



**Principles of International Commercial Contracts**  
**Working Group on Long-Term Contracts**  
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**The UNIDROIT Principles of International Commercial Contracts and Long-Term Contracts**

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I. INTRODUCTION

1. The current 2010 edition of the UNIDROIT Principles of International Commercial Contracts (hereinafter: "UNIDROIT Principles" or "Principles"), which consists of 211 Articles – together with accompanying comments – divided into 11 chapters, covers virtually all the most important topics of general contract law, such as formation, interpretation, invalidity including illegality, performance, non-performance and remedies, assignment, set-off, limitation periods, etc. However, while the UNIDROIT Principles can undoubtedly be considered akin to a "general part" of the law governing international contracts of sale and other contracts to be performed at one time, they may not always provide adequate solutions also for so-called long-term contracts or contracts to be performed over a period of time.

2. At its 92<sup>nd</sup> session in May 2013, the Governing Council of UNIDROIT was seized of a Memorandum prepared by the Secretariat concerning possible future work on long-term contracts (cf. UNIDROIT 2013 – C.D. (92) 4(b)). The Memorandum recalled that the UNIDROIT Principles as they now stand already contain a number of provisions which take into account, at least to a certain extent, the special needs of long-term contracts. Yet at the same time the Memorandum pointed out that there are still issues particularly relevant in the context of long-term contracts that the Principles in their present form do not address at all or do so only in part.

3. The Governing Council expressed its appreciation for the Secretariat's Memorandum which provided a useful basis for further examination of the topic and invited the Secretariat to undertake preliminary in-house steps to identify the issues related to long-term contracts that might be given more adequate consideration in a future edition of the UNIDROIT Principles.

4. Following this decision the Secretariat undertook an inquiry among the members and observers of the Working Group that had prepared the 2010 edition of the UNIDROIT Principles as well as other experts who over the years had shown particular interest in the Principles, soliciting additional comments and suggestions as to the proposed work on long-term contracts. All the replies received<sup>1</sup> stressed the importance of the topic which would constitute a useful integration of the current version of the Principles, and welcomed the decision of the Governing Council to recommend it for inclusion in the Institute's Work Programme 2014-2016.

5. At its 93<sup>rd</sup> session in May 2014, the Governing Council was seized by a second Memorandum of the Secretariat containing an analytical survey of the various proposals that had been made concerning specific issues to be addressed in the envisaged work on long-term contracts in the context of the UNIDROIT Principles (cf. UNIDROIT 2013 – C.D. (92) 4(b)). On the basis of this Memorandum the Governing Council decided to instruct the Secretariat to set up a restricted Working Group composed of experts that have shown particular interest in the proposed work on long-term contracts, for the purpose of formulating proposals for possible amendments and additions to the black-letter rules and comments of the current edition of Principles with a view to covering the special needs of long-term contracts. This position paper, which takes into account also the comments and suggestions made by the experts consulted (see Annexes I and II), is intended to provide a basis for the discussion by the Working Group in this respect.

## II. SPECIFIC ISSUES FOR CONSIDERATION BY THE WORKING GROUP

### (a) *Notion of "long-term contracts"*

6. Given the rather vague notion of "long-term contracts", it might be necessary to better define the subject of the envisaged work to be undertaken. The Working Group may wish to move from a broad notion of long-term contracts and consider the contract duration as merely one of the aspects to be taken into account, since other aspects, such as the associative or "relational" nature of most, though not all, long-term contracts, as opposed to the ordinary exchange contracts with instantaneous performance (so-called "discrete" or "one shot" contracts), represent an equally if not even more important feature.

7. If the Working Group considers it advisable better to define the notion of "long-term contracts" it may do so in Article 1.11 which already contains definitions of other key concepts used in the Principles (or possibly in a new provision to be added in Chapter 1), or have the notion of "long-term contracts" defined, whenever appropriate, in the comments to the individual provisions of the UNIDROIT Principles.<sup>2</sup>

8. In the current edition of the UNIDROIT Principles there is no express reference to long-term contracts in the black-letter rules and only three references in the comments, i.e. in Comment 3 Illustration 2 to Article 2.1.6 (acceptance of offer by silence), in Comment 1 to Article 2.1.14 (relating to contracts with terms deliberately left open) and in Comment 5 to Article 6.2.2 (noting that hardship is of particular relevance in the context of long-term contracts).

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<sup>1</sup> Comments were received from Berhooz Akhlaghi (Iran), Christian v. Bar (Germany), Neil Cohen (USA), François Dessemontet (Switzerland), Paul Finn (Australia), Marcel Fontaine (Belgium), Michael Furmston (United Kingdom/Singapore), Arthur Hartkamp (Netherlands), Ole Lando (Denmark), Pilar Perales Viscasillas (Spain), Hilmar Raeschke-Kessler (Germany), Takashi Uchida (Japan), Zhang Yuqin (China), Reinhard Zimmermann (Germany). - Excerpts of some of the comments received are reproduced *infra* as Annex I.

<sup>2</sup> For further considerations in support of one or the other choice, see paragraphs 48 and 49, *infra*.

9. For the sole purpose of laying down different rules on restitution in case of termination, Articles 7.3.6 and 7.3.7 refer to “contracts to be performed at one time” and “contracts to be performed over a period of time” respectively, and Comment 1 to Article 7.3.6 mentions as examples of the former category not only “ordinary sales contracts”, but also “construction contracts in which the contractor is under an obligation to produce the entire work to be accepted by the customer at one particular time [of which] [a] turnkey contract provides an important example”, while Comment 1 to Article 7.3.7 indicates as examples of the second category “leases (e.g. equipment leases), contracts involving distributorship, outsourcing, franchising, licensing and commercial agency, as well as service contracts in general”.

