

**FRUSTRATION OF CONTRACT DUE TO ABNORMAL INCREASES OF PRICE  
IN MALAYSIA LEGAL PERSPECTIVE**

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**UNIVERSITI TEKNOLOGI MALAYSIA**

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INCREASES OF PRICE  
IN MALAYSIA LEGAL PERSPECTIVE

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*To my beloved parents, brothers and sisters  
Thank you for abundance support and great love*

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## **ABSTRACT**

Malaysia construction industry has become challenging in recent years. The intervention of external sources such as politic, social and economy may affected the construction industry in many ways. For the current trend, since the implementation of Government Service Tax, the industry is still trying to adjust and adapt to the policies. However, during this grace period many impacts have been contributed to the industry due the implementation of such policies. One of the impacts is regard to cost implication to the projects. The market price showed vulnerability in the condition, such as the price might get reduce in a day and fluctuate in another day. Lot of projects seem to suffer with this condition especially project that involves with investment. There is also a case where the parties in the contract have to terminate the contract due to cost implication. Since the contract shall be treated as legally binding between the parties, thus it makes contract cannot simply be discharged their obligation due to certain restrictions. However, it is seemed injustice to force the party to perform their obligation when due no default of neither anyone, resulted the contract to become onerous or impossible. Thus this study is carried out to determine whether the contract may be deemed to be frustrated from an economic perspective. In specific to determine either the contract can be discharged due to one of the reason of abnormal increase of price or global economic crisis. To answer the question a court cases being analyzed and the resulted in tabulated in data analysis section.

## ABSTRAK

Industri pembinaan Malaysia semakin mencabar sejak beberapa tahun kebelakangan ini. Campur tangan faktor-faktor luaran seperti politik, ekonomi dan sosial berkemungkinan menjejaskan lagi industri pembinaan Negara dengan pelbagai cara. Pelaksanaan Cukai Barang dan Perkhidmatan (GST) oleh kerajaan baru-baru ini, menunjukkan industri pembinaan negara masih lagi di dalam tempoh penyesuaian diri ke atas dasar tersebut. Walau bagaimanapun, kesan- kesan ke atas pelaksanaan dasar tersebut telah dapat dilihat di dalam industri pembinaan negara. Salah satu kesan yang ketara adalah implikasi kos yang ketara ke atas projek-projek yang sedang berjalan. Harga di pasaran dijangkakan tidak menentu dari semasa ke semasa sebagai contoh harga pasaran dijangkakan mungkin akan berlaku pengurangan dalam masa sehari dan akan berubah di hari yang berikutnya. Dalam keadaan seperti ini, dijangkakan banyak projek yang akan menderita terutama projek projek di dalam industri pembinaan yang melibatkan pelaburan.

Terdapat juga kes di mana pihak-pihak di dalam kontrak perlu menamatkan kontrak kerana implikasi kos yang melampau. Oleh kerana, kontrak perlu diambil kira sebagai perjanjian yang diikat dari segi undang-undang maka sesuatu kontrak tidak boleh ditamatkan atas halangan tertentu. Walau bagaimanapun, ia seolah-olah tidak adil untuk memaksa pihak-pihak di dalam kontrak untuk melaksanakan kewajipan mereka apabila bukan diatas kesalahan mana-mana pihak sesiapa, kontrak tersebut menjadi membebankan dan mustahil dilaksanakan. Denga itu, kajian ini dijalankan untuk mengkaji sama ada kontrak boleh disifatkan sebagai kecewa dari perspektif ekonomi. Secara terperinci, untuk menentukan sama ada kontrak boleh dilepaskan dari perspektif undang-undang malaysia atas salah satu sebab peningkatan secara abnormal harga atau disebabkan oleh krisis ekonomi global. Untuk menjawab persoalan yang dikemukakan

diatas, analisa kes-kes mahkamah dilakukan dan data analisa dijadualkan di bahagian analisis data.

