COVID-19: Frustration & Contracts of employment

Q: What is the doctrine of frustration?

1. Frustration is a common law doctrine where a contract is treated as discharged by operation of law when an event has occurred which renders continued performance impossible, illegal or radically different to that contemplated by the parties when they entered into the contract. The doctrine was first established in ***Taylor v Caldwell (1863) 3 B&S 826***, where a music hall had been destroyed by fire, but has developed thereafter.

2. In general, a frustrating event is an event which:

   (a) Occurs after the contract has been formed.

   (b) The event strikes the root of the contract and was beyond what was contemplated by the parties when they entered the contract.

   (c) Is not due to the fault of either party.

   (d) Renders further performance impossible, illegal or makes it radically different from that contemplated by the parties at the time of the contract's formation.

3. All of these points are qualified by case law develops in the doctrine of frustration. For example, imprisonment which will be the fault of an employee and thus is an exception to the general rule. This illustrates that the doctrine is nuanced and complex. Furthermore, each case will turn on its own facts.

Q: When will an employment contract be frustrated?

4. The courts and tribunals will be slow to apply the doctrine of frustration in the context of employment law and require strong evidence. The burden of proof lies on the party asserting that the contract has been frustrated. Whether there is a frustrating event is an objective question and the parties understanding, intention, opinion or knowledge is not determinative. Employees have statutory protection against unfair dismissal and

therefore there is great disadvantage to them in finding that their contract has been frustrated.

5. Some established frustrating events in the context of an employment contract are:

   (a) The death of the employee (***Hall v Wright [1859] 120 ER 695***; ***Graves v Cohen (1930) 46 TLR 121***);

   (b) Illness or incapacity (***Notcutt v Universal Equipment Co (London) Ltd [1986] 1 WLR 641***);

   (c) Imprisonment or compulsory service (***Morgan v Manser [1948] 1 KB 184***).

6. Once a contract is frustrated the parties cannot elect to keep it alive (***GF Sharp and Co Ltd v McMillan 1998 IRLR 632, EAT***). This does not prevent the parties entering into another contract and it is also possible that continuity of employment is retained should the relationship continue voluntarily under s212(3)(c) ERA.

Q: When will illness or incapacity frustrate a contract of employment?

7. Frustration of an employment contract is most likely to arise where an employee suffers a prolonged or sudden serious illness or disability. Unfair dismissal, the Equality Act 2010, sickness absence policies, sick pay and permanent health insurance reduce the likelihood that illness or incapacity will result in frustration of the employment contract. This was enforced in ***Warner v Armfield & Retail Leisure Ltd UKEAT0376/12***, where the following comment was made:

   "As a matter of everyday practical reality, employers and employees alike expect to deal with issues of disability, sickness - and absence for other reasons - including imprisonment – within the framework of the employment relationship."

8. Illness or incapacity of an employee are established frustrating events. It is necessary to assess the nature and likely duration of the illness/incapacity and whether it would make performance of the employee's contract impossible or radically different from that envisaged by the contract (***Marshall v Harland and Wolff Ltd [1972] IRLR 90***). In ***Marshall*** guidance was provided as to the factors that should be considered when determining whether an employment contract had been frustrated in incapacity cases:

   (a) The nature of the incapacity in question, its current length and the expected duration: In ***Williams v Watsons Luxury Coaches Ltd [1990]***

IRLR 164, 19 months' sickness absence did not frustrate the contract, even though the last sick note expired 11 months into the absence, and there was no contact thereafter. The absence was caused by a leg injury and there was no suggestion that ***Williams*** could not return to work once it had healed. It was relevant that the employer had failed to make reasonable enquiries about her recovery. However, in ***Collins v Secretary of State for Trade and Industry UKEAT/1460/99*** an employee with a severe hand injury was off work for three years, receiving statutory sick pay and then disability benefit. The employer had provided a P60 and was asked whether he wanted a redundancy payment throughout this period. The EAT upheld the view that the contract was frustrated on the basis that there was very little prospect of ***Collins*** recovering sufficiently from his injury to return to work (this was therefore distinguishable from ***Williams***).

