to frustration? This was explained by the Court of Appeal in **Guan Aik Moh (KL) Sdn Bhd & Anor v Selangor Properties Bhd [2007] 4 MLJ 201** that there are 3 main elements:

- (a) the event must have been one which was not provided for (in other words predicted by) the contract;
- (b) the event that occurred must not have been caused by either party. Self-induced frustration is not allowed; and
- (c) the event which is said to discharge the contractual obligation must be such that renders it radically different from that which was undertaken by the contract.

The courts must find it practically unjust to enforce the original promise. If either of these three elements is missing, section 57 of the CA will not apply.

To demonstrate this, we may look at the case of **Keshore A/L Anupchad Metha & Anor v Abrar Finance Berhad & Anor [2002] MLJU 565** where the court took judicial notice and held that the tenancy agreement was frustrated in view of the Central Bank of Malaysia (BNM)’s directive for the 1st defendant to merge and consolidate with the 2nd defendant, which resulted in the first defendant surrendering its business licence to BNM. The 1st defendant was thus unable to operate at the premises thereby frustrating the performance of the tenancy agreement.

It can be seen from the case of **Abrar Finance Berhad** that courts are prepared to consider the doctrine of frustration as a defence if it involves the implementation of a governmental policy. If the performance of a contract is affected by the MCO, the courts are likely to accept the discharge of that contract by frustration, provided that the 3 elements set out in **Guan Aik Moh (KL) Sdn Bhd** are satisfied.

Whether the MCO gives rise to a frustration of a contract is largely dependent on the facts of each individual case. As such, parties should exercise caution when looking to terminate a contract based on the doctrine of frustration.

FAQ (3): What are the consequences if I terminate a contract based on frustration?

When a contract is discharged by frustration, the contract becomes void. Section 66 of the CA provides for restitutionary remedies:

“When an agreement is discovered to be void, or when a contract becomes void, any person who has received any advantage under the agreement or contract is bound to restore it, or to make compensation for it, to the person from whom he received it.”

Simply put, the party who received an advantage or benefit in the course of the contract must either compensate the losses suffered by the aggrieved party or the restore the same.

One must not forget that when a contract is discharged by frustration, Section 15 of the Civil Law Act 1956 (“CLA”) also applies. It is pertinent to note that Section 15(2) of the CLA clearly sets out that¹:

- (a) prior to frustration, all sums paid by one party to the other shall be recoverable from that party;
- (b) prior to frustration, the sums that are to be paid by one party to the other need no longer be paid; and
- (c) prior to frustration, when a party to whom money has been paid and has incurred expenses for the purpose of the performance of the contract, the Court may allow that party to retain or recover the whole or any part of the sums so paid.

Section 16 of the CLA provides for the application of Section 15.

FAQ (4): What are the good practices for businesses affected by MCO?

To ensure that your business faces minimum interruption from the MCO, below are good practices / measures to be taken:

- (i) Check your contract for provision(s) concerning extension of time and *force majeure* to ensure that your business and its interests are well protected.
- (ii) Make sure that the requirements / pre-conditions are satisfied e.g. service of notice before an extension of time can be granted or prior to invoking the *force majeure* clause.

¹ Extract from the case of *Hong Leong Bank Berhad (dipinda dari EON Bank Berhad kepada Hong Leong Bank Berhad menurut Perintah Letakhak Mahkamah Tinggi di bawah Saman Pemula No: 24(NCC)-175-2011 bertarikh 17.6.2011 bahawa kesemua cagaran, akaun pelanggan dan perniagaan perbankan EON Bank Berhad ditukar kepada Hong Leong Bank Berhad) v Tan Siew Nam & Anor [2014] MLJU 393*

- (iii) Assess the situations surrounding your business before invoking the *force majeure* clause e.g. whether mitigating steps can be practically taken in respect of the contract or a task force can be set up to carry out risk management measures.
- (iv) If mitigation is not possible, write to your counterparty before the breach occurs so that you have a window for an opportunity to seek a remedy in court before the counterparty declares or acts on a breach.
- (v) Proceed to renegotiate or vary the terms concerned with your counterparty.
- (vi) In the event that termination is imminent or the contract has been terminated, proceed to assess the consequences of termination e.g. damages, compensation, losses which you are exposed to.

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*This article is for general information only and should not be relied upon as legal advice. The position stated herein is as at the date of publication on 26th March 2020. For any enquiries on this article, please contact **Tan Min Lee** (minlee@ganlaw.my).*