

Chapter 10

DISCHARGE OF CONTRACTS

A contract may be discharged by performance, agreement, breach or frustration. Each of these is now examined in turn.

10.1 PERFORMANCE**10.1.1 INTRODUCTION**

The performance of his obligations by a contracting party discharges that party from his obligations under the contract. This is the normal method of discharge.

Partial or incorrect performance will not, therefore, suffice. For example, in contracts for the sale of goods, s. 13 Sale of Goods Act 1979 imposes the condition that the goods must correspond with the description, such that, if the seller delivers less or even more goods than he contracts to sell, the buyer is entitled to reject the goods. The classic example of hardship caused by this rule is the case of *Cutter v Powell* (1795) 101 ER 573. A seaman who was to be paid his wages at the end of a voyage died just a few days away from port. His widow was not entitled to recover even the proportion of his wages representing her husband's days at sea, because the husband had failed to perform properly, or completely, his side of the bargain.

10.1.2 MODIFICATION OF THE GENERAL RULE**(a) Divisible Contracts**

A contract may be *entire*, where the agreement provides that complete performance by one party is a *condition precedent* to contractual liability on the part of the other party; or, *partial*, where the contract provides for performance by instalments, with separate payment for each of them. A classic example is in the building trade, where a builder agrees to build a house for £40,000, with £15,000 to be paid on completion of the foundations, £15,000 on erection of the superstructure, and £10,000 six months after completion of the house, in accordance with the specifications. If the buyer failed to do any further work after the foundations are laid, he would still be entitled to recover £15,000.

(b) Acceptance of Partial Performance

Where the party to whom the promise of performance was made, B, *accepts* partial performance of the contract by A, he must pay A for the goods he has accepted or the benefit of which he has received. However, B must have *voluntarily* accepted A's partial performance (cf. *Sumpter v Hedges* [1898] 1 QB 673, where the owner of half-built stables was held not to have had any choice but to finish the building work).

(c) Completion of Performance Prevented by the Promisee

Where full and complete performance of the contract is prevented through the other party's actions, the party unable to complete performance may claim for partial or substantial performance. In *Planché v Colburn* (1831) 8 Bing 14, an author succeeded in recovering half his commission on a book he had half completed, after the publisher prematurely terminated the contract.

(d) **Substantial Performance**

The principle of substantial performance is based on the premise that where there are minor variations from the terms of the contract, the other party cannot void the contract, but must instead rely on a remedy in damages. For example, if a building contractor has completed the essential work, but leaves minor work outstanding, he may claim the contract price, less a deduction for the latter. *Hoening v Isaacs* [1952] 2 All ER 176 illustrates how substantial performance permits enforcement of the contract. In this case, the defendant employed the claimant to decorate and furnish a flat, at a fixed cost of £750. Although the work was completed, there were some defects, which would cost £55 to fix. The defendant moved into the flat, but refused to pay the balance outstanding under the contract. The contract provided for payment of "net cash as the work proceeds and balance on completion", so that the defendant had already paid £350 and the claimant sought to recover the remaining £400. The Court of Appeal held that substantial performance had been completed, and that the claimant would be allowed to recover the contract price, minus the repair costs.

In *Re Moore & Co and Landauer & Co* [1921] 2 KB 519, however, when 3,000 tins of canned fruit were delivered in substantial performance of the contract, packed in cases of 24 tins, when they were supposed to be packed in cases of 30 tins, the defendants were entitled to reject the whole consignment, because the seller had not discharged his obligations under the contract.

10.2 AGREEMENT

Where a contract is formed by agreement, it may also be discharged or terminated through agreement, subject to the conditions of the contract. The agreement to extinguish or terminate the contract itself becomes a binding contract if supported by consideration or made under seal.

10.2.1 BILATERAL DISCHARGE

The contract will be mutually discharged where the parties agree to release one another from any further obligations existing from the original contract. The contract is discharged despite the parties failing to fully or partially discharge all their obligations.

10.2.2 ACCORD AND SATISFACTION

Accord and satisfaction occurs where one party accords the release of another party, who is in breach of the original agreement, from its obligations in return for the satisfaction for the performance of another obligation.

10.2.3 UNILATERAL DISCHARGE

Unilateral discharge occurs where one party has completed its part of the bargain and agrees to release the other party from its outstanding obligations under the contract. The agreement is only binding if supported by consideration or made under seal.

10.3 DISCHARGE BY BREACH

Any breach of contract entitles the injured party to claim damages. The degree of breach and the consequences vary according to the type and nature of the term concerned. There are two types of breach: actual and anticipatory.

