Tenancy Agreement: Can Tenant Declare that the Agreement is Void due to Movement Control Order?

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Abstract

The government of Malaysia has declared Movement Control Order (MCO) for the whole Malaysia in order to flatten the curve of Covid-19 infection. Universities, such as UiTM, consequently has been ordered by the government to close its campuses and as such students who are renting a house are wondering whether they can terminate the tenancy agreement which they have entered into. The paper analyses the legal position of doctrine of frustration and force majeure in this context. The analysis is done based on the cases and/or legal provisions from various jurisdiction such Malaysia, Singapore, and the United Kingdom. This paper finds that force majeure clause is most likely cannot be used to terminate the agreement because this clause is usually not included in the terms of the agreement. Doctrine of frustration on the other hand might be use as a ground to terminate the agreement. However, the court will apply the doctrine of frustration in a very careful manner so as to respect the sanctity of the agreement. In conclusion, whether or not tenancy agreement can be terminated due to MCO, it will all depends on the terms of each tenancy agreement.

Keywords: contract; Covid-19; force majeure; frustration; MCO

Introduction

The imposition of the Movement Control Order (MCO) by the Malaysian government and the spreading of Covid-19 pandemic throughout the world has brought about unprecedented impact on the industry and business community. The closure of business due to restriction order has make it difficult for the company to maintain liquidity and revenue as only essential services can operate. Due to this inactivity, it common for...
the industry to re-organize the structure of the company that result in retrenchment and termination of employees. Employees are layoff and thus suffer loss of income and unable to perform their obligations in certain aspects such as rent payment. Retail Group Malaysia (RGM) estimates that within the period of MCO, the retail outlets in non-essential business industry incurred an estimated RM14.31 billion in operating costs which includes rental of premises (Ganesan, 2020).

Due to disruption of business and the increase of operating cost, some businesses are unable to perform their contractual obligations. In addition, residential tenancies also face the same problem as many have suffered loss of income and job and thus have no means to pay the rent. According to Job Street survey, thirty-five percent of Malaysian have experienced a salary reduction of more than thirty percent during the period of MCO and around fifty-four percent actively searching for a job (Choong, 2020).

MCO also impacted the education sector. Due to the MCO, government has ordered, among others, all universities to close its operation except for essential services. This in turn forces students (who are renting a house) to go back home and thus leave their rented house unused. It should be noted that legal tenancy agreement clearly provides for rights and obligations of both property owner and tenant. If either party has defaulted in any of the obligation stipulated under the agreement, legal action can be taken by the aggrieve party. Among the provisions stipulate under the tenancy agreement are rental amount, landlord’s responsibilities, tenant’s obligation, and tenancy period. Currently no statute to govern the scope and delimitation of tenancy agreement, thus general principles of contract apply. Section 38(1) of Contract Act 1950 provides for performance of obligations to be exact and precise unless any law has dispensed with such performance. Thus, the performance of the obligation must be performed at the time as agreed by the parties (Lim Yoh v. Astana Strategi (M) Sdn Bhd & Anor [1998] 3 MLJ 117).

Where parties fail to comply with the terms of the contract, delay in performing his obligations, or is no longer interested in carrying out their obligations prior to the time agreed, the parties are in breach of contract. Thus, the innocent party is entitled to treat the contract as ended and may be able to recover damages. Moreover, if the defaulting party has received any benefit under the contract, he must restore it back to another party (section 65, Contract Act 1950).

In respect of tenancy agreement during this uncertain-period, due to loss of income for some residential tenants, they are unable to pay rent. For others such as university students, as they are ordered to undergo online learning and thus many of them are going back to their hometown, they refuse to pay rent as they are not staying at the rent house. On the other hand, for commercial tenant, they have to cease their business due to MCO and are not allowed to generate their revenue. The legal issue of whether the inability to perform their obligations as stated in their tenancy agreement such as payment of rent due to the global pandemic of Covid-19 and MCO would constitute the invocation of force majeure clause and doctrine of frustration.
Research Problems

There are 2 problems that this paper tries to address. Firstly, in what circumstances can doctrine of frustration be applied in tenancy agreement. Thirdly, whether force majeure clause can be invoked due to MCO.