(b) The nature of the employment and how quickly the employer needs to fill the post: The more senior or key the employee the more likely frustration will occur.

(c) The duration of the contract: Short-term contracts are more likely to be frustrated than long-term or permanent contracts.

(d) Length of service: A longer relationship is harder to frustrate on the basis that the parties are assumed to contemplate a longer period of illness (***Marshall v Harland and Wolff Ltd [1972] IRLR 90***).

(e) The terms and conditions between the parties, including permanent health insurance (***Villella v MFI Furniture Centres Ltd [1999] IRLR 468),*** sick pay and capability proceedings.

9. Practitioners will consider the full ratio and reasoning in ***Marshall v Harland and Wolff Ltd [1972] IRLR 90*** in considering frustration, but the factors outlined are not exhaustive. The decision was endorsed in ***Egg Stores (Stamford Hill) Ltd v Leibovici [1976] IRLR 376*** and the EAT added the following non-exhaustive factors for determining frustration when the course and outcome of an illness/accident is uncertain (there is some overlap with ***Marshall***):

(a) The length of previous employment and expected duration of future employment.

(b) Nature of the job

(c) The need of the employer to get work done and the need for a replacement to do it.

(d) The employer's risk of liability for redundancy payments or unfair dismissal.

(e) Whether the employer has continued to pay wages.

(f) The acts and statements of the employer in relation to the employment, including whether the employer took steps to dismiss the employee. A frustrating event brings the contract to an end as a matter of law. However, giving an employee notice of dismissal is not fatal to an argument that the contract has been frustrated (***Notcutt v Universal Equipment Co (London) Ltd 1986 ICR 414, CA***).

(g) Whether a reasonable employer could be expected to wait any longer. This will not only include the impact to an employer but also upon an employee.

10. In ***Williams v Watsons Luxury Coaches Ltd 1990 ICR 536, EAT***, two further considerations were added: (1) the contractual terms around sick pay and (2) the prospects of recovery.

11. The employee's disability under s6(1) Equality Act 2010 does not prevent frustration. But an employer will need to adhere to the provisions of the EqA including the duty to make reasonable adjustments. For example, in ***Warner v Armfield & Retail Leisure Ltd UKEAT0376/12***, the employee had a severe stroke amounting to a disability and was absent for months and then lost contact with the employer. The EAT held that the contract was frustrated. However, it also confirmed that where an employer is trying to establish that the contract employment contract with a disabled employee is frustrated, they will need to consider whether any discriminatory conduct has occurred and whether they have complied with the duty to make reasonable adjustments.

Q: What are the consequences when an employment contract is frustrated?

12. Where the contract of employment is frustrated, it is terminated by operation of law and there is no dismissal under the Employment Rights Act 1996. Consequently, the

employee is unable to make a claim for unfair dismissal.[1] Therefore, in unfair dismissal cases it benefits the employer to assert that the contract has been frustrated, and for the employee to allege that it has not.

13. In addition, the contract ends automatically and without fault. Therefore, future obligations under the contract are ended. Any rights accrued prior to frustration remain. However, this means that an employee is not entitled to statutory notice under s86 Employment Rights Act 1996. In some cases an employee will still qualify for a redundancy payment under s136(5) and 139(4) ERA.

Q: How is a contract of employment different to an ordinary commercial contract?

14. This question is important when understanding the application of the doctrine of frustration (and any associated clauses) in the context of employment law. Employment contracts and ordinary commercial contracts have some important differences because the former is a contract of personal service.

15. The terms of the employment contract contain the rights and obligations of the parties to the contract including implied and express terms and those incorporated from other sources such as policies, collective agreements or handbooks. The basic principles of forming a contract and interpreting its terms and conditions are the same for employment and ordinary commercial contracts.

