

FRUSTRATION OF LEASES: WHO BEARS THE RISK ?

*NATIONAL CARRIERS LTD. v. PANALPINA (NORTHERN) LTD.*¹

Property and contract lawyers have spent many pages debating a problem stated in a deceptively simple manner as, "Can a lease be frustrated?" All parties agree that a lease may be made useless by a supervening event. The real issue is, "Who bears the risk of such an eventuality?"

The usual analysis² proceeds on the following basis: *Paradine v. Jane*³ is an example of "absolute liability" being imposed in a contract. This is "a state of affairs where a man acts at his own peril, where he, in effect, shoulders the liability of an insurer to the plaintiff".⁴ Not until the case of *Taylor v. Caldwell*⁵ was there a general relaxation of this rule. The doctrine in *Taylor v. Caldwell* is identified with the doctrine of frustration as a device, "by which the rules as to absolute contracts are reconciled with a special exception which justice demands".⁶ While this exception applied in a wide variety of contexts⁷ it was felt it did *not* apply to leases, the risk of losing expected enjoyment falling on the lessee.⁸ The conflicting judgments by the members of the House of Lords in *Cricklewood Property and Investment Trust Ltd. v. Leighton's Investment Trust Ltd.*⁹ give no clear guidance so it was only open to the House of Lords to review this point of law, lower English courts being bound by the Court of Appeal decision in *Cricklewood*¹⁰ that it did not apply.

¹ [1981] 2 W.L.R. 45. Also reported [1981] 1 All E.R. 161. Hereinafter *National Carriers*.

² *Chitty on Contracts*, Vol. 1, (24th ed. 1977) ch. 23; G. C. Cheshire and C. H. S. Fitoot, *The Law of Contract*, (4th Aust. ed. by J. B. Starke and P. F. P. Higgins, 1981) ch. 25; D. P. Derham and D. M. Da Costa, "Absolute Liability", (1963) 1 *N.Z.U.L.R.* 37 and *National Carriers* itself are representative of this view.

³ (1646) Ayleyn 26; 82 E.R. 897.

⁴ Derham and Da Costa, *supra* n. 2 at 40.

⁵ (1863) 3 B. & S. 826; 122 E.R. 309.

⁶ *Hirji Mulji v. Cheong Yue* [1926] A.C. 497, 510.

⁷ *Chitty on Contracts*, *supra* n. 2 at para [1428] ff.

⁸ *London and Northern Estates Co. v. Schlesinger* [1916] 1 K.B. 20; *Whitehall Court Ltd. v. Ettlinger* [1920] 1 K.B. 680; *Matthey v. Curling* [1922] 2 A.C. 180.

⁹ [1945] A.C. 221. Hereinafter *Cricklewood*. (Viscount Simon, Lord Wright were in favour and Lords Russell and Goddard were against it applying. Lord Porter expressed no opinion.)

¹⁰ [1943] K.B. 493. See *Denman v. Brise* [1949] 1 K.B. 22.

In response to this we should distinguish two separate doctrines:¹¹

- (1) the rule in *Taylor v. Caldwell* by which a condition is implied that impossibility of performance excuses that performance. This is predicated on the basis that the parties, by the nature of the contract, contracted on the basis of the continued existence of a particular "thing".¹² It is submitted that this would be the true basis for excusing the parties in the situation envisaged by Viscount Simon in *Cricklewood* where "some vast convulsion of nature swallowed up the property altogether or buried it in the depths of the sea".¹³
- (2) the doctrine of frustration which is a rule of construction to supply a term to supplement an intention which the parties have only imperfectly expressed.¹⁴ Frustration is concerned with "inordinate delay" in performance.

This distinction is important. Not only does it mean we need not resort to the doctrine of frustration in many cases of clear injustice, it also has important consequences as to what time the doctrine operates. As will be seen, one of the chief difficulties of *National Carriers* is that it tells us that the doctrine of frustration applies to leases but never tells us in what circumstances.

The Facts

The plaintiffs (respondents to the proceedings) were the lessors and the defendants (appellants) were the lessees of a commercial warehouse opposite which was derelict and ruinous Victorian warehouse. This latter warehouse was "listed", that is, it could not be demolished without proper consent. Even assuming a result favourable to demolition, however, the process by which consent was obtained was lengthy and likely to last at least a year. The Victorian warehouse was to be demolished by the local council due to its dilapidated condition but due to objections by "local conservationists" a local inquiry had to be conducted under the procedure laid down in the relevant conservation legislation.