*Qu1: Should the notion “long-term contracts” for the purpose of the UNIDROIT Principles be defined and, if so, how (i.e. defining “long-term contracts” in broad terms so as to cover also “relational contracts” or distinguishing between “long-term contracts” in general and “relational contracts” in particular) and where (e.g. in Article 1.11 or in a new provision to be added in Chapter 1)?*

*Qu2: Should the notions of “contracts to be performed at one time” and “contracts to be performed over a period of time” in Articles 7.3.6 and 7.3.7 respectively, be kept and, if so, what are the differences, if any, between “contracts to be performed over a period of time” and “long-term contracts”?*

*Qu3: Should the reference in Comment 1 to Article 7.3.6 to turnkey contracts as an example of “contracts to be performed at one time” be kept, with the consequence that turnkey contracts would be excluded from the envisaged new black-letter rules and/or comments specifically dealing with long-term contracts?*

*(b) Contracts with open terms*

10. Article 2.1.14, which states that if the parties intend to conclude a contract the fact that they leave a term to be agreed upon in further negotiations or to be determined by a third person does not prevent the contract from coming into existence, is particularly suited to long-term contracts where parties, on account of the duration of the contract and/or the complexity of the subject, often leave open one or more terms because they are unable or unwilling to determine them at the time of the conclusion of the contract. However, the Working Group may wish to expand the Article further.

11. First of all, it was noted (Zimmermann)<sup>3</sup> that the Article does not deal with the standards to be observed by the third person in determining the open term(s) and whether the determination by the third person may be challenged before a court and, if so, on what grounds. Moreover, nothing is said about the procedure to be followed by the third person in his/her determination, i.e. whether it is an adversarial or a non-adversarial procedure.

12. Moreover, it was suggested (Zimmermann)<sup>4</sup> that the case where a third person is appointed by the parties to determine the open term(s) and/or to amend/supplement the terms of the contract whenever appropriate might be distinguished from the case, equally if not even more important in practice, where the function of the third person is merely one of fact finding, i.e. to assess certain facts, mainly of technical nature, which for lack of expertise the parties cannot assess themselves. Thus, while for instance in the Anglo-American legal systems it appears that both functions are generally discussed under the same notion of “expert valuation/certification”, in

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<sup>3</sup> See Annex I, p. viii

<sup>4</sup> *Ibidem*

other systems a distinction is made, at least in case law, e.g. in German law between “*rechtsgestaltendes Schiedsgutachten*” and “*feststellendes Schiedsgutachten*”, in French law between “*arbitrage*” and “*expertise-arbitrage*”, or in Italian law between “*arbitraggio*” and “*perizia contrattuale*”, respectively, to the effect that the first category of third person’s determination may be challenged for “manifest unreasonableness”, while the second category of third person’s determination may as a rule be set aside by a court only if it is based on an erroneous assessment of facts.

13. More in general, the question was raised (Zimmermann)<sup>5</sup> whether it was a good solution to deal with basically the same issue, i.e. contracts with open terms, in two different places, i.e. in Article 2.1.14 and in Article 5.1.7, all the more so since there were no compelling reasons to confine Art. 5.1.7 to the question of price determination. On both points the UNIDROIT Principles differ from other international instruments, and the Working Group might consider adopting the same approach as for instance that most recently taken by the draft Regulation for a Common European Sales Law (CESL).<sup>6</sup>

14. In support of keeping Articles 2.1.14 and 5.1.7 separate, it may be recalled that the main purpose of Article 2.1.14 is to make it clear that, always provided that the parties intend to conclude a contract, even where they leave one or more terms, including essential terms, to be agreed upon by further negotiations, this does not prevent the contract from coming into existence and that, if the parties are unable to reach agreement on the open term(s), the contract does not come to an end “provided that there is an alternative means of rendering the term definite that is reasonable in the circumstances, having regard to the intention of the parties”.

15. Yet even if the two Articles are kept separate, the Working Group may wish to consider mentioning not only in Article 5.1.7 but also in Article 2.1.14 the possibility that the open term(s) is (are) to be determined by one of the parties.<sup>7</sup>

16. The Working Group may also wish to delete paragraphs 2 and 3 of Article 5.1.7 so as to align the Article with the approach taken by Article 5.1.6 as regards the quality of the performance.

*Qu4: Should Article 2.1.14 deal with the standards to be observed by the third person in determining the open term(s) and with the case that the determination by the third person is manifestly unreasonable and, if so, would the solution provided in paragraph 2 of Article 75 CESL (and mutatis mutandis in Article 5.1.7 UNIDROIT Principles) be appropriate?*

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<sup>5</sup> *Ibidem.*

<sup>6</sup> See CESL Article 75 (*Determination by a third party*)

(1) Where a third party is to determine *the price or any other contract term* (emphasis added) and cannot or will not do so, a court may, unless this is inconsistent with the contract terms, appoint another person to determine it.

(2) Where *a price or other contract term* (emphasis added) determined by a third party is grossly unreasonable, the price normally charged or term normally used in comparable circumstances at the time of the conclusion of the contract or, if no such price is available, a reasonable price, or a reasonable term is substituted.

[(3) For the purpose of paragraph 1 a 'court' includes an arbitral tribunal.]

[(4) In relations between a trader and a consumer the parties may not to the detriment of the consumer exclude the application of paragraph 2 or derogate from or vary its effects.]

<sup>7</sup> See also CESL Article 74 (*Unilateral determination by a party*)

Where *the price or any other contract term* (emphasis added) is to be determined by one party and that party’s determination is grossly unreasonable then the price normally charged or term normally used in comparable circumstances at the time of the conclusion of the contract or, if no such price or term is available, a reasonable price or a reasonable term is substituted.

- Qu5: *Should Article 2.1.14 also mention the possibility that the open term(s) is (are) to be determined by one of the parties?*
- Qu6: *Should paragraphs 2 and 3 of Article 5.1.7 be deleted so as to align the Article with the approach taken by Article 5.1.6 as regards the quality of the performance?*
- Qu7: *Should Articles 2.1.14 and 5.1.7 be merged and, if so, where should the new Article be located, i.e. in Chapter 2, Section 1 ("Formation") or in Chapter 5, Section 1 ("Content")?*
- Qu8: *Should the UNIDROIT Principles deal with the case in which the third person is not required to determine a term of the contract but to assess facts and provide that the grounds on which the determination by the third person may be challenged in the two cases are different and, if so, where should this be stated (in Article 2.1.14, in the comments to this Article or in a new Article)?*
- Qu9: *Should the UNIDROIT Principles deal with the question of the procedure to be followed by the third person in determining the open term(s)/in assessing the facts and, if so, what should be the default rule (a non-adversarial procedure or an adversarial procedure) and where should this be stated (black-letter rules or comments)?*

*(c) Agreements to negotiate in good faith*

17. Article 2.1.15 does not affirmatively state a general duty of the parties to negotiate in good faith but merely prohibits negotiations in bad faith. Paragraph 3 specifies that it is bad faith, in particular, where a party enters into or continues negotiations despite its intention not to reach an agreement, and the comments add further examples of negotiations in bad faith, such as where one party has deliberately or by negligence misled the other party as to the nature or terms of the proposed contract, either by actually misrepresenting facts, or by not disclosing facts which, given the nature of the parties and/or the contract, should have been disclosed. However, in view of the fact that long-term contracts are normally concluded after prolonged negotiations and may also in the course of their performance on a number of occasions require (re-)negotiation of individual terms of the contract (see *infra* lit. (e)), the Working Group may wish to consider expanding at least the comments to Article 2.1.15.

