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FRUSTRATION OF CONTRACT IN THE MALAYSIAN CONSTRUCTION CONTRACT MANAGEMENT

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ABSTRACT: In dismissing conditions affecting the performance of a contract, reaching and maintaining an amicable solution between the parties involved is an important consideration. The doctrine of frustration stipulates that frustration occurs whenever the law recognizes that without default of either party a contractual obligation has become incapable of being performed because of the circumstances involved. Consequently, the data for decision whether a contract has been frustrated is often viewed in the light of existing circumstances and other events occurring. This study is an attempt among others to examine the ways a contract can be classified being in a state of frustration finding out whether the Standard Form of contract used in the Malaysian context has been utilized to the best level and identifying procedures followed in frustration projects. Additionally, this study shall provide suggestions and assumptions in an effort to contribute solutions to issues and problem detected. A case study, empirical questionnaires and structured interviews and general observations were made based on experience and surroundings. As results, it was revealed that in dealing with project frustration, experience is essential. In other words, experience is a pre-condition for dealing with project frustration. Besides, this study also identified that the reported cases of frustrated project seem limited in Malaysia, as supported by the general review of literature on frustrated project. In conclusion, this study recommended that future research shall emphasis on the importance of awareness and knowledge on frustrated projects, particulars by arbitrators and those involved in contract document preparations, to be more skill in their undertakings.

KEYWORDS: Frustration, Contract, Construction, Malaysia

❖ INTRODUCTION

“Frustration” in the Oxford Dictionary (2003) has been explained to “prevent from progressing, succeeding or being fulfilled” while frustration means “being frustrated”. Therefore, frustration of an employment contract can be defined as prevention from continuation of a contract when the employee who is employed under the contract becomes unable to perform the work for which he was employed due to reasons beyond control by both parties (employer and employee). When the employee is no longer able to engage in any further employment and that makes it impossible for a contract to be performed further, the said contract of employment is said to be frustrated and comes to an end (Kiong, 2001). According to Ehlert (2003), the current concept of frustration was defined by Lord Radcliffe in Davis Contractors Ltd vs. Fareham Urban District Council (1956) AC 696 at pg. 729 [and adopted by the High Court of Australia in Codelfa Construction Pty. Ltd. vs State Rail Authority of NSW (1982) 149 CLR 337 at (1956) A.C.]

“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 I promised to do”.

A contract is said to be “frustrated” if it becomes impossible to perform, or if circumstances change to the extent that performance would be substantially different from what was anticipated by the parties. (Kevin’s English Law Glossary) (2002). Furthermore, the defining characteristics of the doctrine of frustration that have emerged from the case law have been summarized by Bingham L.J. in the following terms:

“The doctrine of frustration was evolved to mitigate the rigor of the common laws insistence on literal performance of absolute promises. 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. Since the effect of frustration is to kill the contract and discharge the parties from further liability under it, the doctrine is not to be lightly

invoked, must be kept within narrow limits and ought not to be extended. Frustration brings the contract to an end forthwith, without more and automatically. The essence of frustration is that it should not be due to the act or election of the party seeking to rely on it. A frustrating event must be some outside event or extraneous change of situation. A frustrating event must take place without blame or fault on the side of the party seeking to rely on it (Beatson, 1998).

It is not possible to define exactly what comprises a frustrating event, because this depends heavily on the subject matter of contract and the circumstances of the case, but it is obvious that the event must have severe and radical consequences on the obligations of the parties. Frustration is an excuse for non-performance because performance as originally agreed has become impossible. However, frustration cannot be claimed:

- Where the contract has suddenly become more difficult or expensive for one of the parties;
- If the party was partly responsible for the intervening event, which for example destroyed the object of the contract; or
- If the event was foreseeable.

The consequences of termination of frustration are based on the principles of the common law, that when frustration occurs general it discharges the parties from performing their contractual duties in future (Ehlert, 2003). This study is an attempt among others to examine the ways a contract can be classified being in a state of frustration finding out whether the Standard Form of contract used in the Malaysian context has been utilized to the best level and identifying procedures followed in frustration projects.