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## **LIST OF ABBREVIATIONS**

<b>AMBB</b>	<b>Arab Malaysian Bank Berhad</b>
<b>HDR</b>	<b>Housing Developers Regulation</b>
<b>LAD</b>	<b>Liquidated Ascertained Damages</b>
<b>PWD</b>	<b>Public Work Department</b>
<b>Reg.</b>	<b>Regulation</b>
<b>SPA</b>	<b>Sales and Purchase Agreement</b>
<b>SPPA</b>	<b>Supplemental Sales and Purchase Agreement</b>



## CHAPTER 1

### INTRODUCTION

#### 1.1 Background of Research

Generally, the law of contract provides the ground rules in which contract can be discharged. Malaysia's Contract Act provides that contract can be discharged through performance<sup>1</sup>, agreement<sup>2</sup>, frustration<sup>3</sup> and breach<sup>4</sup>. Besides that, the parties can also discharge his obligation by varying the terms of their contract by agreement (Ali Mohammad Matta. 2006). Similarly to most engineering and construction contract, allocation of provision to discharge a contract is mostly in the contract itself. According to Ramsey, V., et all (2007) most of engineering or construction contract will have an internal machinery for one or other party to determine and discharge the contract.

Discharge in general can be defined as official permission to leave a place or job (Wehmeir, S., McIntosh, C., Turnbull, J., et all. 2005). According to Oxford Dictionary of Law (2013), discharge of contract refers to release of the contractual obligation

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<sup>1</sup> Part V, Section 38-68, Act 136, Contract Act 1950

<sup>2</sup> Section 63& 64, Act 136, Contract Act 1950

<sup>3</sup> Section 57, Act 136, Contract Act 1950

<sup>4</sup> Section 40, Act 136, Contract Act 1950

between the parties in contract. It is when parties have complied with their obligation or other events have occurred that release one or both parties from performing their further obligation (Fitzgerald, J and Olivo, L, 2005). After discharging the contract, the parties are no longer obliged to perform their future duties and obligation as set out in the term and condition of the contract.

The general rule at common law is that parties are bound to perform any obligation that they have undertaken even though performance subsequently becomes impossible. The performance of a contract must be exact and precise according to what the parties has been promised.<sup>5</sup> Equally the performance should be in accordance with the term and condition of the agreement in order to discharge the contract obligation. This is called the 'strict' and 'exact performance' rule under law.<sup>6</sup>

Whereas, in *Sumpter v Hedges*<sup>7</sup>, law has recognized some exceptions to the general rule of the strict performance of a contract. In this case, the plaintiff was appointed by the defendant to construct certain buildings on the grounds based on a lump sum amounted of 565 pounds. Instead of completed the work, the plaintiff was only succeed to do some part of the work amounted to 333 pounds. Subject to that, the defendant took the initiative to complete the rest of the work. As a result, the plaintiff sued on quantum meruit as much as he or she has incurred in the cost. From the judgment of the trial the judge awarded the plaintiff for the value of the materials used, but nothing in respect to the work done.

The decision was upheld by The Court of Appeal affirmed that the plaintiff could not recover from the defendant in respect to the work done as part of quantum meruit due to the fact that the contract was for a lump sum, and there was no evidence that an

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<sup>5</sup> *Chuah Ngah Chin v Ng Kie En* (1968), 2 MLJ 267

<sup>6</sup> *Cutter v Powell* (1795) 6 TR 320

<sup>7</sup> (1898) 1 QB 673

agreement for part performance was formed<sup>8</sup>. As a result the decision in Sumpter and other similar decisions have resulted the common law to further acknowledge some exemptions to the general rule other than that performance of a contract must be absolute and accurate according to the terms.

Besides of the mechanism to discharge a contract made under statutory, the contract also can be discharged by provision under the agreement that governed between the parties. The parties may expressly insert the provision that in the event of certain condition, the contract shall *ipso facto* being determined or one of the parties have the option to cancel the contract.

In such cases, contract is said to have internal machinery<sup>9</sup> for one or other party to determine the contract. These provisions whether express or implied, allow parties to access the right of determination or termination in certain circumstances to treat the contract to an end.