16. It is not possible in this article to restate every distinction, but the main differences include:

    (a) The court will not *generally* order specific performance of an employment contract as a remedy (***Chappell and others v Times Newspapers Limited and others [1975] 1 WLR; Geys v Societe Generale [2012] UKSC 63; Ashworth and others v The Royal National Theatre [2014] EWHC 1176(QB)***).[2] Instead the remedy is to sue for damages for breach of contract.[3] In ***Chappell*** and others this was explained as being because of the relationship of mutual trust and confidence between the parties and

[1] No entitlement to claim unfair dismissal or any notice or PILON (***GF Sharp and Co Ltd v McMillan 1998 IRLR 632, EAT***). It may be redundancy might be relied on under s136(5) Employment Rights Act 1996.
[2] Specific performance was ordered in ***Hill V CA Parsons and Co Ltd [1972] Ch 305***, where trust and confidence still existed between the parties and the notice of dismissal was only issued under TU pressure.
[3] There are clearly examples as an exception to the general rule that injunctive relief of specific performance will not be ordered – for example in the context of restraining an employer from breaching the terms of a contractual disciplinary policy.

the fact that an employer will not seek to prolong such a relationship when that confidence no longer exists i.e. where the employer does not want to employee the employee, or the employee does not want to work for the employer. Further, s236 Trade Union and Labour Relations (Consolidation) Act 1992, confirms that an employee shall not be compelled to perform work or attend any workplace for the doing of any work.

(b) A repudiatory breach will not automatically terminate an employment contract. The innocent party has the choice whether to accept the breach or insist on performance (and sue for damages) (***Geys v Societe Generale at para 97*** – where the SC confirmed the "elective theory").

(c) Employees have statutory protection against unfair dismissal etc. opposed to just common law remedies, therefore employment contracts have necessarily developed more stringently. The need to separate common law principles relating to contract law from statutory rights in the context of employment law was considered to be "fundamental" by the Supreme Court in ***Gisda Cyf v Barratt [2010] UKSC 41***.

(d) The parties to an employment contract do not have equal bargaining power. This is a subject that has influenced the interpretation of contracts, enabling the courts to look behind descriptions of employment status set out in contractual documentation (such as the car valeters in ***Autoclenz v Belcher [2011] IRLR 820***).

(e) The Unfair Contract Terms Act 1977 does not apply as employees are not "consumers" and are unlikely to be covered.[4] Contracts of employment are excluded from the Consumer Rights Act 2015 under s48.

(f) One cannot assign a contract of employment at common law without consent (***Co-operative Group (CWS) Ltd v Stansell Ltd [2006] EWCA Civ 538***). TUPE is a clear exception to this rule.

(g) Employee obligations cannot be enforced by a third party. Employer obligations can.

[4] There does remain uncertainty as to whether s3 UCTA may cover employment contracts and further appellate authority is necessary to determine this issue. There may also be an argument if the arrangement relates to the provision or sale of services. In addition, any loans could be encompassed by the Consumer Credit Act 1974.

Q: Will the COVID-19 pandemic frustrate contracts of employment?

17. At the time of writing, there is clearly no domestic authority as to whether the pandemic amounts to a frustrating event. There is some case law on similar events in other jurisdictions which support that it might be e.g. China during the SARS breakout in 2003. However, in the UK the courts and tribunals are likely to be slow to conclude that COVID-19 is a frustrating event, especially in the context of employment contracts.

18. There seems likely to be an argument that COVID-19 was an unforeseen event which would fall outside of the contemplation of the parties to an employment contract. The question is likely to be whether the pandemic renders the performance of the employment contract impossible or radically different from that contemplated between the parties. This will always be fact specific.

19. The guidance to work from home and around social distancing (including shielding) in one way is unforeseen in that it has never happened before. However, given the similarity of this to health and safety and ill-health absence considerations there must be an argument that through that prism it was either expressly or impliedly contemplated between the parties. Much will turn on the wording of contracts but employees are entitled to sick pay and health and safety protections under statute.

20. Where a business has collapsed due to unforeseen consequences arising from the pandemic it might be that insolvency practitioners or the secretary of state (defending national insurance fund claims) might attempt to run frustration arguments. Time will tell.

21. In evaluating the likelihood of COVID-19 being a frustrating event, it is worth considering when the doctrine of frustration has not been available generally. In short, frustration is generally not available in the following circumstances:

    (a) When the parties have made express provision for the consequences of a particular event which has occurred or where the frustrating event should have been foreseen by the parties. If we are considering just the fact of the pandemic that seems unlikely. However, ill health absence or incapacity will be expressly or impliedly foreseen and provided for in the contract of employment. This will usually include that the contract will

subsist in the event of sickness absence however the level and type of absence will be dependent on the terms.