❖ THE TEST OF FRUSTRATION (THEORETICAL BASIS)

Considerable judicial attention has been paid to the theoretical basis on which the doctrine of discharge of a contract by frustration rests, perhaps because of a perceived need to explain why a finding of frustration does not constitute a reallocation of risks nor permit an escape from a bad bargain (Beatson, 1998). The courts over the years have had a great deal of difficulty in deciding what is the proper theoretical basis for the court intervening in the contract and declaring it to be frustrated. The theories have varied and there have been fashions over the years (<http://law.anu.edu.au/colin/Lectures/frust.htm>). The heading below reflect the three phases or fashions, with the last one being the one which courts tend to adopt today.

a) IMPLIED TERM

The first theory was that declaring a contract to be frustrated was simply another aspect of the court's ability to imply a term into the contract. If an officious bystander had asked the parties just before they committed themselves to the contract: "What is the result if such and such happens?" the parties would have dismissed the bystander, testily, with and "Of course our contract would be at an end". This was the basis for the decision in *Taylor vs. Caldwell*, where the judgment of Blackburn J is centered on an implied term analysis. He concludes that the existence of the subject matter of the contract is an implied basis for the continuing of the contract (<http://law.anu.edu.au/colin/Lectures/frust.htm>). Beatson (1998) explained implied term theory using a different case. According to him, Lord Loreburn in *F.A. Tamplin Steamship Co. Ltd. vs. Anglo-Mexican Petroleum Products Co. Ltd.* is generally considered to be the classic exposition of the reasons on which the implied term theory of frustration was based:

Court can and ought to examine the contract and the circumstances in which it was made, not of course to vary, but only to explain it, in order to see whether or not from the nature of it the parties must have made their bargain on the footing that a particular thing or state of things would continue to exist. And if they must have done so, then a term to that effect will be implied, though it be not expressed in the contract... Sometimes it is put that performance has become impossible and that the party concerned did not promise to perform impossibility. Sometimes it is put that the parties contemplated a certain state of things which felt out otherwise. In most of the cases it is said that there was an implied condition in the contract which operated to release the parties from performing it, and in all of them I think that was at bottom the principle upon which the Court proceeded. It is in my opinion the true principal, for no Court has an absolving power, but it can infer from the nature of the contract and the surrounding circumstances that a condition which was not expressed was a foundation on which the parties contracted... Were the altered conditions such that, had they thought of them, they would have taken their chance of them, or such that as sensible men they would have said, 'If that happens, of course, it is all over between us'?

Beatson (1998) goes on by saying, the expression 'an implied term' is, however, ambiguous. It may be used in a subjective sense; that is to say, it may mean a term which the Court reads into the contract in order to give effect to what is regards as the parties' real intention at the time of contracting. On the other hand, the implied term may be formulated more objectively. It may mean a term which, in the light events which have actually arisen, the parties as reasonable people would have imported into the contract to deal with that possibility. When used in this sense, the implied term

is betrayed by a similar artificiality. The ‘reasonable person’ has not real existence and represents ‘no more than the anthropomorphic conception of justice’; an opinion ascribed to such a person is, in fact, that of the Court, which is and must be the spokesman of the fair and reasonable person. An implied term of this sort is no more than a fiction. Something added to the contract by the law (<http://law.anu.edu.au/colin/Lectures/frust.htm>) supports this point by saying, the problem, as always with implied terms is that it maybe very difficult to arrive at a clear conclusion as to what the alleged implied term should be. Remember that it has to be capable of clear expression and it must be so obvious that it goes without saying. Of course the parties will differ about these matters.

b) AS A MATTER OF CONSTRUCTION

The second theory is based on constructing the obligations in the contract and limiting them to normal circumstances and not to extraordinary circumstances. This is really not very different from implying a term. But instead of adding an implied term, the technique is to construe the express terms (<http://law.anu.edu.au/colin/Lectures/frust.htm>). This approach is described by Manson J in his judgment in the *Codelfa* case, the leading High Court case on frustration. He refers to Lord Reid’s approach in *Davis Contractors vs. Fareham UDC*. Lord Reid in his facts said, the implied term theory is rejected and instead it is said that the parties never agreed to carry out their obligations in the type of circumstances which have eventuated. This is a matter of construing the principal obligations of the contract. The same idea is reflected in the words of Lord Wright in *Denny Mott Dickson Ltd. vs. James B Fraser & Co. Ltd.* Manson J continued, if we look at the *Codelfa Construction Pty Ltd vs. State Rail Authority of NSW* case, the building of eastern suburbs railway in Sydney was overtaken by disaster when residents obtained an injunction which prevented work being done at night. Codelfa, the contractor, had quoted on the basis of being able to work a three 8-hour shift day. It attempted unsuccessfully to argue that an implied term should meet the new circumstances whereby Codelfa obviously could not finish on time and there were extra costs incurred as a result of the new arrangements. The High Court was however prepared to order that the contract had been frustrated. The result was that the contract came to an end once the injunction was granted. In fact Codelfa finished the work. This work had to be paid for on the basis of a fair and reasonable remuneration, that is, on the basis of restitution, because there was no longer any contract to determine how much Codelfa should be paid for the work. In the course of discussion about the proper basis for the operation of the doctrine of frustration. Manson J made it clear that the court’s task is to compare performance of the contract under the new conditions with the performance contemplated by the contract before the changed circumstances. If performance is radically different, then the contract is frustrated. In this case this was so even though there was a clause -cl 8(2) (c) - which appeared to cover the events which arose. But Manson J said that it was not intended to cover such a radically disruptive event - a court injunction - which prevented the basic system of work from being employed.