Research Method

This paper aims to analyze the application of doctrine of frustration and force majeure clause in the situation when supervening event strike beyond the control of contracting parties in respect of their obligations under the tenancy agreement. In order to achieve this objective, the researchers started of by looking at the Malaysian legal position on this matter. The researchers analyze the relevant statute and provisions of the law and also the relevant case-law that discusses about termination of contract due to event such as MCO. The researchers also explore the position of the law from other commonwealth jurisdiction countries such as the United Kingdom (UK), and Singapore. This study uses qualitative method in order to investigate the position of law pertaining to effect of contract on unprecedented situation likes MCO due to Covid-19, where a method of legalistic analysis is adopted. A primary and secondary data are employed by analyzing the legislation, case-law and official documents. This method aims to identify the elements which create the legal issue and resolve it through legal discussion. The materials are obtained, among others, through online database such as LexisNexis.

Discussion

Malaysia and the UK’s position on the doctrine of frustration

Section 52 (2) of Contract Act 1950 is the provision that provides for the doctrine of frustration. It stated that ‘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. From this provision, Section 52 (2) is applicable for situation where the contract becomes impossible ‘after’ a contract has been made. If the contract is impossible to be performed ‘before’ the contract was made, then it will be governed by Section 52 (1). Also, based on Section 52 (2) a contract can become impossible to be performed either due to some supervening event or supervening illegality.

To see the application of Section 52 (2), the researchers refer to the case of Eastacres Development Sdn Bhd v Fatimah Bt. Mutallip & Anor [2000] MLJU 46, where the Malaysian High Court has made reference to the UK’s case of Davis Contractor Ltd v Fareham Urban District Council (1956) AC 696 where Lord Radcliffe has laid down the test in determining as a question of law whether a particular contract has been discharge by frustration or not and this is what his Lordship 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. It was not this that I promised to do.”

The Malaysian High Court also held that the doctrine of frustration must be applied narrowly. The court referred to the House of Lords decision in the case of Tsakiroglou & Co Ltd v Noblee Thorl G mb H (1962) AC 93 where Viscount Simonds held that the nature of the contract must be ‘fundamentally altered’ before the contract can be said to have been frustrated. His Lordship said that “..it does not automatically follow that, because one term of a contract, for example that the goods shall be carried by a particular route, becomes impossible of performance, the whole contract is thereby abrogated.” The court went on to held that the doctrine of frustration must be confined to a narrow circumstances for the simple reason that commercial bargains should not be lightly brushed aside upon a mere change of circumstances.

From this case, the researchers found that the words use by Lord Radcliffe are ‘a thing radically different from that which was undertaken by the contract’ and Viscount Simonds use the word ‘fundamentally altered’. These words are used as a ‘test’ before the doctrine of frustration can be applied.

In another case, the Malaysian Court of Appeal in the case of Bandar Subang Sdn Bhd lwn Persatuan Penganut Sri Maha Mariamman Kajang Selangor (pemegang amanah dan pengurusan Kuil Sir Maha Mariamman, Ladang Bremer) [2019] 5 MLJ 732 referred to the judgment of Lord Denning MR in the case of Ocean Tankers Corporation v V/O Soyfracht [1964] 1 All ER 161 where, in determining what does ‘a thing radically different from that which was undertaken by the contract’ means, His Lordship said this “To see if the doctrine applies, you have first to construe the contract and see whether the parties have themselves provided for the situation that has arisen. If they have provided for it, the contract must govern. There is no frustration. If they have not provided for it, then you have to compare the new situation with the old situation for which they did provide. Then you must see how different it is. The fact that it has become more onerous or more expensive for one party than he thought, is not sufficient to bring about a frustration. It must be more than merely more onerous or more expensive. It must be positively unjust to hold the parties bound. It is often difficult to draw the line.” Thus, in order to determine whether the supervening event is ‘a thing radically different from that which was undertaken by the contract’, it must be ‘positively unjust’ to hold the parties to the strict performance of the contract.

In the UK case of Edwinton Commercial Corp and another v Tsavliris Russ (Worldwide Salvage and Towage) Ltd (The “Sea Angel”) [2007] EWCA Civ 547, the UK Court of Appeal in this case referred to the same statement of Lord Radcliffe in the case of Davis Contractors Ltd v Fareham Urban District Council [1956] AC 696 AT 729 as referred in Malaysian case above, which the researcher do not intend to reproduce. The UK Court of Appeal also referred to the statement of Lord Simon in the case of National Carriers Ltd v Panalpina (Northern) Ltd [1981] AC 675 where he stated that "Frustration of a contract takes place when there supervenes an event (without default of either party and for which
the contract makes no sufficient provision) which so significantly changes the nature (not merely the expense or onerousness) of the outstanding contractual rights and/or obligations from what the parties could reasonably have contemplated at the time of its execution that it would be unjust to hold them to the literal sense of its stipulations in the new circumstances; in such case the law declares both parties to be discharged from further performance.”