For instance, the local Public Work Department Form of Contract 203A (Revised 1/2010)<sup>10</sup> has allocated provisions of list of the event on default of obligation by government or contractor and the consequence after the defaults' event respectively in the standard form. Provision in the contract also expressly stipulated the procedure to be followed by parties to enable the contract to be terminated on any default committed on behalf of other party.

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<sup>8</sup> (1898) 1 QB 673

<sup>9</sup> Ramsey, V. (2007) "*Construction Law Handbook*". Thomas Thelford. pp, 461.

<sup>10</sup> Jabatan Kerja Raya Malaysia, 'Standard Form Of Contract Where Bills of Quantities Form Part Of The Contract' JKR Malaysia, 2010, page 31-36

For instance, Clause 51(a) of the standard form detail out on the event and consequences of default by the contractor under the form. Meanwhile Clause 51(b) lay down the principal of termination on default by the contractor. In particular, the form also has included the provision of termination on national interest and termination of corruption and unlawful or illegal activities respectively under clause 52.0 and 53.0 of the form.

However, these rights of determination need to be accessed strictly according to procedure under the contract since it is mandatory in nature. Therefore any procedure required and stipulated in the determination clause must be followed exactly by the parties<sup>11</sup>. In case of any failure to comply with such procedures, it may result the termination to turn out to be invalid.

Alternatively, if the provision to determine a contract is not included in the contract, the parties may mutually enter into another contract to terminate their existing contract by mutual consent. This should be before all of the obligations have been met. There are two possible situations with regards to this alternative;

- i) Where the contract is executory, the mutual exchange of promises to release one another from future performance will be sufficient consideration, or
- ii) Where the contract is executed, whereby one party has performed, or partly performed their obligations, the other party must provide consideration.

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<sup>11</sup> Fajar Menyensing Sdn Bhd v Angsana Sdn Bhd, (1998) 6 MLJ 80

As conclusion, there are number mechanisms to discharge a contract that can be opted by contracting parties. The mechanism to discharge a contract can be utilized under the principles law under statutory or predetermine under the provision of determination made in the agreement. In case of the parties opt to select to allocate the provision of determination in their agreement, the procedure has to be strictly complied when accessing their right. Any failure to do so, may result the termination to become invalid. Despite of that, the parties also may agree to terminate and discharge a contract by mutual agreement.

## **1.2 Problem Statement**

The general rule provides that parties are obliged to carry out any obligation that they have promised even though performance later becomes not possible.

In *Paradine v Jane*<sup>12</sup>, rule of absolute promises had been imposed in this case. Rule of absolute promise is justified as when a person made a legally binding agreement they cannot simply discharge the obligation from that contract due to events turned out to be differently than what is contemplated by the parties.

The fact of this case is Paradine (Plaintiff) sued Jane (Defendant) for a failure to pay rent for three years on leased lands. Jane insisted in the defense that the lands had been seized and occupied by Prince Rupert of Germany, resulted Jane had been put out of possession and frustrated in the performance of his duties under the lease. Thus Jane was not obliged to perform their obligation which was paying the rent under the contract.

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<sup>12</sup> [1647] EWHC KB J5

In this case, the court held that if the law rather than a party created a duty and the party was unable to perform due to frustration of purpose, that duty would be excused. However if the party created the duty and becomes unable to perform due to frustration of purpose, the law would not protect the party in his own agreement and performance would not be excused. The court held that in this case the lessee would have gained the advantage of the profits and therefore he must bear the risk of the losses. Therefore, Jane was still liable to pay for the rental amount, the rule of absolute promises had been imposed in the verdict saying that when a person made a contract they cannot simply deny their liability from such agreement due to events happened to be differently than expected and rendered the contract to be impossible to perform.

In addition, the performance of a contract must be exact and precise<sup>13</sup>. This rule is addressed as strict performance rule of contract. Under strict rule performance of contract, performance is said should be in accordance with what has been promised in order to discharge the contract obligation. There is a complete discharge of contract when both parties carry out exactly what they promised to do. For instance, contract of sale of purchase only can be discharged once offer is made by the buyer and payment is accepted by the seller.