(b) The frustrating event is due to the conduct of one of the parties. Whilst COVID-19 is totally unrelated to the conduct of an employer of employee that in itself might not be the frustrating event relied on. It may be that it is a linked issue and that the parties own conduct has exacerbated or caused the frustrating event such as not following government guidance.

(c) An alternative method of performance is not possible (see the commercial case of ***The Furness Bridge [1977] 2 Lloyd's Reports 367***). Furlough under the job retention scheme, working from home or alternative arrangements might mean that alternative performance is possible.

(d) The contract is more expensive to perform or changes in economic conditions. Whilst frustration might not be available this may result in redundancy issues.

(e) The alleged frustrating event is already apparent when the contract is made and gets no worse during the contract term. This might be important for contracts of employment entered into after pandemic and its consequences were apparent (for example, February/March 2020 onwards).

(f) The aforementioned case law on ill-health and incapacity may also be relevant during the COVID-19 pandemic in considering whether absence amounts to a frustrating event. Employers are referred to the discussion in the handout relating to Equality & Discrimination issues for risks in this regard.

Q: What is force majeure clause?

22. A force majeure clause expressly anticipates that there may be a supervening event beyond the control of the parties (but not necessary unforeseen in English law), which might affect the performance of a contract. This could be a change of factual circumstances such as a pandemic causing staff to be ill and unable to work or a legal

change such as the government's guidance on isolation, social distancing and shielding.

23. It is rare for a force majeure clause to be drafted into a contract of employment but not impossible. Therefore, careful consideration of the contract and any associated incorporated (or other) documents should be undertaken.

24. An example of a broad force majeure clause would cover events like, acts of God or the public enemy; war, insurrection or riots; fires; governmental actions; strikes or labour disputes; inability to obtain aircraft materials, accessories, equipment or parts from vendors; or any other cause beyond the parties control. It is more common in commercial contracts to include epidemic or pandemic also. It is very unusual to see these clauses in employment contracts unless the employee is senior in the organisation. Such clauses often require notice to be give by the other party as soon as possible of the difficulty or impossibility of performing the contract.

25. Whether a clause covers the supervening event is entirely dependent on the construction of the contractual wording. However, such clauses are construed restrictively and under implied limitations. The burden of proof lies on the party relying on the clause to demonstrate the scope of the clause and whether the facts in question fall within it. If they can do so the consequences are also determined by the wording of the contract which might provide for non-performance, suspended performance, automatic discharge of the contract.

26. The circumstances arising must be beyond the control of the party and for which the party has not assumed responsibility. Therefore, there must not have been any reasonable steps which could have been taken to avoid or mitigate the supervening event or its consequences. Compliance with the government's guidance will be relevant either because compliance with it causes problems or failure to adhere to it causes the problem.

27. For example, in ***Notcutt v Universal Equipment Co (London) Ltd [1986] I WLR 641***, the Court of Appeal considered whether a force majeure clause in an employment contract, which suspended salary when the employee was absent from work or sickness or incapacity, was enforceable. It concluded it was not engaged where the employee had a heart attach leading to permanent disability.

28. Many 'boiler plate' force majeure clauses have been well litigated before the courts and are already well considered in case law. Some contracts will have clauses which

include epidemics and pandemics (check your insurance policies for example) but not usually employment contracts. A lot of contracts include “Act of God” clauses and historically this has been understood to cover events such as floods, earthquakes which involved no human agency (***Transco plc v Stockport Metropolitan Borough Council [2003] UKHL 61***). There might be an argument that an epidemic or pandemic is an Act of God but whether or not that is the case will be a matter for the courts to determine. Clauses which encompass “events beyond the parties control” are also likely to be litigated. Each case will rise and fall on the wording of the precise clause in question.

The contents of this article should not be taken as legal advice on the circumstances of any particular case. Tailored legal advice should always be obtained prior to acting, especially during such a developing and everchanging public health crisis.

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