The UK Court of Appeal further refers to the concept of justice propounded by Lord Simon where His Lordship stated that “In the first place, the doctrine has been developed by the law as an expedient to escape from injustice where such would result from enforcement of a contract in its literal terms after a significant change in circumstances. As Lord Sumner said, giving the opinion of a strong Privy Council in Hirji Mulji v Cheong Yue Steamship Co Ltd [1926] AC 497, 510: “It is really a device, by which the rules as to absolute contracts are reconciled with a special exception which justice demands.”. Secondly, in the words of Lord Wright in the Cricklewood Property case [Cricklewood Property and Investment Trust Ltd v Leighton’s Investment Trust Ltd [1945] AC 221] at p 241: “…the doctrine of frustration is modern and flexible and is not subject to being constricted by an arbitrary formula”. It is therefore on the face of it apt to vindicate justice wherever owing to relevant supervening circumstances the enforcement of any contractual arrangement in its literal terms would produce injustice.” The Court of Appeal also referred to LJ Bingham statement in the case of The Super Servant Two [1990] 1 Lloyd’s Rep 1 where His Lordship said “The object of the doctrine was to give effect to the demands of justice, to achieve a just and reasonable result, to do what is reasonable and fair, as an expedient to escape from injustice where such would result from enforcement of a contract in its literal terms after a significant change in circumstances…” Based on the authorities cited in the UK’s case, it is clear that the doctrine of frustration exist in order to serve what the justice demand.

Malaysia, Singapore, and the UK’s position on the force majeure clause

In the same Malaysian case of Eastacres Development Sdn Bhd v Fatimah Bt. Mutallip & Anor [2000] MLJU 46 [5], the Malaysian High Court held that “...and in contract where there is a force majeure clause, the court must be cautious and must look into the construction of the clause in order to determine whether such clause is wide enough to cover the contingency in question (Hong Guan & Co Ltd v R Jumabhoy & Sons Ltd (1960) 26 MLJ 141).” From this case, it is clear that the application of force majeure clause will depend on how wide the clause can cover the supervening event in question whereas the doctrine of frustration is much more wider in scope as it is not limited to the wording of the clause in a contract.

The Singapore’s Court of Appeal in the case of RDC Concrete Pte Ltd v Sato Kogyo (S) Pte Ltd and Another Appeal [2007] SGCA 39 explained principles relating to force majeure clause. The court stated that the purpose of having force majeure clause is for the parties to contractually allocate the risks with regards to the occurrence of future events
in specific circumstances which are stipulated within the clause itself. The court further stated that "...the precise construction of the clause is paramount as it would define the precise scope and ambit of the clause itself. The court is, in accordance with the principle of freedom of contract, to give full effect to the intention of the parties in so far as such a clause is concerned."

The Singapore’s Court of Appeal further refers to the observations of Prof Sir Guenter Treitel, one of the leading academic commentators on contract law in the Commonwealth, in the leading work in this particular area of the law (see Sir Guenter Treitel, Frustration and Force Majeure (Sweet & Maxwell, 2nd Ed, 2004) at para 12-001) with regards to force majeure clause where he stated that “Although the doctrine of frustration can be applied in most circumstances, the court would still adhere to the basic principle of freedom of contract. With this regards, having force majeure clause in a contract is a type of freedom of contract where firstly, force majeure clause can exclude the doctrine of frustration where the parties have contracted on terms which indicate that the contract is to remain in being in spite of the occurrence of an event which would, but for such a provision [viz, the force majeure clause], have discharged it. Secondly, it can enable the parties to provide for discharge, or some other form of relief, on the occurrence of any event which, but for the provision, would have had no effect on their legal rights and duties because the change of circumstances brought about by the event was not sufficiently serious or fundamental to discharge the contract under the general common law doctrine.” Thus, from these statements, it shows that force majeure clause allows the parties to exclude the application of doctrine of frustration or provides for some other reliefs should the occurrence of any supervening event. Force majeure clause also allows the parties to provide for discharge of contract on the occurrence of some specific event which would fall short under the doctrine of frustration. These are an important feature of force majeure clause as it could allow the contract to remain alive (or end it, as the case may be) as compared to the doctrine of frustration that will kill the contract entirely. In this sense, force majeure clause provides some flexibility to the contracting parties.