The problem in the present case arose because the Victorian warehouse became dangerous and the street in which it was situated was closed to vehicular traffic. The commercial warehouse became of no use to the lessees for the period of the closure: they could not move goods to or from the warehouse, the only access being from the

¹¹ See especially R. G. McElroy, *Impossibility of Performance*, (ed. by G. L. Williams, 1941), at 222-224.

¹² *Taylor v. Caldwell*, *supra* n. 5 at 829. McElroy, *id.* 22f.

¹³ *Supra* n. 9 at 229. Further, it explains why Lord Russell in *National Carriers*, while dissenting on the issue of frustration, reserved for later consideration cases of physical destruction and total disappearance of the site. *Supra* n. 1 at 71.

¹⁴ McElroy, *op. cit.*, *supra* n. 11 at 223. Cf. the classic formulation of Lord Radcliffe in *Davis Contractors Ltd. v. Fareham U.D.C.* [1956] A.C. 696, 729.

closed street. The lease was for a total of ten years. The street closure was effected after five years of the lease had run and the local inquiry was expected to take 18-20 months. This would leave a total of three years for the lease to run after the street was re-opened.

Could the lease *in principle* be frustrated? Clearly, the issue is which of two innocent parties must bear the loss. If the doctrine of frustration is successfully invoked the law is imposing a solution to the problem of non-anticipation of risk, casting the incidence of risk on one party or another as the circumstances require having regard to the express provisions of the contract.

With only Lord Russell dissenting, their Lordships decided frustration *could* in principle apply to leases. Lord Russell accepted with "minor qualifications" the decision of Lord Russell and Lord Goddard in *Cricklewood*. This reverses an opinion widely held in both the English¹⁵ and Australian¹⁶ professions and thus the basis of legal advice to clients. Strong reasons are needed for a decision of this sort.

The Nature of the Leasehold Interest

The arguments against applying the doctrine of frustration centre around the nature of the leasehold interest. Following Lord Simon in *National Carriers*¹⁷ the argument can be broken down into three elements:

- (1) *The lease is itself the "venture" or "undertaking"*. The "foundation" of the contract is the transfer of the landlord's possession of the demised property for a term of years. Its contractual foundation can *never* be destroyed because this happens once and for all on execution of the lease. This is most strikingly put by Lord Goddard in *Cricklewood*.

In the case of a lease the foundation of the agreement is that the landlord parts with his interest in the demised property for a term of years, which thereupon becomes vested in the tenant, in return for a rent. So long as the interest remains in the tenant, there is no frustration, though particular use may be prevented.¹⁸

- (2) *The lease is more than a contract*. This is the central argument of those who oppose applying the doctrine to leases. As Lush, J. has stated in *London and Northern Estates Co. v. Schlesinger*:

It is not correct to speak of this tenancy agreement as a contract and nothing more. A term of years was created by

¹⁵ *National Carriers*, *supra* n. 1 at 53.

¹⁶ Lang states, "Whatever the ultimate result of the controversy, whether the doctrine of frustration may apply to leases, the better view appears to be that it does not apply". A. G. Lang, *Leases and Tenancies in New South Wales* (1976) at 29, Lewis and Cassidy are to the same effect. E. C. Lewis and D. I. Cassidy *Tenancy Law of New South Wales* (1966), 84, 356f.

¹⁷ *Supra* n. 1 at 66.

¹⁸ *Supra* n. 9 at 245.

it and vested in the appellant, and I can see no reason for saying that because this order disqualified him from personally residing in the flat [because he was an alien enemy] it affected the chattel interest which was vested in him by virtue of the agreement.¹⁹

- (3) *Contractual obligations in a lease are merely incidental to the landlord and tenant relationship.* Lord Russell in *Cricklewood* expresses this clearly:²⁰

The contractual obligations thereunder of each party are merely obligations which are incidental to the relationship of landlord and tenant created by the demise, and which necessarily vary with the character and duration of the lease. It may well be that circumstances may arise during the currency of the term which render it difficult, or even impossible, for one party or the other to carry out some of its obligations as landlord or tenant, circumstances which might afford a defence to a claim for damages for their breach, but the lease would remain. The estate in the land would still be vested in the tenant.²¹

Lord Russell accepts this argument in *National Carriers* with "minor qualifications".²² His is a lone dissent, however. The majority of their Lordships strongly reject this analysis:

(a) Lord Wilberforce,²³ adopting the analysis of Viscount Simon in *Cricklewood*, pointed out that it is an incomplete argument to say that because a lease is more than a contract but is an estate in land frustration does not apply. The further step is needed of saying that an estate in land once granted cannot be divested, which begs the question.