18. In particular, the Working Group may wish to deal more in detail with the case that the parties in their contract have expressly agreed on a duty to (re-)negotiate in good faith. At present such a case is only incidentally mentioned in the last paragraph of Comment 2 to Article 2.1.15, but the Working Group might give it further consideration by adding in the comments to Article 2.1.15 a new Comment 4 which, after high-lighting the importance that such agreements to negotiate in good faith have in practice especially in the context of long-term contracts, could indicate in greater detail what specific duties a duty to negotiate in good faith involves so as to provide some guidance to the parties and, in case of dispute, to courts and arbitral tribunals. A first indication of this sort may be found in Comment 5 to Article 6.2.3, i.e. that both parties must conduct the (re-)negotiations in a constructive manner, in particular by refraining from any form of obstruction and by providing all the necessary information. Further specifications may be added, such as *[to be selected by the Working Group]*: keeping to the negotiation framework set out by the agreement, respecting the remaining provisions of the contract, showing willingness to reach a compromise, making concrete and reasonable suggestions for solutions/adjustments instead of mere generic declarations of willingness to find a solution, maintaining flexibility in the conduct of negotiations, giving appropriate reasons for one's own suggestions as to possible solutions/adjustments, obtaining expert advice in difficult and complex consensus proceedings, responding promptly to proposals

from the other side, avoiding an unfair advantage or detriment to the other side, maintaining efforts to reach agreement over an appropriate length of time, avoiding unnecessary delays in the consensus proceedings, etc. In addition the proposed Comment 4 could mention the remedies available in case of breach of an agreement to negotiate in good faith, i.e. all the remedies for breach of contract, including the right to performance (as currently stated in the last paragraph of Comment 2 to Article 2.1.5).

*Qu10: Should in the comments to Article 2.1.15 a new Comment 4 be added dealing with the case that the parties have expressly agreed on a duty to (re-)negotiate in good faith either in general terms as a first step in resolving disputes and/or with respect to particular contingencies (e.g. in case of hardship, force majeure; etc.) and, if so, should Comment 4 indicate some specific duties deriving from such a duty to (re-)negotiate in good faith, and the available remedies in case of breach?*<sup>8</sup>

*(d) Contracts with evolving terms*

19. In view of the fact that most long-term contracts are “evolutionary” in nature, i.e. require adaptations in the course of performance, it was noted (Finn)<sup>9</sup> that, even where the parties address at length what are to be the terms of their contract, their conduct over time often deviates from those terms and for quite good reasons in some instances. Likewise, what the actual contract between the parties is, can from time to time be quite controversial, especially when the parties themselves acknowledge that their contract is an evolving one which is likely to require additional clauses, re-negotiation etc. but what already has been agreed and what needs to be, or remains to be, agreed is disputed between the parties.

20. It was noted (Fontaine)<sup>10</sup> that a first answer to these questions may be found in acknowledging the particular importance of Article 4.3 UNIDROIT Principles and the reference therein contained to “practices which the parties have established between themselves” and to “the conduct of the parties subsequent to the conclusion of the contract” as a means of interpretation of

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<sup>8</sup> Thus Comment 4 could open with a statement that especially in case of long-term contracts, which are normally concluded after prolonged negotiations and which also in the course of their performance on a number of occasions require (re-)negotiation of individual terms of the contract, parties may wish to go beyond the mere prohibition to negotiate in bad faith laid down in the present Article and affirmatively state in their contract a duty to negotiate in good faith. If they do so, two questions arise: what specific duties derive from such a duty to negotiate in good faith, and what the remedies available in case of breach are. As to the first question, the parties will certainly have to conduct the (re-) negotiations in a constructive manner, to refrain from any form of obstruction and provide the necessary information (see Comment 5 to Article 6.2.3). Additional specifications of the duty to negotiate in good faith are, among others [*to be agreed by the WG*], keeping to the negotiation framework set out by the agreement, respecting the remaining provisions of the contract, showing willingness to reach a compromise, making concrete and reasonable suggestions for solutions/adjustments instead of mere generic declarations of willingness to find a solution, giving appropriate reasons for one’s own suggestions as to possible solutions/adjustments, obtaining expert advice in difficult and complex consensus proceedings, responding promptly to proposals from the other side, avoiding an unfair advantage or detriment to the other side, maintaining efforts to reach agreement over an appropriate length of time, avoiding unnecessary delays in the consensus proceedings, etc. As to the available remedies in case of breach of the duty to negotiate in good faith, they are all the remedies for breach of contracts, including the right to performance [*so at present the last paragraph of Comment 2 to Article 2.1.15 and Illustration 4, which will have to be deleted there and added here*].

<sup>9</sup> See Annex I, p. v.

<sup>10</sup> See Annex I, p. vii.

long-term contracts. In this respect, it was pointed out (Cohen)<sup>11</sup> that because these contracts by their very nature involve repeated performance (and repeated opportunity for a party to object if that party is displeased), conduct occurring after the conclusion of a contract can provide the basis for inferences as to what the parties believe their obligations are and, thus, can be a useful tool in contract interpretation.

21. Yet also Article 5.1.1 by stating that the parties' obligations are not limited to those expressly stipulated in the contract but may also be implied, and Article 5.1.2, by specifying that "[i]mplied obligations stem from (a) the nature and purpose of the contract; (b) practices established between the parties and usages; (c) good faith and fair dealing; (d) reasonableness", may become relevant in this respect.