10.3.1 ACTUAL BREACH

One party may breach one or more of the terms of the contract in such a way that it amounts to a breach of the contract.

10.3.2 ANTICIPATORY BREACH

An anticipatory breach occurs where a contracting party indicates by express words or by implication through conduct *before* performance that he will not honour his contractual obligations.

This breach immediately gives rise to an action for breach of contract by the innocent party. Thus, in *Hochster v De La Tour* (1853) 2 E&B 678, the claimant was engaged to start work on the 1st of June as a travelling courier. A few weeks before the start date, however, he was informed that his services were not required. The court held that the claimant was not obliged to wait until the 1st of June before bringing a claim for damages.

(i) *The 'Innocent' Party's Options*

If the 'innocent' party fails to accept repudiation within a reasonable time, the contract remains open for the benefit and risk of both parties. The 'innocent' party is not obliged to terminate after the 'guilty' party's anticipatory breach. The innocent party may elect to do one of two things: (1) affirm the contract and demand that the unwilling party actually perform when the due date arrives; or (2) he may terminate the contract.

(ii) *The Claimant's Affirmation*

If the 'innocent' party affirms the contract but the 'guilty' party still refuses to perform his side of the bargain by the due date of performance, the 'innocent' party's right to accept the breach at that later date is not lost. Alternatively, even though the 'guilty' party has made it obvious that he no longer intends to be bound by the contract, the innocent party may continue performing his side of the bargain if he affirms the contract; *White and Carter (Councils) Ltd v McGregor* [1962] AC 413. There are two exceptions to the *Carter* rule:

- (1) where the contract involves joint rather than individual performance, A cannot compel B to perform just because A wishes to continue with the contract; and
- (2) where A can demonstrate that he has no legitimate interest in performing despite B's breach, he cannot enforce upon B the added burden attendant with his performance. This is because the latter exception to the rule in *Carter* lies in C's *wholly unreasonable* behaviour in continuing with his side of the contract.

(iii) *The Claimant's Acceptance of D's Breach*

If C elects to terminate the contract, rather than affirming it, he must follow two courses of action: (1) communicate his acceptance of the 'guilty' party's breach to that 'guilty' party by either unequivocal words or unequivocal actions; and (2) he must not subsequently act in a manner inconsistent with having accepted the 'guilty' party's breach.

10.4 FRUSTRATION

A contract is said to be frustrated where the conditions of the contract can no longer be performed, due to a change in circumstances not provided for in the contract, which occurs after the contract was concluded, and which was beyond the fault of the parties to the contract. Where it is impossible to perform the contract, the court will hold that the obligations of the parties are extinguished from the time that the contract became frustrated.

Frustration is not the same as initial impossibility, which may render the contract void from commencement (*ab initio*) on the grounds of mistake.

10.4.1 EXAMPLES OF FRUSTRATION

(a) Destruction of the Specific Object Essential for Performance of the Contract

In *Taylor v Caldwell* (1863) 3 B & S 826, Caldwell let a music hall to Taylor, so that four concerts could be held there, but the hall was destroyed by fire before the date of the first concert. The court held that Caldwell could not be held liable for breach of contract, since the destruction of the subject matter rendered the contract impossible to perform. Total destruction of the goods in question is not a prerequisite; mere destruction of the merchantable quality of the goods is sufficient (*Asfar v Blundell* [1896] 1 QB 123).

(b) Personal Incapacity to Perform a Contract of Personal Service

Personal incapacity, where the personality of one of the parties is significant, may frustrate the contract: *Condor v The Baron Knights* [1966] 1 WLR 87. In that case, 16-year old Condor was contracted to play as a drummer in a pop group, seven nights a week when work was available. His doctor later advised him that he could only work safely four nights a week, whereupon the group terminated his contract. The court held that Condor's contract of employment had been frustrated in a commercial sense, as it was impracticable (double rehearsals, etc.) to engage a stand-in for the three nights a week when Condor could not work. A contract of personal service, the court held, is based on the assumption that the employee's health will enable him to perform his duties. Personal incapacity of the employee will, therefore, frustrate his employment contract.