¹⁹ *Supra* n. 8 at 24. Lord Wilberforce expresses agreement with this but inexplicably says it does not apply to *all* leases. *Supra* n. 1 at 59.

²⁰ *Supra* n. 9 at 233-4.

²¹ Put into its strongest form this argument is summarized by Yahuda: "Here the chattel interest is erected into the fee simple which by its very nature does not fall with the lease as a contract, but continues vested in the tenant whatever may befall the property during the term of the lease". S. Yahuda, "Frustration and the Chattel Interest", (1958) 21 *M.L.R.* 637, 638. Indeed, Yahuda's distinctions are too strong. He contrasts Lord Goddard's views on the chattel interest with Lord Russell's views who allowed express provisions in a lease to terminate it and thus saw it as "not indefeasible". But Lord Russell clearly distinguished the express provision case and the operation of a doctrine of law which automatically and without reference to the parties' intention, determines the allocation. ". . . I am unable to grasp how the doctrine can ever apply so as to put an end to lease and the respective liabilities of landlord and tenant thereunder". *Supra* n. 9 at 232 (my emphasis). He saw *no contradiction* in this position.

²² *Supra* n. 1 at 70-72. He allows that a lease may be involved in the frustration of a commercial adventure when it is "merely incidental to" and "a subordinate factor" of that adventure,

²³ *Id.* 57.

To put the matter in this way, however, is to misrepresent the argument. It is *not* denied that an estate in land can be divested.²⁴ What is denied is that it can be divested in this particular way.

(b) All of the majority judgments²⁵ either implicitly or explicitly approve Atkin, L.J.'s dissenting judgment in *Matthey v. Curling* in which he said:

Seeing that the instrument as a rule expressly provides for the lease being determined at the option of the lessor upon the happening of certain specified events, I see no logical absurdity in implying a term that it shall be determined absolutely on the happening of other events — namely those which in an ordinary contract work a frustration.²⁶

Lord Simon in the present case noted the wide variety of cases in which leases may be determined and said:

Perhaps forfeiture by denial of title is the most relevant (though now largely of historical interest), since it depended on a rule of law extraneous to any term of the lease or to agreement of the parties whereby the lease was prematurely discharged. I can see no reason why a rule of law should not similarly declare that a lease is automatically discharged on the happening of a frustrating event.²⁷

This argument is not convincing. The rule of law Lord Simon refers to has been called an "outmoded doctrine",²⁸ one deriving from the feudal principle that repudiation of the lord destroys the tenure. The tendency has been to restrict this rule.²⁹ That there is a difference between a rule of law operating without reference to the parties' intention and express provisions in the contract has been noted above.³⁰ It is no "logical absurdity" to make such a distinction.

(c) Developed systems of law draw a distinction between interests in land which are relatively permanent and other types of property which are relatively perishable. Lord Hailsham in *National Carriers* noted that "one can overdo the contrast".³¹ In England "houses, gardens, even villages and their churches" can fall into the North Sea due to coastal erosion. In America houses and land disappear into vast sinkholes. In Australia a more relevant example would be that

²⁴ See R. Megarry and H. W. R. Wade, *The Law of Real Property*, (4th ed. 1975), 653-75 who give *eight* other ways in which the lease may be divested.

²⁵ *Supra* n. 1 at 55, 57, 65, 77.

²⁶ *Supra* n. 8 at 199-200.

²⁷ *Supra* n. 1 at 65.

²⁸ Megarry and Wade, *op. cit. supra* n. 24 at 655.

²⁹ *Ibid.* This historical doctrine may be an argument *against* applying frustration to leases for it is merely another example of the policy of the law to restrict the rights of the lessee. See the further example of this in *Industrial Properties (Barton Hill) Ltd. v. A.E.I. Ltd.* [1977] 1 Q.B. 580 esp. 607.

³⁰ See n. 21.