22. Moreover, it was noted (Fontaine)<sup>12</sup> that in particularly complex long-term contracts with more than two parties involved the parties may wish to set up a permanent structure, such as a "contract management committee", dedicated to following the evolution of the contract over time and to suggesting possible adaptations thereof that may appear advisable, even beyond major disturbances such as *force majeure* or hardship (for a somehow similar proposal see paragraph 30, *infra*).

23. Finally, it was recalled (Cohen)<sup>13</sup> that because parties to a long-term contract are well-aware that the background conditions that give rise to the relationship may well change over time, long-term contracts are more likely to incorporate external standards, either to measure performance or to determine payment. Such external standards, because they can change with changing circumstances, can be very useful, but they can also produce significant difficulties if those standards become missing or inappropriate with the passage of time.

24. Article 5.1.7 (4), which provides that "[w]here the price is to be fixed by reference to factors which do not exist or have ceased to exist or to be accessible, the nearest equivalent factor shall be treated as a substitute", addresses the issue, at least in part, with respect to price determination. The Working Group may wish to consider adding a similar provision in Article 5.1.6 on the determination of the quality of performance, and expanding Comment 4 to Article 5.1.7 (as well as a corresponding Comment 3 to be added in the comments to Article 5.1.6) so as to explain more in detail the relevance and possible (mis-)functioning of external standards referred to by the parties to long-term contracts to measure performance and/or determine payment.

*Qu11: Should a new paragraph be inserted in the comments to Article 4.3 stating that the criteria listed in this Article may have particular relevance in the context of long-term contracts?*<sup>14</sup>

*Qu12: Should a new paragraph be inserted in the comments to Article 5.1.2 stating that the criteria listed in this Article may have particular relevance in the context of long-term contracts?*

*Qu13: Should the UNIDROIT Principles suggest<sup>15</sup> that parties to particularly complex long-term contracts set up a "contract management committee" dedicated to monitoring the evolution*

<sup>11</sup> See Annex I, p. ii.

<sup>12</sup> See Annex I, p. vii.

<sup>13</sup> See Annex I, p. ii.

<sup>14</sup> The new paragraph could be framed along the lines set out in paragraph 20 of the text.

<sup>15</sup> In making this or any other suggestion to the parties, one could choose among three different kinds of suggestion: the strongest kind of suggestion would be a statement that the parties "should" take a particular course of action; an intermediate kind of suggestion could be expressed by the words "it is advisable" or "desirable" that the parties adopt a particular course of action; the weakest kind of

*of the contract and to suggesting possible adaptations thereof, and if so, should this be done in a black letter rule (e.g. Article 5.1.2) or only in the comments (e.g. to Article 5.1.2)?*

*Qu14: Should the UNIDROIT Principles address the issue of a reference by the parties to long-term contracts to external standards to measure the quality of performance and/or to determine the price and, if so, could Article 5.1.7(4) (and a corresponding new paragraph in Article 5.1.6), together with expanded comments, provide a first answer to it?*

*(e) Supervening events*

25. The UNIDROIT Principles grant only in case of hardship the aggrieved party the right to request renegotiation of the contract with a view to adapting its terms to the changed circumstances (see Article 6.2.3 (1)), while in case of *force majeure* the party affected by the supervening impediment may only invoke it as an exception with a view to its non-performance being excused either permanently or temporarily, depending on whether the impediment is of a permanent or only temporary nature (see Article 7.1.7). Significantly enough, however, Comment 4 to Article 7.1.7, after recalling that “[i]nternational commercial contracts often contain much more precise and elaborate provisions in this regard”, openly invites the parties to adapt, whenever appropriate, the content of this Article so as to take account of the particular features of their transaction. Especially with respect to long-term contracts, where normally neither party would have an interest in terminating a relationship that may have lasted for years and/or involved large investments, it may be argued that also for the case of *force majeure* the parties are well advised to make in their contract provision for the continuation, whenever possible, of their business relationship, and to envisage termination only as a last resort.

26. A first device to this effect would be expressly to provide in the contract that, except where it is clear from the outset that the impediment is of a permanent nature, the obligation(s) of the party affected by the *force majeure* are suspended for a fixed period of time or for a “a reasonable time”, and that the other party may terminate the contract only at the end of a fixed period of time (e.g. 30 days, one year, etc.) after receiving notice of the impediment.

27. Moreover, the contract may expressly state the duty of the party affected by the impediment (or of both parties) to make all reasonable efforts to eliminate or overcome the impeding event or its consequences. It may be argued that such duty is already implicit in the very definition of *force majeure* in Article 7.1.7(1) (“[...] impediment beyond [the party’s] control and that [the party] could not reasonably be expected [...] to have [...] overcome it or its consequences”) and also follows from the general duty to mitigate loss in accordance with Article 7.4.8, but an explicit statement to this effect in the contract would certainly be more effective.

28. Finally, and most importantly, parties may wish expressly to provide in their contract that in case the impediment persists even after the expiry of a fixed time limit they shall enter into negotiations in good faith with a view to adapting the contract to the changed circumstances and that termination should be permissible only if those negotiations do not lead to any agreement within a certain period of time.

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suggestion would be by using language such as “the parties may wish to provide in their contract” or “the contract might contain [a particular provision]”. In the context of the Principles the second and third kind of suggestion would appear to be more appropriate.



29. Apart from *force majeure* cases, in the course of the performance of long-term contracts there may be a number of other occasions where the parties have to face unexpected situations and/or resolve disagreements or veritable disputes about their respective obligations under the contract. The question was raised (Zimmermann)<sup>16</sup> whether the UNIDROIT Principles should suggest that also for such cases the parties provide in their contract that they should first engage in negotiations in good faith and, should they fail to reach a satisfactory solution within a given period of time, that they should try to settle the dispute by mediation conducted by a qualified third person before resorting to arbitral or judicial proceedings.

30. In addition or alternatively, the parties may provide in their contract for the establishment of a so-called “dispute review board”, i.e. a permanent body composed of one or three persons with special expertise, with the task of aiding the parties in resolving their disagreements and disputes by issuing either mere recommendations or making veritable decisions which the parties have contractually agreed to accept as binding under specific conditions.