There is also a circumstance where the performance is not done according to contract which results to breach of contract. However, there is also major problem regards to performance of contract where the impossibility of performance that might be encountered during the honoring period of contract. The impossibility may be triggered by a situation where the obligation cannot be performed due to any default of the parties.

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<sup>13</sup> Chuah Ngah Chin v NG Kie En (1968), 1 MLJ267

Upon that, the contract is said to be frustrated and released the party from any further obligations arise from the impossibility to perform without default of any of them. This circumstance is regarded as frustration of contract under the law provided.

Generally, the doctrine of frustration is first acknowledge in court case of Taylor v Caldwell<sup>14</sup>. In this case, Blackburn J reasoned that the continued existence of the subject matter which was in this case Music Hall in Surrey Gardens, was an implied condition crucial for the existence of the contract. Thus the damage of the music hall was the fault of neither party, and rendered the performance of the contract of the party become not possible. From the mentioned case, it is concluded that the contract may subject to be frustrated and discharged, in event the impossibility of performance resulted from default of neither party.

Event though, the law allows the contract to be rescinded due to default of neither party, to ensure the sanctity of the contract the application of this doctrine need to be strict in view. The judges will have strict interpretation on what render the contract frustrated while making the decision. Over times this doctrine is evolved through cases been trial to courts.

In Malaysia, doctrine of frustration is allocated under provision of Section 57(2) of the Contract Act 1950<sup>15</sup>. This section reads;

*'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, become void when the act becomes impossible or unlawful'*

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<sup>14</sup> 3 B. & S. 826

<sup>15</sup> Contract Act 1950 (Act 136)

From the Act, it reads as the change of circumstance after the creation of the contract that caused impossibility of performance without the default of the parties to the contract, discharged them from further obligation. The Act also does not describe the word impossible in details yet the section envisaged the instance of frustration that result the contract become physically impossible by performance or it becomes impossible to perform due to Act. For instance, in the illustration part of the Act, an example is given that if the parties do contract in such circumstance to discover treasure by magic, the agreement is said to be void and cannot be performed.

Even though the Act has elaborated roughly the instance of frustration, issues encountered regarding the frustration of contract is the grounds that may render the case in point frustrated are too broad to be extinguished. It is not possible to define exactly what comprise a frustrating event since it is highly depend on the subject matter per se. For instance, frustration may be resulted from several reasons such as destruction of subject matter<sup>16</sup>, outbreak of war<sup>17</sup>, non occurrence of particular event<sup>18</sup>, death or incapacity for personal service and many more.

In building contract, the ground that may subject the contract become frustrated can be difficult to find as in building contract most of the risks are being interpreted prior to contract signing. Thus grounds to be the argument that contract can become frustrated could be as random and wide subject on how the contract being interpreted.

A case such Metropolitan Water Board v Dick, Kerr & Co Ltd<sup>19</sup> is among the pioneer that addressed the issue of frustration in building contract. It was held by the judges in

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<sup>16</sup> 3 B. & S. 826

<sup>17</sup> (1949) MLJ 4

<sup>18</sup> (1903) 2 KB 740

<sup>19</sup> (1918) AC 119



this case that the interruptions by the statutory prevention in such character and duration as to make the contract if resumed in effect a radically different contract and resulted the contract to be totally frustrated and unable to perform.

Meanwhile in *Davis Contractor Ltd v Farehan UDC*<sup>20</sup> the contention of the appellants that the contract was frustrated due to shortage of labour and several materials was rejected by the judges and it had been held that the contract was not frustrated only because it become onerous or expensive. The appellants were obliged to perform their duty and in fact they were still able to complete the project after substantial delay.

Due to these uncertainties of the grounds of frustration, it is really critical for the party to ensure that they know and anticipate what make the contract frustrated and void. It is essential to know what render the contract can or cannot be discharged so as those risks could be taken into consideration before the contract is concluded.