³¹ *National Carriers, supra* n. 1 at 54.

given by Lord President Clyde in *Tay Salmon Fisheries Co. Ltd. v. Speedie*³² viz. whole estates being overblown with sand. Even granted the relative indestructibility of land Lord Simon noted that this would,

. . . perhaps make a lease so much the less likely to be frustrated in fact, but would not constitute inherent repugnance to the doctrine.³³

It is interesting to note Lord Russell's (dissenting) judgment in *National Carriers* on these matters. His Lordship reserved judgment on a case of total destruction or disappearance of the site:

In that last case I would not need the intervention of any court to say that the term of years could not outlast the disappearance of its subject matter: the site would no longer have a freehold lessor, and the obligation to pay rent, which issue out of the land, could not survive its substitution by the waves of the North Sea.³⁴

Since its enunciation and acceptance as a general doctrine, frustration has been applied to a wide variety of interests. Without doubt the doctrine applies to licences, the case of *Krell v. Henry*³⁵ being the leading example. Further, it appears to operate in respect of an executory agreement for a lease³⁶ by which an equitable term of years is created.³⁷ The *real* complaint evident in *National Carriers* is that it is undesirable to allow the doctrine to depend on fine distinctions such as whether it is a lease or a licence, or a legal or equitable interest.³⁸ Lord Wilberforce maintained that the onus lies on those who assert that the doctrine never applies to leases.³⁹ Lord Simon strongly urged that:

. . . the law should if possible be founded on comprehensive principles: compartmentalism, particularly if producing anomaly, leads to the injustice of different results in fundamentally analogous circumstances.⁴⁰

He even doubted the usefulness of the distinction between a lease and a licence:

. . . the distinction . . . is notoriously difficult to draw, and, when it comes to the application of a doctrine imported to secure justice, even more difficult to justify.⁴¹

It is submitted, with respect, that the above distinctions are still important ones. That some of the distinctions are fine can be admitted

³² 1929 S.C. 593, 600.

³³ *Supra* n. 1 at 67.

³⁴ *Id.* 71.

³⁵ [1903] 2 K.B. 740.

³⁶ Goff, J. in *Rom Securities Ltd. v. Rogers (Holdings)* (1967) 205 E.G.

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³⁷ By the rule in *Walsh v. Lonsdale* (1882) 21 Ch.D. 9.

³⁸ *Supra* n. 1 at 54, 57, 64, 66-7, 75.

³⁹ *Id.* 57.

⁴⁰ *Id.* 64.

⁴¹ *Ibid.*

but they nevertheless exist, and the law has drawn finer. Windeyer, J., in the leading Australian case of *Radaich v. Smith*⁴² has stated, "The distinction between a lease and a licence is clear". He stated the distinction in the following terms:

What then is the fundamental right which a tenant has that distinguishes his position from that of a licensee? It is an interest in land as distinct from a personal permission to enter the land and use it for some stipulated purpose or purposes.⁴³

A formulation of the distinction in these terms makes it clear that the lease/licence distinction is only another way of saying that the allocation of risk is fundamentally different when an estate in land is involved. A licence is inherently susceptible to frustration because it is a relationship entered into merely for "some stipulated purpose". When the land is made useless for that purpose this allows the intention of the parties as to the termination of the relationship to have full effect. It should be noted that Lord Simons' concern with a doctrine "imported to secure justice" is more strictly concerned with the rule in *Taylor v. Caldwell* rather than the doctrine of frustration.

Lord Simon stated:

The rule can hardly depend on whether the estate or interest in land is legal or equitable: no-one has so suggested; and it would constitute an even more absurd anomaly than those to which I have ventured already to refer.⁴⁴

With respect, his Lordship has ignored that there is a distinction between a legal and equitable interest. The entitlements under an agreement for a lease are closely linked to the parties' entitlement to enforce that agreement by specific performance. Being an *equitable* remedy it is a discretionary remedy, and may be refused in cases of futility, impossibility or undue hardship (such as exposing one of the parties to prosecution for breach of local government legislation).⁴⁵

Thus, as Lang states:

The lessor or lessee could become effectively discharged from performance of the agreement, by refusal of a decree of specific performance on discretionary grounds, based on similar facts where the doctrine of frustration would apply in a purely contractual situation.⁴⁶

The rule in *Walsh v. Lonsdale* is *not* to be taken as destroying the difference between legal and equitable estates. The very basis of relief in the granting of specific performance is founded on the distinction

⁴² (1959) 101 C.L.R. 209, 221.