*Qu15: Should the UNIDROIT Principles suggest that the parties to long-term contracts expressly provide in the contract that in case of force majeure, except where it is clear from the outset that the impediment is of a permanent nature, the obligation(s) of the party affected by the force majeure is(are) suspended for a fixed period of time (or for “a reasonable time”), and that the other party may terminate the contract only at the end of a fixed period of time after receiving notice of the impediment, and, if so, should this be stated in the black-letter rule of Article 7.1.7 or in the comments (e.g. after Comment 4)?*

*Qu16: Should the UNIDROIT Principles suggest that the parties to long-term contracts expressly provide in the contract that in case of force majeure the party affected by the impediment (or both parties) is (are) under a duty to make all reasonable efforts to eliminate or overcome the impeding event or its consequences and, if so, should this be stated in the black-letter rule of Article 7.1.7 or in the comments (e.g. after Comment 4)?*

*Qu17: Should the UNIDROIT Principles suggest that the parties to long-term contracts expressly provide in the contract that in case of force majeure, if the impediment persists even after the expiry of a fixed time limit, the parties shall enter into negotiations in good faith with a view to adapting the terms of the contract so as to permit the continuation of their ongoing relationship before resorting to other remedies such as withholding performance or termination and, if so, should this be stated in the black-letter rule of Article 7.1.7 or in the comments (e.g. after Comment 4)?*

*Qu18: Should the UNIDROIT Principles suggest that the parties to long-term contracts expressly provide in the contract that any disagreement or veritable dispute that may arise in the course of its performance should be settled by negotiation in good faith and, if they cannot reach a satisfactory solution within a given period of time, that they should try to settle the dispute by mediation before resorting to arbitral or judicial proceedings and, if so, would it be sufficient to make such suggestions in the comments (e.g. in a new Comment 5 to Article 2.1.15)?*

*Qu19: In addition or alternatively, should the UNIDROIT Principles suggest the establishment of special “dispute review boards” and, if so, would it be sufficient to make such suggestion in the comments (e.g. in a new Comment 6 to Article 2.1.15)?*

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<sup>16</sup> See Annex I, p. viii.

(f) *Co-operation between the parties*

31. It was pointed out (Finn)<sup>17</sup> that the duty of co-operation between the parties in the course of the performance of the contract is particularly relevant in the context of long-term contracts. Since Article 5.1.3 states the duty of co-operation only in general terms, there might be the need to elaborate it further, either in the black-letter rule or in the Comments.

32. With respect to the black-letter rule, the Working Group may wish to consider adding a new paragraph along the lines of Article 7.4.8 (2), addressing the issue of possible reimbursement of the expenses incurred by a party in actively assisting the other party in the performance of its obligations under the contract.

33. With respect to the comments, one might consider splitting the present single Comment to Article 5.1.3 into two separately numbered comments, i.e. Comment 1 indicating the relevance of the duty of co-operation for all kinds of contracts including ordinary exchange contracts with instantaneous performance, and Comment 2 pointing out the special importance of that duty in the context of long-term contracts.

34. Comment 1 could open with the statement that the duty of co-operation constitutes an application of the general principle of good faith and fair dealing as stated in Article 1.7, and that its most significant instances are expressly or impliedly provided for in the Principles either in the black-letter rules (see Article 5.3.3 (*Interference with conditions*), Article 7.1.2 (*Interference by the other party*), and Article 7.4.8 (*Mitigation of harm*) or in the comments (see e.g. Comment 3(a) to Article 6.1.14 concerning the duty to assist the other party in obtaining a public permission, and Comment 10 to Article 7.1.4 concerning the aggrieved party's duty to permit the non-performing party's cure of the non-performance). In this context one might also consider to moving Illustration 1 in the Comment to Article 5.1.3 to Comment 1 to Article 7.1.2.

35. Comment 2, in stressing the special importance of the duty of co-operation in the context of long-term contracts, could refer to some particularly significant examples in this respect, such as e.g. the duty of the purchaser in contracts for the construction of industrial works to provide the contractor with certain types of information relevant to its performance (e.g. information concerning safety or environmental laws in force in the country of the purchaser) and to co-operate in other ways with the contractor (e.g. by storing the contractor's equipment or materials), or, in case of an inter-firm agreement, the duty of the individual member firms not to interfere with each other's professional practice (e.g. by seeking to hire the other's personnel, etc.), or, with respect to all kinds of long-term contracts, the duty to produce documents and other information that are necessary to enable the other party to apply for required public permissions or avoid financial penalties under governmental export and foreign currency regulations, etc.

*Qu20: Should the parties' duty of co-operation as stated in general terms in Article 5.1.3 be further elaborated with reference to long-term contracts and, if so, should a new paragraph along the lines of Article 7.4.8 (2) be added to Article 5.1.3, addressing the issue of the possible reimbursement of the expenses incurred by a party in actively assisting the other party in the performance of its obligations under the contract?*

*Qu21: Should the comments to Article 5.1.3 be expanded so as to highlight the particular importance of the duty to co-operation in the context of long-term contracts and, if so, by splitting the present single comment into two separately numbered comments, i.e. Comment 1 indicating the relevance of the duty of co-operation for all kinds of contracts*

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<sup>17</sup>

See Annex I, p. v.

*and Comment 2 pointing out the special importance of that duty in the context of long-term contracts?*

*(g) Restitution after ending contracts entered into for an indefinite period*

36. Though rather rare, there are cases where the duration of long-term contracts is neither determined nor determinable, or where the parties have stipulated that their contract is concluded for an indefinite period. For all these cases Article 5.1.8 provides that the contract may be ended by either party by giving notice a reasonable time in advance. However, granting the parties such a unilateral right to put an end to the contract may not be sufficient and it might be advisable to provide, analogously to Article 7.3.7, that once the contract has been ended restitution for past performances is excluded.