c) AS A MATTER OF JUSTICE AND REASONABLENESS

This is really another way of expressing the previous theory. The court will intervene and declare the contract to be frustrated when it would be quite unreasonable to expect the parties, or one of them, to perform under the changed circumstances (<http://law.anu.edu.au/colin/Lectures/frust.htm>). The key to this is found at the end of the para in an extract from Lord Radcliffe’s judgment in *Davis Contractors vs. Fareham UDC* “It was not this that I promised to do”. Just completing the examination of the *Codelfa* case, note that Manson J examined the question whether an arbitration clause survives the termination of the contract because of a frustrating event. There was a mistake view that termination of the contract meant that everything came to a halt, including an arbitration clause. This view is not correct. There are certain matters provided for in the contract which do survive the termination of the contract. Beatson (1998), further more explained that recognition of these facts led certain of the judges (and notably Lord Wright and Lord Denning) to the conclusion that the basis of the doctrine of frustration was the desire of the Courts to reach a justice and reasonable result. ‘The truth is’, Lord Wright said, ‘that the Court or jury as a judge of fact decides the question in accordance with what seems justice and reasonable in its eyes’. This view however might be taken to suggest that a Court had the power to release the parties from their obligations whenever it was just and reasonable to do so, even, for example, where the only effect of the subsequent event had been to render the contract financially more onerous than the parties had anticipated. But it is clear that the circumstances in which a contract will be held to have been frustrated are far more limited in scope.

❖ RESEARCH METHODOLOGY

Data collection was acquired through case study, questioners, observation, structured interviews (both contractor and clients). The scope of case study and questioner’s distribution was confined to Penang. The questionnaire in this study consisted of two segments; basically Segment “A” and Segment “B”. Segment “A” consisted of information related to the demographic data of the respondents. Among the variables in this section include, age, gender, years of experience and profession of the respondent. In Segment B, questions posed were more related to the research paper,

and included items on awareness in frustration of contract, the frequency of such frustration, the cause for a project to frustrate and the procedures taken when a project frustrates. A total of 30 questionnaire forms were distributed to selected respondents. The method used by the researchers in the distribution was on a personal contract-basis. In this method, the researchers went to meet the respondents and provided them with a copy of the questionnaire. The technique used in data collection was a drop and pick-up technique. In this technique, respondents were given the questionnaire and told that the completed questionnaire shall be picked up the next day. There were cases when the researcher had to do a number of follow-ups before picking-up the questionnaires. However, only 15 respondents returned the questionnaire. Out of this, 11 respondents provided complete information as required, 4 responders did not provide complete information. The other 15 respondents did not return the questionnaires. Hence, the response rate in this study can be reported as 50%. This response rate was satisfactory due to constrain in getting respondents for their area of study that is frustration of contract. Another reason for the acceptable response rate was due to the frequent follow-up by the researchers in getting back the questionnaires.

❖ RESULTS AND ANALYSIS

In analyzing the detailed information based on questionnaire in this study, an obvious legitimate factor that contributes towards the high level of awareness regarding frustration of contract is experience. In this context, experience refers to the ability and knowledge in handling problematic projects, particularly frustrated projects. On the other hand, those who reported being unaware about it could possibly be due to the limited occurrence of frustrated project in the scope and course of their job. This observation is further supported by the findings that show only a small percentage of those who seem to be aware of the frustration of contract reported coming across it in their working experience. Furthermore, in documenting the frequency of occurrences, this study revealed findings that supported the limited cases of frustrated projects in the construction industry. In further strengthening this observation, an extensive review of literature showed that such cases (frustration projects) were usually limited in nature. All the reasons of frustration according to respondent's answers have been listed out below:

- Act of God
- Client underestimates the scope of work and not willing to pay extra to complete the job (payment)
- Natural Disaster
- Overlapping of authorities
- The project did not deliver on time due to lack of cooperation between parties
- Delay in site possession
- Awarded the contract before Building Plan approval
- Commitment of involved party.