⁴³ *Id.* 222.

⁴⁴ *National Carriers*, *supra* n. 1 at 67.

116 C.L.R. 328, 337.

⁴⁵ *Cf.* Lang, *op. cit.*, *supra* n. 16 at 30, citing *Pottinger v. Genge* (196

⁴⁶ *Ibid.*

tion between executory and executed contracts.⁴⁷ Certain writers⁴⁸ have used the rule in *Walsh v. Lonsdale* to argue that because leases cannot be frustrated neither can agreements for leases. It is submitted that it is to ignore the basis on which the equitable rule is founded to argue either this or the converse proposition propounded by Lord Simon.

(d) Several of their Lordships were critical of the assertion that the foundation of the contract remains, that "the tenant will have that which he bargained for, namely, the leasehold estate".⁴⁹ Lord Roskill pointed out:

In many cases he is interested only in the accompanying contractual right to use that which is demised to him by the lease and the estate in land which he acquires has little or no meaning for him.⁵⁰

Or as Lord Wilberforce succinctly put it, "the lease . . . is a subsidiary means to an end, not an aim or end of itself".⁵¹

By itself, of course, this is inconclusive. No one denies that the lease may be made useless, just as title to land may be made useless after sale. The issue is, who bears the risk of that eventuality.

The Incidence of Risk

One of the basic principles of land law is that the risk of accidents passes to purchasers on the signing of the contract.⁵² The previously accepted argument proceeded on the basis that a lease was no different from a sale of land. In statutory language it is a "conveyance".⁵³ On execution of the contract the purchaser gets both the advantages and disadvantages of purchase. Risk thus passes to him.

Both Lord Wilberforce and Lord Simon were at pains to dispel this argument. Lord Wilberforce said:

But the two situations are not parallel. Whether the risk — or any risk — passes to the lessee depends on the terms of the lease: it is not uncommon, indeed, for some risks — of fire or destruction — to be specifically allocated. So in the case of unspecified risks, which may be thought to have been mutually contemplated, or capable of being contemplated by reasonable men, why should not the court decide on whom the risks are to lie.⁵⁴

Lord Simon argued:

⁴⁷ See cases cited in R. P. Meagher, W. M. C. Gummow and J. R. F. Lehane, *Equity: Doctrines and Remedies* (1975), para. 2001-2004.

⁴⁸ G. C. Cheshire and C. H. S. Fifoot, *The Law of Contract*, (4th Aust. ed. by J. G. Starke and P. F. P. Higgins, 1981), para. 2522.

⁴⁹ *National Carriers, supra* n. 1 at 58, 68, 76.

⁵⁰ *Id.* 76.

⁵¹ *Id.* 58.

⁵² See, for example, Megarry and Wade, *op. cit.*, *supra* n. 24 at 576, 674.

⁵³ Conveyancing Act, 1919 (N.S.W.), s. 7.

⁵⁴ *National Carriers, supra* n. 1 at 58.

Moreover the sale of land is a false analogy. A fully executed contract cannot be frustrated; and a sale of land is characteristically such a contract. But a lease is partly executory: rights and obligations remain outstanding on both sides during its currency.⁵⁵

This is no answer to those who believe as Lord Russell in *Cricklewood* that the contractual obligations are merely *incidental* to the demise. The lessee may be relieved of obligation in certain circumstances but the basic issue remains.

The issue of who bears the risk assumes greater importance when we realize that third parties may acquire rights under a lease and termination of an estate would destroy the interests of sub-lessees and mortgagees whose title depends on the lease.⁵⁶ However, it may be that their interests are of little value anyway if the contract is frustrated; and a contractual action (for example, to recover a mortgage debt) is not precluded.⁵⁷

Their Lordships could not see why the lessor should be free of the burden of risk. Lord Hailsham sees only a difference "in degree" between chattels and real property. Lord Roskill seemed to regard it as a matter of "policy".⁵⁸

In the judgments in *National Carriers* we can see, perhaps, the reflection of a change of attitude as to the burden of risk in real property transactions. This is evident in the English decisions on frustration of contract for the sale of land. Although no reported case actually decides that a contract for the sale of land can be frustrated⁵⁹ several recent Court of Appeal decisions "assume" it can be.⁶⁰ It is submitted that if the principle in *National Carriers* is accepted as correct there should be no hesitation in deciding that contracts for the sale of land may be frustrated. This point has been most clearly seen in

⁵⁵ *Id.* 68.