The Singapore’s Court of Appeal also stated that “The prevalent practice of incorporating force majeure clauses into commercial contracts today stems largely from the blunt nature of the doctrine of frustration as a tool to allocate loss. It has often been said that the juridical basis for the doctrine of frustration is unclear, the doctrine is difficult to invoke and the consequences of its operation are drastic, in the sense that the contract is automatically brought to an end. Parties therefore often include force majeure clauses in their contracts to avoid the uncertainty and hardship that might otherwise result from relying on the common law doctrine of frustration. Uncertainty and inconvenience are avoided by incorporating a well-drafted clause that clearly defines the events or circumstances that constitute force majeure. Hardship is also minimized in so far as a force majeure clause can be crafted to provide a more nuanced response to events of force majeure. For example, it may be provided that, in circumstances constituting force majeure, an extension of time may be granted to the party in default, there may be
cancellation of the contract at the option of one party, or the defaulting party’s duty to perform the contract will be suspended. The contract is thus not automatically brought to an end.”

On how the force majeure clause should be interpreted, the Singapore’s Court of Appeal said this “As S Rajendran J observed in the Singapore High Court decision of Magenta Resources (S) Pte Ltd v China Resources (S) Pte Ltd [1996] 3 SLR 62 at 78, [60] (“Magenta Resources”) (affirmed in China Resources (S) Pte Ltd v Magenta Resources (S) Pte Ltd [1997] 1 SLR 797: What is referred to as force majeure in our law (as opposed to French law from which that term originates) is really no more than a convenient way of referring to contractual terms that the parties have agreed upon to deal with situations that might arise, over which the parties have little or no control, that might impede or obstruct the performance of the contract. There can therefore be no general rule as to what constitutes a situation of force majeure. Whether such a (force majeure) situation arises, and, where it does arise, the rights and obligations that follow, would all depend on what the parties, in their contract, have provided for.” The Singapore’s Court of Appeal further stated that the force majeure clause will be construed strictly.

The Singapore’s Court of Appeal also held that a party who relies on the force majeure clause must show not only that it has brought itself within the clause concerned (see Channel Island Ferries (at 327); Magenta Resources ([57]; supra at 86, [98]); and Chitty on Contracts (Sweet & Maxwell, 29th Ed, 2004) vol 1 at para 14-140.) but also that it has taken all reasonable steps to avoid its operation, or mitigate its result (see the UK’s Court of Appeal decision of Channel Island Ferries Ltd v Sealink UK Ltd [1988] 1 Lloyd’s Rep 323 (“Channel Island Ferries”) at 327).

Meanwhile, to add another UK’s case is the case of Seadrill Ghana Operations Ltd v Tullow Ghana Ltd [2019] 1 All ER (Comm) 34, where the court held that, when a party seeks to rely upon on force majeure clause, he must show that the situation and the consequences are beyond his reasonable control.

The application of doctrine of frustration and force majeure clause in the tenancy agreement

For the purpose of this paper, the researchers will focus on the application of the doctrine of frustration and force majeure clause due to the enforcement of MCO to the tenancy agreement. For example, when MCO was enforced in Malaysia, all education institutions were ordered to close operation in an effort to curb and flatten the curve of the Covid-19 cases. The MCO was in force for around 3 months from March 2020 until May 2020. Even so, after May 2020, MCO was still in force under various names such as Perintah Kawalan Pergerakan Bersyarat and Perintah Kawalan Pergerakan Pemulihan. Up until August 2020, most of the public universities have decided to stick or proceed with the online classes, at least until December 2020. A lot of students are renting a house outside their campuses. Due to this closure of universities, students are wondering whether they
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can terminate the tenancy agreement as it would be pointless to keep paying the rent when they do not even use the house anymore.