While some seem to fit in the literature on frustration other had different perceptions on this matter. The most common form of contract utilized in the relevant projects was PWD 203/203A standard form of contract. The underlying explanation for this is the kind of organization handling the project. In this aspect, the forms used more of government based forms simply because the projects were government projects. In further elaborating on this subject, some of the respondents agreed that such forms of contract could help in overcoming frustrated projects. The answers gathered from this research were, no legal clash/dispute between the related or contracted parties, compliance to Acts, there is an implied which we can do so, the architect may issue instruction to contractor informing the postponement of the work and clearly specify of clause. Meanwhile, other respondents do not agree that these forms of contract can help them in overcoming a frustrating project based on the outlined reasons such as no provision sometimes in contract, not directly as it does not address issues directly, there is no explicit provision for such situation within both forms of contracts, the only recourse in both contracts is to grant an extension of time based upon reasons of Force Majeure. However this may not be fair to the contractor as the extra costs consequential to the frustration is not dealt with and finally because it is a natural disaster, nothing can be done. In summary, as printed documents, the standard forms of contract used depend on the nature of a particular frustrated project. Respondents outlined several related producers when a project faces frustration. In analyzing these producers, the study noted the most obvious or common producer was discussion of parties involved. This producer seems rather general and broad, without being specific on the current aspects of such project. Probably, a more logical and in-depth procedure should be established. Whatever the procedure maybe, the essential point is to guide towards an amicable solution with both parties benefiting from it. The suggestions offered in resolving frustrating project seems varied. Some respondents emphasis on the need for managing, controlling, planning, organizing, scheduling, understanding and being reasonable to resolve frustrating project or contract, discussions and report writing based on function and objectives, to have supplementary agreement, to understand contract widely is good for contractual implementation, refer to the scope of work in the contract and architect will access the

problems accrued and have meeting with contractor and the client. Date of commencement will be postponed and the date of completion shall be appropriately modified or recalculated. Others reported as nothing can be done (Act of God), knowing authorities requirements and contractors techniques of negotiations is a must, observe the client's capacity and attitude. If negative, propose to discharge of duties and fees due but if its positive revises the schedule of work and work hard to meet the target and also as a Quantity Surveyor you will have to let the S.O/ Architect to lead. Our part is secondary. Finally, get the two parties involved to meet and discuss one way to resolve by way of brainstorming with agreement to terminate the contract including ant compensation if any (negotiation). As a matter of fact, we cannot classify such suggestions as wrong or right. Each suggestion has its own merit. The feasibility of suggestion provided depends on the relevant discussion between parties that are involved in frustrating projects. In recommending ways to avoid or minimize the risk of frustration the strategies articulated include:

- Take necessary precaution or only involve in projects where certainty of cooperation is assured;
- Set of objectives, brainstorming and generate actions;
- Have more discussion and meeting with the client to ensure everything in order before awarding the contract;
- Collaboration of parties involved must be perfect;
- Understand contract Memorandum of Agreement and all stipulated in the requirements;
- Study the client, nature of work entrusted very carefully before engaging yourself into the contract;
- All parties to play active role of their respective profession. They must have/put the project interest first;
- State clearly the scope and works in the contract to avoid arguments. The contract must be fair to the contractor as well and in he case of example you have given; the contractor cannot be expected to perform beyond the original scope and work;
- In my opinion, the risk of frustration is unpredictable. As such there is no way to avoid/ or minimize this risk as natural disaster or catastrophe is the Act of God. We as human being are not able to overrule the Almighty God;
- Frustration clause deals with elements beyond one's control. Therefore, there is no control expect pray it does not happen;
- There was one contract, the researchers came across which mentions that if ever both parties encounter any problem, both parties are to sit down and negotiate to solve the problem.

Nevertheless, the applicability of these suggestions seems to vary from situation to situation. A suggestion suitable for a particular case might not be applicable to another case in frustrated project. Thus, it would be important to review and analyze the appropriateness of the recommended suggestions from time to time. This study has contributed to the body of existing knowledge related to frustrated project. Cooperation by the various sectors in the industry seems encouraging. Additionally, the responses by the respondents provided vase insight into this study. This study also reinforced that frustrated project is a limited case in the construction industry in Malaysia. This observation was further strengthened by the lack of knowledge on frustration of contract. The primary reason underlying such lack of knowledge is limited occurrence of frustrated projects in Malaysia. A few professionals seem to have some knowledge on frustration, whole others do not seem to be well versed in this area or scope. It can be also be concluded that quantity surveyors, compared to other professionals in the construction industry, are the one who possess more knowledge, thus being able to contribute significantly towards discussing the issue on frustration.