⁵⁶ *Cricklewood*, *supra* n. 9 at 244, 245 (Lord Goddard) 233, 234 (Lord Russell).

⁵⁷ *Derham and Da Costa*, *supra* n. 2 at 43-4.

⁵⁸ *National Carriers*, *supra* n. 1 at 55, 74. Historically the policy was always against the lessee. The lessee was seen as a high speculator, a mere usurer. Plucknett said of him, "His term is not his natural means of subsistence; it is speculation, an operation of high finance which is certainly sinful, undertaken at his own risk in this world and the next". 40 *Harvard Law Review*, note at 124. The termor was seised but not of free tenement to his seisen was not protected by the petty azzizes. This was the fundamental reason for distinguishing real and personal property.

⁵⁹ But see the Privy Council decision *Wong Lai Ying v. Chinachem Investment Co. Ltd.* (Unrptd, 27th Nov. 1979) which applies the doctrine to the assignment of a leasehold interest. The case, however, seems to turn more on the particular terms of the contract involved.

⁶⁰ *Amalgamated Investment and Property Co. Ltd. v. John Walker & Sons Ltd.* [1977] 1 W.L.R. 164 per Buckley, L. J. at 173; *Universal Corporation v. Five Ways Properties Ltd.* [1978] 3 All E.R. 1131 at 1135 approved on appeal by Buckley, L. J. at [1979] 1 All E.R. 522 at 554. See G. Walker "Insurance and the Sale of Land" (1981) 9 *Australian Business Law Review*, 948 for a survey of the main positions on the burden of risk in a contract for the sale of land.

Canada in *Capital Quality Homes Ltd. v. Colwyn Constructions Ltd.*⁶¹ where, after accepting that frustration applies to leases, Evans J.A. continues:

I am unable to distinguish any difference between leases of land and agreements for the sale of land, so far as the application of the doctrine is concerned. Each is more than a simple contract. In the former an estate in land is created while in the latter an equitable estate arises. There does not appear to be any logical reason or binding legal authority which would prohibit the extension of the doctrine to contracts involving land.⁶²

Although the purchaser is the equitable owner of the land this does not mean that he should be treated as owner for *all* purposes (and thus the bearer of the risk) for his equitable ownership is merely an incident of the right of specific performance. A vendor could not cast the burden of a loss on the purchaser by means of specific performance. Specific performance is a mutual remedy and if the vendor is unable to perform his side of the bargain the remedy is unavailable.⁶³

The Application of the Doctrine to Leases

Although the judgments in *National Carriers* clearly indicate that *in principle* the doctrine of frustration applies to leases the *application* of this doctrine is given very little attention. There is no reported case of a lease being frustrated in English law. When does frustration apply? Their Lordships tell us "not never" but "hardly ever" and hope this is sufficient to forestall greatly increased litigation. Two issues are involved:

(1) *If the doctrine operates, does it operate automatically?* The judgments in *National Carriers*⁶⁴ reflect the conventional wisdom that the doctrine of frustration operates "automatically". The dissolution of the contract follows without further being given by either of the parties, who can themselves neither aid nor prevent the dissolution. In the context of leasehold properties, however, this does not make a great deal of sense.

First, it may not be appropriate in the context of real property to allow it to operate automatically. The N.S.W. Supreme Court in *Halloran v. Firth* was alarmed by the:

. . . extraordinary effect of terminating automatically the estate vested in the lessee and of putting the lessor back into possession irrespective of the wishes of the parties.⁶⁵

⁶¹ (1976) 61 D.L.R. (3d) 385 Evans, J.A. speaking for the Ontario Court of Appeal.

⁶² *Id.* 397.

⁶³ See the forceful argument of Harlan Stone, "Equitable Conversion by Contract" (1913) 13 *Columbia L.R.* 369, 385-388.

⁶⁴ See esp. Lord Roskill, *National Carriers*, *supra* n. 1 at 74.