(c) The Non-occurrence of a Specified Event

The non-occurrence of a specified event may frustrate the contract. So, where a room was rented for a specific event, even though the contract made no reference to the use of the room for the specified event, the contract will be frustrated if that event does not take place (*Krell v Henry* [1903] 2 KB 740). By contrast, where there is more than one object of the contract, the contract will not be frustrated: *Herne Bay Steamboat Co v Hutton* [1903] 2 KB 683. Here, a steamboat was hired for two days, to take passengers cruising around the royal fleet and to see the naval review, on the occasion of the King's coronation. Although the review was cancelled owing to the King's illness, the naval review was not the only event upon which the intended use of the boat was dependent. The second object of the contract remained, viz. to cruise round the fleet. Therefore, the court awarded the owner of the steamboat the agreed hire charge, less what he had earned from the normal use of the boat over the two-day period. In cases of partial impossibility, a contract can be discharged if its *main purpose* can no longer be achieved; however, in cases of frustration of purpose, the courts have applied the more stringent test of inquiring whether *any part* of the contractual purpose, other than a part which was wholly trivial, could still be achieved: if so, the contract will not be discharged.

(d) Interruption which Prevents Performance of the Contract in the form Intended by the Parties

Inordinate and unexpected delay may frustrate a contract. The problem is to establish how long a party must wait before the delay can be said to be frustrating. *Jackson v Union Marine Insurance* (1873) LR 10 CP 125 made it clear that the interruption had to detract from the agreed duration of the contract, *to such an extent* as to alter the fundamental nature of the contract. In that case, a ship chartered to load a cargo of iron rails for carriage from Wales to San Francisco underwent extensive repairs, whereupon the US charterers

repudiated the contract. The delay was held to be so long as to put an end, in a commercial sense, to the commercial speculation entered into by the ship owner and the charterers. Whilst danger and accidents of navigation had been expressly accepted by the parties, these were not intended to cover an accident causing such extensive damage and the contract would, thus, be considered frustrated.

10.4.2 LIMITATIONS OF THE DOCTRINE

“The doctrine of frustration must be applied within very narrow limits”, per Viscount Simmonds in *Tsakiroglou & Co Ltd v Noblee Thorl GmbH* [1962] AC 93. It is “not lightly to be invoked to relieve contracting parties of the normal consequences of imprudent commercial bargains”, per Lord Roskill in *Shipping Ltd v BTP Tioxide Ltd (The Nema)* [1982] AC 724.

The doctrine is subject to a number of important limitations, including:

10.4.2.1 Express Provision for Frustration

The doctrine is inapplicable where an express contractual provision deals with the frustrating event.

10.4.2.2 Mere Increase in Expense or Loss of Profit

In *Davis Contractors v Fareham UDC* [1956] AC 696, Davis Contractors agreed to build 78 houses in eight months, at a fixed price. Bad weather and labour shortages meant that the work took 22 months and cost £17,000 more than expected. The builders argued that the unforeseen shortages frustrated the contract and that they were entitled to recover the £17,000, on a *quantum meruit* basis. The court held that the fact of unforeseen events, including mere hardship, loss or inconvenience, which made a contract more onerous than was anticipated, did not frustrate it.

10.4.2.3 Alternative Mode of Performance Still Possible

The same conclusion was reached in *Tsakiroglou & Co Ltd v Noblee Thorl GmbH* [1962] AC 93 (*supra*). In that case, Tsakiroglou agreed to sell groundnuts to Noblee, to be shipped from the Red Sea coast to Hamburg. The closure of the Suez Canal made it impossible to ship the cargo in this manner, and Tsakiroglou argued that the alternative route for shipment via the Cape of Good Hope would make the contract “commercially and fundamentally” different, and was therefore frustrated. The court disagreed, holding that the change in circumstances was not fundamental; there was no implied term that the shipment should be via Suez and nor would the nuts have deteriorated on the longer journey. The alternative method of performance could, and should, have been used, and the contract was not, therefore, held to have been frustrated.

10.4.2.4 Government Intervention

A contract may be frustrated by government intervention, such as where governmental declaration of war against another nation renders one of the parties to the contract an enemy alien. In such a case, the contract will be frustrated; see *Fibrosa Spolka Ackyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32. Governmental requisitioning of property can have a similar effect, such as in *Metropolitan Water Board v Dick Kerr* [1918] AC 119, where a contract for a reservoir’s construction was frustrated during the First World War when the Minister of Munitions demanded that the defendant must stop work and liquidate the assets.

10.4.2.5 EFFECTS OF FRUSTRATION

Frustration discharges the contract automatically. There is no election by either of the parties to treat the contract alive by affirming it, as in the case of a breach of contract (see above).

