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Backgrounder

LRC 3—Report on the Need for Frustrated Contracts Legislation in British Columbia

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Contracts may become impossible to perform for a wide variety of reasons beyond the control of contracting parties—reasons such as, for example, war, the destruction of the subject matter of the contract by fire, the enactment of legislation making the performance of the contract illegal, a labour dispute, or the restriction of credit. When these events, or similar events, occur the contract is said to be frustrated. If the contract does not expressly provide for how frustration should be dealt with, then (at the time this report was written) the common-law doctrine of frustration applies. Under this doctrine, a frustrated contract is void from the time of its frustration. This result raises questions about how the parties should be treated in connection with what has gone on prior to the frustrating event. What should happen when one party has paid all or part of the contract price? What should happen if one party has carried out substantially all of its obligations under the contract?

In the view of the commission, the common-law rule does not provide adequate solutions to these issues, and the time has come to consider enacting legislation to address them. In enacting legislation, British Columbia would be following the lead of a number of other jurisdictions in Canada, Australia, and elsewhere. The report considers a Uniform Act, recommended by the Uniform Law Conference of Canada and adopted by a number of provinces, as a model for legislative reform.

After a brief introductory chapter, the report considers the origins and development of the common-law doctrine of frustration in detail. Prior to the mid-nineteenth century, the parties to a contract were considered to be liable to perform their obligations under that contract even if an event that was unforeseeable or beyond the control of the parties occurred and made performance impossible. The rationale for this harsh rule was that the parties could have expressly provided in their contract that their obligations would terminate on the happening of a particular event. In an 1863 judgment, an English court tempered this rule by reading an implied term into a contract involving a series of performances at a music hall. Before the first performance, the music hall burned down. The court reasoned that the parties would never have intended for their obligations to continue in the face of such

an event. Reading in an implied term formed the basis of the original doctrine of frustration, but as the law developed, this rationale was replaced with the view that the courts are acting independently to impose a reasonable solution in cases where a radical change in the obligations of the parties has occurred. The doctrine developed in the English courts, but it was rapidly adopted in Canada and elsewhere. The chapter proceeds to review the application of the doctrine in the courts of British Columbia. After reviewing the origins, development, and application of the doctrine of frustration, the commission then considers some problems related to the doctrine. In particular, the commission notes that the fact that the doctrine does not apply to leases is an obvious defect in need of remedying.

The report goes on to examine various examples of frustrated contracts legislation. It considers in detail the features of legislation in force in England, New Zealand, and the Australian state of Victoria, as well as a Uniform Law Conference of Canada act that has been adopted in a number of Canadian provinces. The report concludes that the Uniform Act provides the best model for British Columbia legislation, but it also notes that there are several problems with that act. These problems are reviewed in detail, along with proposed solutions. In particular, the Uniform Act does not contain a clear set of rules supporting the basic principle that parties to a frustrated contract should be entitled to restitution for the performance or part performance of any contractual obligations. The report gives detailed consideration to specific rules for restitution and apportionment in these circumstances.

Further Developments

See *Frustrated Contracts Act*, S.B.C. 1974, c. 37 (now *Frustrated Contract Act*, R.S.B.C. 1996, c. 166); *Landlord and Tenant Act*, S.B.C. 1974, c. 45, s. 61 (e) (now *Residential Tenancy Act*, S.B.C. 2002, c. 78, s. 92); *Commercial Tenancies Act*, R.S.B.C. 1960, c. 207, s. 34 (now *Commercial Tenancy Act*, R.S.B.C. 1996, c. 57, s. 30).