⁶⁵ (1926) 26 S.R. (N.S.W.) 183, 187. Supported on appeal by Knox, C.J. and Gaven Duffy, J.: *Firth v. Halloran* (1926) 38 C.L.R. 261, *cf.* Isaacs, J. at 269.

Secondly,⁶⁶ in the context of a lease it is of the utmost importance in determining when frustration occurs with exactitude. The lessee will want to know when his obligation to pay rent ceased. It is in this context that we must distinguish the principle in *Taylor v. Caldwell* from that of frustration. It is obvious that if the "thing" on which the contractual relation depends disappears (for example, by fire or disappearance into the sea) the dissolution follows "automatically from the event". But if as a result of inordinate delay the contract is frustrated there is *no* definite time at which it can be said the doctrine has operated.

Thirdly,⁶⁷ the automatic theory may lead to uncertainty. While the theory was formulated to avoid the injustice of requiring *both* parties consent before dissolution was effective, if one party is unaware of the impact of the doctrine the other may maintain a prolonged hold over him to his disadvantage by only telling him of the frustration when he tries to enforce the agreement. Injustice can be the result.

To avoid these difficulties McElroy and Williams⁶⁸ proposed that *either* party be entitled to elect to declare the contract at an end. The date of dissolution is the date election has been communicated to the other party. This suggestion has the merit of making this branch of contract law consistent with discharge by breach.

Diplock, L.J.'s judgment in the Court of Appeal in *Hong Kong Fir Shipping Co. Ltd. v. Kawasaki Kaisha Ltd.*⁶⁹ emphasises that it is the *event* and not the fact that the event is a result of a breach of contract which relieves the party not in default of further performance of his obligations. An election to declare the contract at an end should thus exist no matter what the cause of the event. When the effect of an event is to make further performance impossible it is easier, of course, to infer that an election has taken place. In all cases, however, the right to an election should exist.

It follows that on this analysis either the lessor or the lessee could elect to declare the contract at an end. The tenant is more likely to be the elector but there seems to be no reason why the landlord cannot find himself in the situation of saying to the tenant, "*Non haec in foedera veni*".⁷⁰ This, however, raises the second problem: in what circumstances can either party say this?

(2) *Relevant Factors in Determining When a Lease is Frustrated.*

(a) *The length of the lease* is seen by some writers as being decisive in determining whether a lease will be frustrated by any particular event:

⁶⁶ See McElroy, *op. cit.*, *supra* n. 11 at 225f.

⁶⁷ *Id.* 227.

⁶⁸ *Id.* 229.

⁶⁹ [1962] 2 Q.B. 26 at 69.

⁷⁰ *Davis Contractors Ltd. v. Fareham U.D.C.* [1956] A.C. 696, 729 per Lord Radcliffe.

Where the transaction is of a kind that is generally understood to allocate the risk that has occurred, relief will be properly refused. A long term lease allocates practically all risks; a short term licence for a specific purpose allocates many fewer.⁷¹

(b) Others talk of the *proportion of time the lease is affected* (a crucial factor, it appears, in the present case). Thus:

If . . . the frustrating event affects the use of land during a negligible part of the period of the lease or of the unexpired portion thereof . . . frustration does not apply. . . . But if the use of the land is or presumably may be affected during the whole of the term or of the unexpired period thereof, it is submitted that there is no reason for maintaining that frustration does not apply.⁷²

Some consideration should be given to the degree of likelihood of interruption needed to establish frustration. The interruption in the present case was "indefinite" but not, apparently, sufficiently indefinite to justify the tenant claiming that the lease had been frustrated.

(c) Restrictions on particular user are also relevant. These will affect the rental value which is the chief means of allocating risk.⁷³

Given that we are now willing to allocate risk to other than the lessee, Professor Atiyah's analysis of when frustration applies⁷⁴ suggests that the ultimate decision will rest on the question: on which party is it reasonable to place the risk?⁷⁵ Professor Atiyah's classification sits well with the factors discussed above:

(i) *Express Agreement* to accept the risk. For example, insurance by the tenant would indicate an acceptance of risk.

(ii) *A party takes the risk of circumstances affecting his purpose and not the common object of both parties*. Thus if a reasonable use remains for the subject matter it is probable that the alleged frustrating event affects the motive of only one of the parties. This basis has been used to explain the different results in the "Coronation Cases".⁷⁶ Thus the lessee of a saloon in Canada was held to take the risk occasioned by prohibition legislation — he could also sell cigars, soft drinks, meals and let lodgings.⁷⁷ As noted above this restriction on use will affect the rental value of the premises, thus:

⁷¹ S. M. Waddams, *The Law of Contracts*, (1977), 233.