*Qu22: Should Article 5.1.8 be amended so as to make it clear that once a contract for an indefinite period has been ended restitution for past performances is excluded? Or would a statement in the comments that as far as restitution is concerned the rules laid down in Article 7.3.7 apply with the necessary adaptations be sufficient?*

*(h) Implementation by a group of linked contracts*

37. It was recalled (Fontaine)<sup>18</sup> that long-term contractual arrangements are often implemented by means of a group of linked contracts, either simultaneous (e.g. distinct contractual arrangements about financing / technical assistance / insurance) or successive (e.g. a basic framework contract to be implemented by the future conclusion of specific contracts).

38. In this context a first aspect worth mentioning relates to the case where, as is often the case in practice, the parties make a reference to links with other contracts in the recitals of the main contract. One might consider to advise the parties that such a generic reference in the recitals remains normally without any legal effect. If the parties intend to create any sort of legal linkage between the various contracts, e.g. by making the entry into force or the performance of (some of) them a suspensive condition for entry into force of the main contract, they should clearly state this not in the recitals but in the body of the main contract, e.g. in a special provision on “closing” (see Comment 5 to Article 5.3.1).

39. More importantly, whenever the main contract (e.g. a works contract) permits one of the parties (e.g. the contractor) to subcontract the performance of (some of) its obligations, it is highly recommendable for the provisions of the main contract and of those of the subcontract to be in harmony so that the scope, quality and timing of the work to be performed by the subcontractor fulfil the obligations of the subcontracting party under the main contract.

40. Likewise, in complex operations such as the various types of privately financed infrastructure projects (BOT, BTO, BROT, BOOT, DBO, etc.) which involve a number of interrelated contractual arrangements among the participants (project or concession agreement, off-take agreement, construction agreement, operation and maintenance contract, insurance contracts, financing contracts, etc.) defining the respective rights, obligations and risks of each party, it is of the utmost importance that at least key provisions such as the *force majeure*, choice-of-law and dispute resolution clauses be consistent throughout all contracts to the maximum extent possible.

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<sup>18</sup> See Annex I, p.vii.

*Qu23: Should the UNIDROIT Principles address the issue of long-term contracts implemented by means of a group of linked contracts and, if so, would it be sufficient to do so in the comments (e.g. in a new Comment X to Article Y) along the lines set out in paragraphs 38 to 40 of the text?*

(i) *Termination for cause*

41. The UNIDROIT Principles do not address the question as to whether, and if so to what extent, parties to long-term contracts are entitled, even in the absence of any special provision to this effect in the contract, to terminate their contract for irreparable breakdown of their mutual trust and confidence (so-called "termination for cause"). Especially relational contracts, i.e. long-term contracts that give rise to a more or less enduring relationship based on trust and confidence between the parties and on an ongoing duty to cooperate, are subject not only to the usual risks of a breach by one of the parties or of supervening events making performance impossible or excessively more onerous, but also to the risk of an irreparable breakdown of the parties' mutual trust and confidence making the continuation of their relationship, at least for one of the parties, no longer sustainable. Of course, when entering into contracts of this kind, the parties are well advised to address the issue, and indeed in actual practice frequently do so by so-called termination clauses which define the contingencies in which the contract may be terminated for such a particular cause and specify how the right to terminate may be exercised (e.g. by mere notice to the other party or by a court decision), whether termination takes effect immediately or only after a certain period of time, whether the terminating party or the other party is entitled to damages, etc. However, a problem arises when the contract is silent on this issue and it may be argued that the UNIDROIT Principles, like a number of domestic legislations (e.g. § 314 of the German Civil Code (as amended in 2001))<sup>19</sup> should include default rules on termination of long-term contracts for cause.

42. The topic of termination for cause had already been extensively discussed by the Working Group entrusted with the preparation of the 2010 edition of the UNIDROIT Principles,<sup>20</sup> and the decision of that Working Group not to pursue the work on that topic was mainly due to lack of time rather than to the opinion that the drafting of a rule in that respect might not be necessary or feasible. Among the experts consulted with a view to soliciting comments and suggestions in relation to the proposed work on long-term contracts (see paragraph 4 *supra*), there was strong support for the proposal to include the topic of termination for cause among those to be addressed in the envisaged new edition of the UNIDROIT Principles and, significantly enough, such support was

<sup>19</sup> § 314 BGB  
*Kündigung von Dauerschuldverhältnissen aus wichtigem Grund*

(1) Dauerschuldverhältnisse kann jeder Vertragsteil aus wichtigem Grund ohne Einhaltung einer Kündigungsfrist kündigen. Ein wichtiger Grund liegt vor, wenn dem kündigenden Teil unter Berücksichtigung aller Umstände des Einzelfalls und unter Abwägung der beiderseitigen Interessen die Fortsetzung des Vertragsverhältnisses bis zur vereinbarten Beendigung oder bis zum Ablauf einer Kündigungsfrist nicht zugemutet werden kann.

(2) Besteht der wichtige Grund in der Verletzung einer Pflicht aus dem Vertrag, ist die Kündigung erst nach erfolglosem Ablauf einer zur Abhilfe bestimmten Frist oder nach erfolgloser Abmahnung zulässig. § 323 Abs. 2 findet entsprechende Anwendung.

(3) Der Berechtigte kann nur innerhalb einer angemessenen Frist kündigen, nachdem er vom Kündigungsgrund Kenntnis erlangt hat.

(4) Die Berechtigung, Schadensersatz zu verlangen, wird durch die Kündigung nicht ausgeschlossen.

[For an English translation of the provision see Annex II, p. ix, Fn 1].