In order to determine whether a tenancy agreement can be terminated due to the MCO or not, this is where the application of doctrine of frustration can be tested. Based on the position of law highlighted in Section 4.1 of this paper, there are 3 tests to be fulfilled in invoking the doctrine of frustration. Firstly, whether the contract has made a provision for supervening event in question. If the contract has made a provision for the supervening event in question, then contract must be governed by the provision. There will be no frustration. However, assuming the tenancy agreement does not have provision for the occurrence of supervening event such as MCO, then the first test is likely to be fulfilled. Secondly, the supervening event relied by the tenant must not be due to tenant itself or tenant’s fault. To put it simply, self-induced frustration is not allowed. Based on the fact that MCO was enforced by the government, the second test is also likely to be fulfilled. Thirdly, the supervening event which called for the performance of the contract must be that it renders it a thing radically different from that which was undertaken by the contract. Here is the trickiest part. The tenancy agreement is usually drafted in a manner where the owner would rent the house to tenant and the tenant agrees to rent the house for the agreed price. That is it. It usually did not go further in specifying the purpose of the rental of such premises. By applying this example to the third test, the owner can still rent house to the tenant and tenant can still rent (and stay) in the house in accordance with the tenancy agreement. Since the tenancy agreement can be performed without any act which is ‘radically different from what has been agreed in the contract’, the doctrine of frustration is likely to fail to be invoked. However, the outcome would be different if the tenancy agreement was drafted in a more specific manner, for example, it has a term which stated that the house is rent for the purpose of tenant’s education at the Univeristi Teknologi MARA, Shah Alam Campus (UiTM). The researchers argue that if the tenancy agreement has a term like the example given, then may be the doctrine of frustration can be successfully invoked. The reason being is that, the third test in doctrine of frustration requires the supervening event to ‘fundamentally altered’ the contract or make radical change to the term of the contract. Thus, since the MCO had caused the UiTM to be closed, the contract can be argued has been radically changed since the tenant can no longer rent the house for the purpose of his or her study at UiTM. It can also be argued that it is positively unjust to hold the parties to the strict performance of the contract when the basic structure of the contract (i.e the tenancy agreement was entered for the purpose of enabling the tenant to study at UiTM) has been fundamentally altered. Thus, in order to determine whether the doctrine of frustration can be applied in terminating the tenancy agreement, the contract must be examined individually based on what has been agreed by both parties. There can be no straight forward answer that will applies to all tenancy agreement.

Next, whether the tenant can terminate the tenancy agreement using the force majeure clause. In order to answer this question, based on the Section 4.2 of this paper, it
can be said that there are 3 tests to be fulfilled also. Firstly, there must be a force majeure clause in the tenancy agreement. If there is no force majeure clause, then the tenant could not rely on the force majeure clause and has to rely on the doctrine of frustration. Secondly, the tenant who wants to rely on the force majeure clause, has a duty to bring himself within the ambit of the force majeure clause. Failure to adhere to this duty would fail him in his attempt to invoke the force majeure clause. For example, by using the same example above, the tenant must ensure that the MCO or the closure of UiTM due to MCO falls within the list of supervening events in the force majeure clause. Based on the researchers’ study, there is unlikely any contract has put the MCO as one of the supervening events in the force majeure clause. Furthermore, it would not be unwise for parties to be so specific in putting the term ‘MCO’ as one of the supervening events as the government might use different names in the future. As such, based on the research, the term like ‘government intervention’ can but put as one of the supervening events as MCO can be argued as a government intervention as it was the government who ordered the enforcement of MCO and consequently the UiTM was being ordered to close. Thirdly, the tenant must show that the occurrence of the supervening event in question must not be of his or her doing or within his or her reasonable control. If this matter goes to court, after having fulfilled the tests for the application of force majeure clause, the court would then determine what has the parties agreed should such supervening event triggered the application of force majeure clause. If the clause provides for the end of the contract and discharge the parties from further obligation, then the court will make such orders. If the clause provides for some other relief such as an extension of time or compensation paid by owner to tenant, then the court will make such orders. At this juncture, it is worth to note that in invoking the force majeure clause, the rights and obligations of parties are all depends on what they have agreed when contracting. The court will respect the wishes of parties based on the terms of the contract. Similarly, in the case of force majeure clause application, there is no blanket answer to all the tenancy agreement as each agreement will depends on what the contracting parties have agreed into.

Conclusion

As a result of the pandemic, businesses and industries have been affected. Covid-19 pandemic undoubtedly prevents many contracting parties from further performing their obligations. No one has anticipated the rapid spreading of the viruses nor the restrictions imposed by the government. Whether Covid-19 pandemic qualify as a force majeure event and entitle the respective party from further performance will depend on the construction of the terms of their tenancy agreement. Force majeure clause is most likely cannot be used to terminate the tenancy agreement because this clause is usually not included in this type of agreement. In addition, the end result of discharge of frustration is not favorable especially to the commercial tenant as it will put an end the whole contract. Compromise and negotiation might be the best method to solve this matter for the best interest of all parties during this exceptional event. In addition, it is not sufficient for the
party to prove the pandemic qualifies to invoke the doctrine if it does not hinder the party from further performing the obligations. Similarly, the rigidity of common law in upholding the sanctity of the contract will make it difficult to avoid legal obligations under this doctrine. Reassessment of contractual obligation taking into consideration of global pandemic can be taken into account in construing future terms of contract.

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