On top of that, the current challenging and vulnerable situation of economy and politics in Malaysia for the time being should have been taken seriously by the parties to interpret all their risks in the early negotiation so as it would prevent the abandonment of the contract in the later stage.

Study carried out by Doraisamy et all (2014) cited that one of the reasons of project abandonment is the situation which that are not able to be predicted at the earlier stage, such as the Asian financial crisis which occurred from the year 1997-1998, causing an increase in the cost of building materials which ultimately led to project abandonment in some of the Asian countries.

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<sup>20</sup> (1956) AC 696

In particular, it is clear that due to unexpected event which occur during the contract period resulted the parties to abandon their contract. It is firmed that neither of any parties' negligent caused the project to be stalled. In fact such risks have not been interpreted in the early of the agreement thus it is injustice to force the parties to perform their obligation in such circumstances.

From the above statement, there is a need to really study and consider the condition or event of frustration to avoid dispute and problem in the construction contract. Questions such as, in what circumstances and what is the condition of the contract can be discharged the party from their obligation need to be addressed properly. Could the parties claim the contract obligation can be discharged due to one of the reason of abnormal increase of price? Or it is an induced frustration on behalf of promisor when they are unable to perform the contract due to radical change of price? Has the condition of contract has been utilize at their best that might release the party from his obligation in case of such event?

So, this study will be carried out by looking into the problems related to the above mentioned problems. This study will explain in details doctrine of frustration and the effect of the economic crisis or in case of radical changes of contract price in regards to the Malaysia legal perspective.

### **1.3 Research Objective**

From the problem statements stated above, the objective of the research is to determine whether the contract may be deemed to be frustrated due to abnormal increase of price or economic crisis under Act of Malaysia.

#### **1.4 Scope and Limitation of Research**

The approach of this research is based on the analysis of court cases. The court cases discussed is generally focused on Malaysia court cases. All the contemplated cases referred in this research are related to doctrine of frustration particularly in construction building contract. Despite that, the related cases are narrowed down in scope which is focused on the doctrine of frustration on economic perspective.

The reviewed court cases are limited to cases which is available in the Lexis Nexis website only.

#### **1.5 Significant of the Research**

Construction industry nowadays has become more challenging due to many factors included politics and economics. This circumstance may tremendously affect construction industry in many terms for example one of it is the plaguing of abandonment projects among the parties. The participants in construction industry need to have serious outlook on this issue and better understanding of the problem so that any necessary steps could be taken to overcome the contract and project are being abandoned during the work.

So, this study conducted in hope to increase the awareness and knowledge of both contractors and employers in relation to the issue of frustration of contract subject to the perspective of economic. The findings of this research is also purported to provide a

better understanding to the contractors and the employer of their legal positions related to frustration in construction building contract subject to the perspective of economic.

It is strongly believed that this research can bring lot of benefits especially to contractors who face problems in abandonment project due to financial crisis resulted from unpredicted event during the contract period.

## **1.6 Research Methodology**

The research methodology of this research is basically divided into five (5) phases. The processes are comprised of phase one (1) which is the preparation of research proposal. This research is followed then by phase two (2), the writing of literature review. The following phase is phase three (3) which is all about research methodology. Data collection and analysis are being discussed in the subsequent phase which is phase four (4). The final chapter in this research is phase five (5), is the suggestion of conclusion and recommendation for this research.

Detail of research process will be explained in details in chapter three (3) which is in research methodology section of the research.

## **1.7 Chapter Organization**

This research dissertation is divided into 5 chapters namely as chapter one (I) which is the introductions of the research. It is followed by chapter two (II) that comprised of the literature review of the research. Subsequently, the research consisted of chapter three (III) which explained in detail on research methodology of the dissertation. Chapter four (IV) is about the distribution of data collection and analysis of the research. The final chapter which is chapter five (v) gives details on the conclusion and recommendation of the whole research.

Detail of chapter organization will be explained in details in chapter three (3) which is in research methodology section of the research.