The Law Reform (Frustrated Contracts) Act 1943 was passed to provide for a just apportionment of losses where a contract is discharged by frustration. However, the parties to a contract can contract out of the provisions of the Act. Moreover, the Act does not apply where wholly performed contractual obligations can be severed from those affected by the frustrating event. Its main provisions are as follows:

(a) Recovery of Money Paid

Section 1(2) of the Act sets down the following rules:

- all money still owed ceases to be due;
- money paid before the frustrating event is recoverable; and
- the court has discretion to award expenses to a party which has incurred expenses before discharge in relation to performing the contract, up to the limit of the amount payable before the frustrating event, on the basis of losses 'lying where they fall'.

Section 1(2): The principal effect of the subsection is to: (i) entitle a person to recover money paid under a contract prior to the frustrating event; (ii) remove any obligation to pay money that existed prior to the frustrating event; and (iii) entitle a payee to set off against the sums so paid, expenses which he has incurred prior to the discharge in the performance of the contract.

The case of *Gamerco SA v ICM/Fair Warning Ltd* [1995] 1 WLR 1226 illustrates the section in operation. A contract was in place to promote a "Guns N' Roses" concert; however, when the Spanish government decided to close the stadium where it was supposed to take place, the contract was frustrated. The claimant had paid over \$400,000 to the defendant before the stadium's closure and pursued the defendant for recovery under s. 1(2). Meanwhile, the defendant had sustained costs of approximately \$50,000 in outlays and argued that it should be allowed to keep this amount. It was held that, to do justice under the section, the full amount (\$400,000) would have to be returned, without deduction for the defendant's expenses.

(b) Valuable Benefit

Section 1(3) provides that, if one party has, by reason of anything done by the other party in performance of the contract, obtained a *valuable benefit*, other than payment of money, before the frustrating event (e.g. if one party has delivered to the other some of the goods to be supplied under the contract), he may be ordered to pay a sum in respect of it, if the court considers it just, having regard to all the circumstances of the case.

In *BP Exploration Co (Libya) Ltd v Hunt (No 2)* [1982] 2 WLR 253, the defendant had entered into an agreement with the claimant to share a concession he had been granted from the Libyan government to explore for and extract oil in Libya. The Libyan government subsequently nationalised the industry, causing a significant loss to the claimant, whilst the defendant was compensated by the Libyan government for the termination of contract that ensued from the nationalisation. The House of Lords held that the defendant's profits amounted to a valuable benefit, so the claimant was successful in claiming damages from the defendant due to the frustration of the contract.

10.5 FORCE MAJEURE

“Force majeure” is a concept that originated in French, not English, law, and is not a doctrine under common law. However, force majeure does have legal effect where provided for in English law-governed contracts (and no effect without the existence of such a clause in the contract). “Force majeure” literally translates as “superior forces” and refers to the arising of unforeseen conditions or events beyond the control of both parties, which unavoidably disrupts performance of the contract.

Force majeure clauses are used in contracts due to the limited application of the doctrine of frustration.

Examples of *force majeure* events include such natural events as earthquakes and floods. The definition also includes human-initiated actions such as strikes and acts of war. “Acts of God” and force majeure are *not* interchangeable terms because an “Act of God” does not include human-initiated actions.

If the clause is triggered, the effect on the contract varies; from an extension of time for performance of obligations or suspension of the execution of those obligations during the force majeure event, up to partial or full relief from the specified obligations by one or more of the contracting parties. Negligence or wilful default is not covered, nor is commercial impracticality or inability (*Tennants Lancashire Limited v Wilson CS & Co Ltd* [1917] AC 495). Interpretation is based on the words the parties use in the clause, rather than the general intention of the parties (*Coastal (Bermuda) Petroleum Ltd v VTT Vulcan Petroleum SA (No 2) (The Marine Star)* [1996] 2 Lloyd’s Rep 383).

Unlike frustration, force majeure clauses do not necessarily operate to end the contract. Further, force majeure clauses can be relied on even if the party that is reliant could reasonably have been expected to take the condition or event into account at the time of entering into the contract.

The burden of proof is on the person seeking to rely on the force majeure clause to show that:

- the condition or event falls within the force majeure clause or constitutes a force majeure event;
- as a result of the event, the party was unable to fully or partially fulfil their performance obligations under the contract;
- any other conditions of the force majeure clause (such as notice) are complied with.

Further, where a force majeure clause refers to events “beyond the control of the relevant party”, it has been held that such a clause can only be relied on if the party relying on it had taken all reasonable steps to avoid its operation or mitigate its results (*Channel Island Ferries Ltd v Sealink UK Ltd* [1988] 1 Lloyd’s Rep 323).