<sup>20</sup> On that occasion the Working Group was seized by two preparatory documents by Professor François Dessemontet (cf. UNIDROIT 2007 – Study L – Doc.104 and UNIDROIT 2009 – Study L – Doc.109, excerpts of the latter are attached hereto as ANNEX II).

expressed not only from experts from civil law systems but also from experts from common law systems. Reference was made, among others, to a recent Australian decision concerning the winding up of a long-term business relationship between an Australian manufacturer and a Singapore distributor, which openly denounced the inadequacy of Australian law in dealing with cases of breakdown of mutual trust and confidence between the parties to long-term contracts.<sup>21</sup>

*Qu24: Should the UNIDROIT Principles deal with termination of long-term contracts for cause and, if so, is the topic suitable to be the subject of new black-letter rules or should it merely be addressed in the comments (which)?*

*Qu25: Would it be desirable and feasible to define the notion of "cause" and to distinguish it from other supervening events that according to the UNIDROIT Principles may lead to the termination of the contract, i.e. hardship (see Articles 6.2.2-6.2.3); force majeure (see Article 7.1.7); fundamental non-performance (see Article 7.3.1)?*

*Qu27: Should termination for cause take place by mere notice by one party to the other party(ies) or should it require a court intervention and when does it take effect in the two cases?*

*Qu28: What is the relationship between termination for cause and damages?*

*Qu29: What are the effects of termination for cause by one or some of the parties to a multi-party contract?*

*(j) Post-contractual obligations*

43. It was pointed out (Fontaine)<sup>22</sup> that the UNIDROIT Principles only marginally referred to post-contractual obligations. In fact, Art. 7.3.5 (3) merely states that "[t]ermination does not affect any provision in the contract for the settlement of disputes or any other term of the contract which is to operate even after termination". In view of the fact that in the context of long-term contracts the issue of post-contractual obligations is definitely more complex, the Working Group may consider dealing with it in a more detailed manner.

44. To begin with, long-term contracts after termination often leave behind situations that have to be settled between the parties in one way or another. For instance, with respect to distributorship contracts, what should be done with unsold stock in possession of the distributor and what with outstanding orders? Or, with respect to agreements for the transfer of technology, is the transferee at the expiry of the contract bound to return the various documents (guides, plans, etc.) it had received from the transferor? Likewise, in case of works contracts terminated prematurely, what is the fate of the unfinished works, i.e. who – the contractor/the purchaser – is to take the measures necessary to protect the unfinished works and/or clean up the site, and who is to bear the cost?

45. However, in addition to obligations in relation to the winding up of the past relationship, there may also be obligations of the parties that existed before the end of the contract and extend into the future for a certain period of time. Two typical examples of this kind of post-contractual obligations – both particularly frequent with respect to employment contracts, distribution agreements, licensing agreements, contracts for the transfer of technology and subcontracts in general – are the prohibition for one of the parties to divulge confidential information received from the other party, or a covenant to restrain it from various forms of competition, not only for the

<sup>21</sup> Cf. *Australian Medic-Care Company Ltd v Hamilton Pharmaceutical Pty Limited* (per Justice Finn).

<sup>22</sup> See Annex I, p. vii.

duration of the contract but also for a certain period after its termination. Other cases of post-contractual obligations are guarantee obligations of the contractor for the construction in its entirety or for single parts of it lasting for a period of time after completion longer than that provided for by the applicable domestic law, the obligation of the concessionaire of a public infrastructure to transfer after the expiry of the concession certain technology or know-how required to operate the infrastructure facility to the contracting authority, the commitment of one of the parties that in case it decides to enter into any new agreements of the same kind to do so with the same party or at least to give that party first refusal, etc.

46. It is true that at least some post-contractual obligations may be considered to be implied terms of the agreement, i.e. to follow from the very nature or type of contract in question, but the Working Group may wish to expand Comment 3 to Article 7.3.5 by suggesting that the parties state expressly in their agreement what specific obligations, if any, should survive the termination of the contract, whether they are binding only for one or for both of the parties, what their precise content is, what the remedies are, if any, in case of breach, etc. The parties may also be advised that their freedom of contract in this respect might be limited by applicable mandatory provisions of domestic law (e.g. by those prohibiting covenants in restraint of competition if they have not certain geographical and temporal limitations).

*Qu30: Should Comment 3 to Article 7.3.1 be expanded and suggest that parties to long-term contracts expressly state in their contract whether they shall be bound by post-contractual obligations either relating to the winding-up of their relationship or intended to survive the termination of the contract for a certain period of time, and, if so, specifically to address issues, such as the precise content of the obligations, whether they are binding on one or both of the parties, what are the remedies, if any, for breach, their compatibility with applicable mandatory domestic rules, etc. ?*

### III. RELEVANCE TO BE GIVEN TO THE PROPOSED ADDITIONS AND/OR AMENDMENTS TO THE BLACK-LETTER RULES AND/OR COMMENTS OF THE EXISTING EDITION OF THE UNIDROIT PRINCIPLES TO TAKE INTO ACCOUNT THE SPECIAL NATURE AND NEEDS OF LONG-TERM CONTRACTS.

47. After agreeing on the additions and/or or amendments to be made to the black-letter rules and/or comments of the existing edition of the UNIDROIT Principles to take into account the special nature and needs of long-term contracts, the Working Group may wish to consider the relevance to be given to such additions and amendments in the new edition of the Principles.

48. A first possibility is to make such additions and/or amendments in the appropriate locations throughout the text of the Principles without any further reference to them elsewhere, except perhaps by means of special entries in the subject-matter index.

49. A second possibility is to provide a definition of long-term contracts in general and relational contracts in particular in Article 1.11 which already contains definitions of other key concepts used in the Principles (see paragraph 7 and Qu1 *supra*), and to add in the comments to Article 1.11 a new Comment 5 with cross-references to the Articles and/or Comments where the additions/amendments in question have been made. Such an approach would permit to high-light the fact that the new edition of the Principles gives due consideration to the special needs of long-term contracts and to provide from the outset an overview of where this has been done (for a similar approach see Comment 1 to Article 1.7 with respect to the numerous applications of the general principle of good faith and fair dealing throughout the Principles). Moreover, this approach would permit to make in the same Comment 5 to Article 1.11 also a reference to the Articles and/or Comments of the current edition of the Principles which are either expressly or impliedly relevant to long-term contracts.

**COMMENTS AND SUGGESTIONS**

by

Professor Neil B. Cohen  
Justice Paul Finn  
Professor Marcel Fontaine  
Professor Reinhard Zimmermann

## Professor Neil B. Cohen

Long-term contracts have great economic importance but, until surprisingly recently, they have not been the subject of serious academic attention (particularly in the United States, where I have greater familiarity with the literature). The work of Stewart Macaulay and Ian Macneil on relational contracts stands out, as do several studies of price adjustment in long-term contracts.