## 1.8 Research Flow Chart

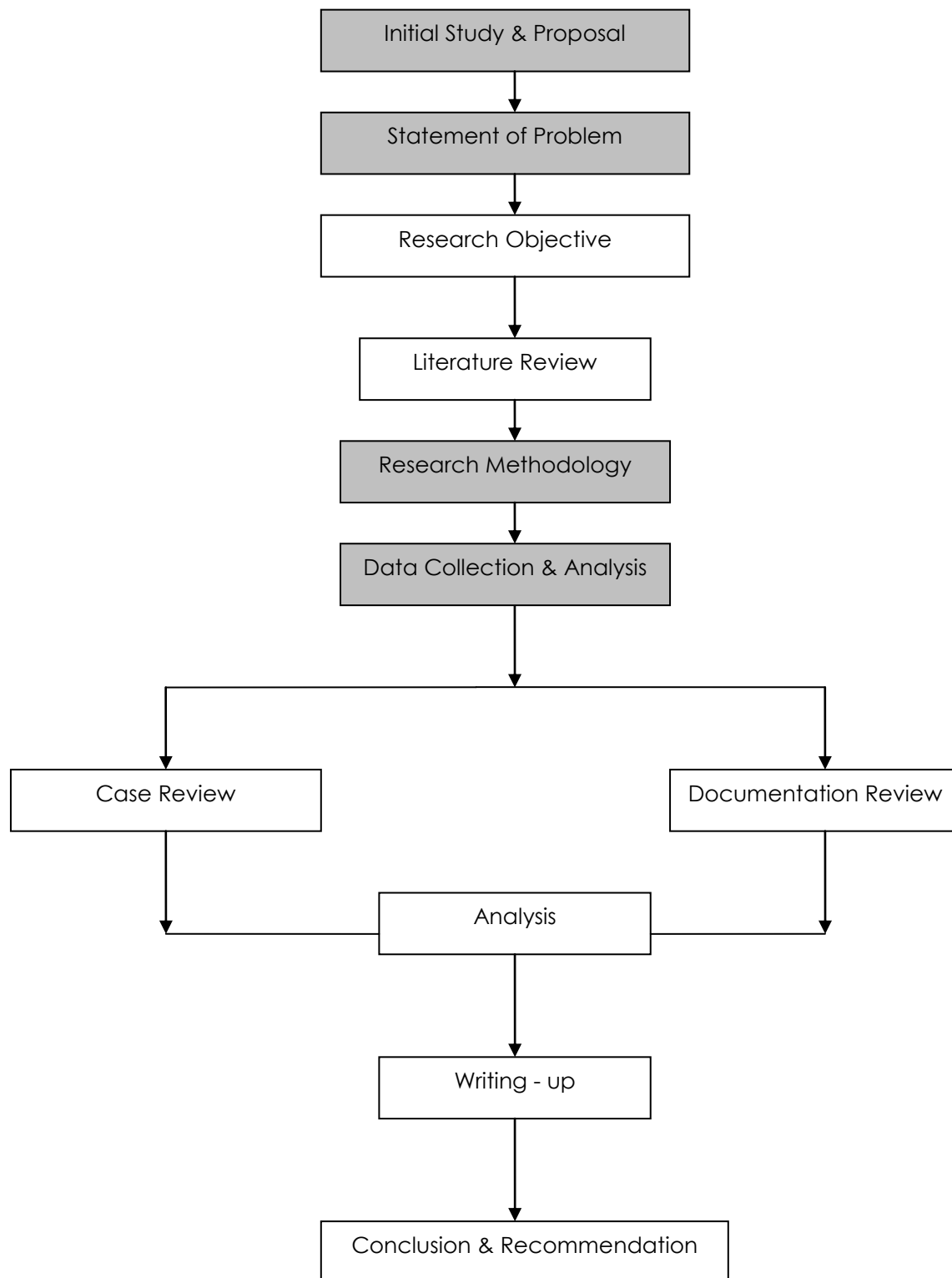


Figure 1.1: Overall Research Flow Chart

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