❖ CONCLUSIONS

This segment shall provide some the major conclusions related to the questionnaire research analysis. After, analyzing the detailed information, this study confirmed that used of the various standard forms of contract as described in the Literature Review. The difference types of forms of Contract are PWD 203A, PAM and CIDB. As such, relevant to their study, the mostly used form of contract was the Government Standard Form of Contract (PWD). According to the Clause 52 (Effect of War or Earthquake) any queries respecting the continuance, suspension or termination of the contractor, or failing such agreement shall be settled by Arbitration as provided in Clause 54 hereof. Furthermore, the form of contract used in Malaysia has been reported beneficial and ethical in overcoming a frustrated project. In analysis, the procedures to be taken when a project frustrated, ii was observed that some of the respondents suggested for mutually terminating the contract without any conditions. Such response was supposed by the verdict of judges as documented in the literature review. Accordingly, one of the rules adopted by the judges stated that each party must fulfill his contract obligations before a frustrating event occurs; otherwise the party is excused should frustration occur later. In discussing the ways towards resolving a frustrating project, the soundest proposal is this study is to terminate the project. Such a proposal seems to be in accordance with the literature in frustrated project. For example, Ehlert (2001) stated that the consequences of termination of

frustration are based on the principles of the common laws. The common law stipulates that when frustration occurs, it discharges the parties from performing their contracted duties in future. In short, frustration brings a contract to an end, almost automatically. In elaborating the ways to avoid or minimize the risk of frustration, one respondent presented his opinion that the risk of frustration is unpredictable. As such, it is difficult to avoid or immune their risk. As human beings, we can only pray and are unable to overrule the Almighty God. Such an opinion can further be strengthening based on the general literature and sample cases emphasizing the notion of unpredictability in the risk of frustration. Based on the literature review and after analyzing the respondent's views in this study, the following segment shall present some ideas related to the subject of study. In my observation, the most possible explanation offered by the respondents regarding ways to avoid or minimize the risk of frustration was that since the risk of frustration is unpredictable, hence there is no particular way to avoid or minimize such risk. Additionally, this view is in accordance with the general literature on frustration projects. Some of the views expressed by respondents, in my analysis, do not seem to fit in appropriately in discussing the ways to avoid or minimize frustration. Most of the responses seem to talk about precautions in dealing with risk of frustration that has already occurred and not on how to avoid such risks of frustration. Such views include:

- Take necessary precautions or only involve in projects where certainty of cooperation is assured.
- Set of objectives, brainstorming and generate actions.
- Have more discussion and meeting with the client to ensure everything in order before awarding the contract.
- Collaboration of parties involved must be perfect.
- Study the client, nature of work entrusted very carefully before engaging yourself into the contract.

Furthermore, in my own analysis one of the best ways in avoiding or minimizing frustration is to have contract discussions detailed checklists and thoroughly and prepared contingency plans. Consequently, it's also advisable to purchase relevant insurance bonds that could possibly assist in dealing with future frustrated projects. In further presenting my views on ways to resolve a frustrating project and contract, among others, includes the need to brainstorm decide whether to terminate a project without paying any compensation from both parties, or to make a supplementary agreement with view of continuing a frustrated project. This in my observation is the most appropriate way to satisfy both parties without involving the legal procedure, which encompasses tedious procedure and is time consuming. In addition, based on both the case study and questionnaires analysis, it can be concluded that there is lack of knowledge and experience involving frustrated project in Malaysia. This, in my analysis is primarily due to the limited sample of frustrated project in Malaysia. Such a conclusion also implies that only professionals that are involved in contracted preparation such as Quantity Surveyor, supplemented with a sound legal background, are well versed in frustration. Finally, it is most important to research findings and information generated shared among professionals in the construction industry. Undoubtedly, such information sharing leads to an expansion to the body of knowledge in dealing with both theoretical and practical, the legal aspects and related areas in frustration. Subsequently, I recommend that in future a more elaborate and in-depth study be conducted to examine the issues contained in doctrine of frustration applicable to kind of unforeseen circumstances.

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