⁷² Yahuda, *supra* n. 21 at 640.

⁷³ *National Carriers*, *supra* n. 1 at 69.

⁷⁴ P. S. Atiyah, *An Introduction to the Law of Contract*, (2nd ed. 1971), 174-8.

⁷⁵ Apart from legislative intervention into this area (for example, the Frustrated Contracts Act, 1978 (N.S.W.)) there is no suggestion of a sharing of the bad luck by reducing the rent.

⁷⁶ A room overlooking a procession is only of use if the procession takes place but a cruise around the fleet "was very well worth seeing without the review" (Sir Frederick Pollock (1904) 20 *L.Q.R.* 4).

⁷⁷ *Charrier v. McCreight* (1917) 33 D.L.R. 689, 692 (Alta C.A.).

(iii) *An abnormally large remuneration* indicates it is only reasonable to place on the landlord some of the risk.

(iv) *A person who undertakes to do something takes the risk that performance may prove more onerous than expected due to slight deviations from the normal, whereas he does not take the risk of performing the impossible owing to utterly abnormal occurrences.*

Thus, events perfectly foreseeable, or which should have been foreseeable, are unlikely to cause frustration. Therefore, although Lord Simon stated that the "more commercial the character of an agreement, the more various are the circumstances in which it is liable to frustration",⁷⁸ we should note that in business contracts, with commercially experienced parties, a range of events are likely to be excluded as being able to frustrate a contract. In the present case, for example, we might argue that environmental, planning and conservation law is of such a large magnitude businessmen should have foreseen the events which occurred.⁷⁹ Lord Simon noted that commercial men are entitled to act on "reasonable commercial probabilities" at the time they make up their mind.⁸⁰

(v) *If a remedy is available against a third person* the person possessing that remedy is more likely to bear the risk. Thus if compensation is given for government interference (for example, resumption of leased premises) then frustration is unlikely to relieve the tenant if the tenant is the recipient of that compensation.

(vi) *The doctrine of frustration can rarely, if ever, apply to speculative ventures.* Thus a long term lease which allocates all risks is unlikely to be frustrated.

Conclusions

If the doctrine of frustration does apply to leases in N.S.W. regard must be had to the Frustrated Contracts Act, 1978. This Act is concerned strictly with frustration and has no application to impossibility.⁸¹ The Act intends to lay down flexible procedures which parties can administer themselves. If the adjustment of loss procedures laid down are inappropriate the Court may "substitute such adjustments in money or otherwise as it considers proper" (s. 15(1)). Note, however, that the procedure under the Act may be excluded (s. 6(1) (e)). Because property contracts are often in standard form and because it is the tenant who is more likely to be the one claiming frustration we may find a practice arising of the exclusion of the doctrine altogether or landlords imposing their own adjustment procedures. If the procedure under the Act is excluded and no contrary

⁷⁸ *National Carriers*, *supra* n. 1 at 68-9.

⁷⁹ See *Amalgamated Investment and Property Co. Ltd. v. John Walker & Sons Ltd.*, *supra* n. 60 at 173 per Buckley, L.J.

⁸⁰ *National Carriers*, *supra* n. 1 at 69.

⁸¹ *Cheshire and Fifoot, op. cit.*, *supra* n. 48 at para 2533.

provision is made one must resort again to the common law. No longer does the lessee always bear the risk. In the analysis above he may elect to end the contract and be discharged from any further obligations under it.

It seems therefore, that *National Carriers* marks another step to an altered burden of risks in real property transactions. It is submitted, however, that this should not be achieved by the blurring of important distinctions between real and personal property or between legal and equitable estates. As Lord Russell argued in *National Carriers*⁸² leasehold interests are one of the two presently existing legal interests in land. These interests are of such importance and such large sums of money are involved that to change the allocation of risk necessitated legislative activity. If the courts could not wait for this they should have laid down clear guidelines as to both *why* and *when* the doctrine applies. This the House of Lords has not done.

DONALD ROBERTSON, B.Ec. (Hons.) — Third Year Student.

⁸² *National Carriers*, *supra* n. 1 at 70.