Despite the dearth of interest in the subject, it is clear that long-term contracts play a fundamentally different business and economic role than “one-shot” contracts involving a single exchange at a single time. Indeed, if one were to describe the difference using metaphor, it could be said that the difference between a one-shot contract and a long-term contract is the difference between a trade and a marriage. After all, the contrast is between, on one hand, an isolated one-time exchange between parties who may be strangers to each other and, on the other hand, an extended relationship involving performance and payment diffused over time and over several installments with some degree of mutual interdependence between the parties.

While long-term contracts play a very different role than do one-shot contracts, there is general agreement that the same basic structure of contract law applies to them. The argument is not that they are entirely different species of interrelationship requiring an entirely different set of rules. Rather, it is that there are enough important differences between long-term contracts and contracts for a single exchange to justify, in appropriate circumstances, either special versions of existing rules or special rules not relevant to single exchanges. Indeed, it is no longer seriously argued that the general body of contract law, designed for single exchanges, fits long-term contracts with no need for adjustment or supplementation. Thus, the question is not whether a system of contract law should have *any* rules that are customized for long-term contracts but, rather, which such rules are needed and how distinctive they should be.

In resolving that question, it is necessary to identify ways in which long-term contracts differ from standard contracts. An illustrative, and necessarily incomplete, list would include the following:

1. Because they involve repeated performance (and repeated opportunity for a party to object if the party is displeased), conduct occurring after the conclusion of a contract can provide the basis for inferences as to what the parties believe their obligations are and, thus, can be a useful tool in contract interpretation.
2. Because parties to a long-term contract are well-aware that the background conditions that give rise to the relationship are likely to change over time, long-term contracts are more likely to incorporate external standards, either to measure performance or to determine payment. Such external standards, because they can change with changing circumstances, can be very useful. On the other hand, they can produce significant difficulties if those standards become missing or inappropriate with the passage of time.
3. Alternatively, the parties may deal with the likelihood of change in background conditions over time in a very different manner – by leaving important contract terms open for future agreement, or to be set by one of the parties.
4. In a long-term contract, the value of what one party is to receive from the other may decrease in unanticipated ways over course of the contract:
  - a. From the perspective of a party paying money for goods, services, or other consideration, the value of that performance to the payer may diminish in ways not predicted by the parties.
  - b. From the perspective of a party providing goods, services, or other consideration in exchange for the payment of money, the value of that payment may diminish unpredictably (e.g., from inflation or currency devaluations).
5. Conversely, the value of what one party is to receive from the other may increase in an unanticipated way, resulting in the possibility of windfall.
6. Over the course of a long-term contract, the burden of a party’s agreed performance may increase beyond the range predicted or anticipated:



- a. The burden of providing goods, services, or other non-monetary consideration may increase (reasons may include, for example, changed market conditions or differing technological or regulatory constraints)
  - b. Alternatively, payment of the agreed price by the paying party may become more difficult over time, either as a result of market conditions or factors unique to that party.
7. One of the parties to a long-term contract may become unreliable, or be seen by the other party as unreliable, raising the prospect of future non-performance even before the occurrence of any actions constituting breach of the contract.
  8. After a passage of long period of time, provisions agreed to in the distant past that made sense at the time may seem silly or bizarre (or unfairly surprising) when unearthed many years later.

Parties to long-term contracts may have a variety of reactions to the problems resulting from those differences from short-term single performance contracts. In some cases, for example, one or both parties may seek relief from such problems in a variety of ways, such as by seeking reformulation (or reformation) of the contract, either by agreement or by judicial fiat, or seeking to end the contract early.

Alternatively, parties may seek judicial remedies when problems arise. Remedies can be difficult to devise, however, if their logic requires either a prediction of future conditions or re-creation of conditions of the distant past.

The current edition of the UNIDROIT Principles does not separately address long-term contracts, but it does not ignore them completely. Three provisions of the UNIDROIT Principles explicitly refer to long-term contracts. All three references however, are in the comments rather than in the Principles themselves. The three provisions in which reference is made are:

- Article 2.1.6, Comment 3 Illustration 2 (acceptance of offer by silence)
- Article 2.1.14, Comment 1 (relating to contracts with terms deliberately left open)
- Article 6.2.2, Comment 5 (noting that hardship rules are most relevant in the context of long-term contracts)

While these provisions contain the only three explicit references in the UNIDROIT Principles to long-term contracts, several other provisions relate specially to, or are particularly relevant to, long-term contracts. An example is provided by Article 6.2.2, which addresses situations in which the occurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party receives has diminished. Such examples can be found throughout the Principles.

What should be done in light of the significance of long-term contracts, their characteristics that distinguish them from one-shot contracts, the problems unique to them, and the lack of systematic treatment of them in the Principles?

One possibility was provided by Professor Dessemontet in the paper he prepared in conjunction with the development of the 2010 edition of the Principles. Professor Dessemontet suggested an innovative addition to the Principles that could apply to long-term contracts – termination for just cause. Under this view, a long-term contract “may be terminated for just cause by either party at any time, in exceptional circumstances.” Just cause, it was stated, results from a change in circumstances “if continuation of the contract cannot reasonably be expected from the terminating party because of the importance of the change.” Ultimately, however, Professor Dessemontet's proposal was not incorporated in the 2010 Principles.

Where does this leave us? The current situation can be seen as unsatisfying and in need of further thought:

1. While long-term contracts are certainly not ignored by the UNIDROIT Principles, existing rules that relate to them are scattered throughout the Principles. The result is that it is somewhat difficult to study these rules as a coherent whole and similarly difficult for a court or arbitral tribunal to ascertain a full sense of the treatment of the issues by the Principles.

2. Some areas of importance to long-term contracts are not addressed. One such area is the ability to exit the long-term contract (the subject of Professor Dessemontet's proposal). Other examples may include:
  - a. The ability of judges to manage the process of determining the parties' obligations when contract mechanisms fail; and
  - b. Whether, and under what circumstances, to provide relief from surprising application of anachronistic features of agreements entered into in the distant past.

In my view, systematic analysis of the area, from both economic and comparative perspectives, is called for in order to determine a comprehensive list of situations in which contract law would benefit from the adaptation of the Principles to the context of long-term contracts. Regardless of how such augmentations might be codified in the Principles (whether, for example, they are presented together in a separate chapter or scattered throughout the Principles), it is probably most constructive to think about the treatment of long-term contracts systematically and, provisionally, as separate species. This will enable those conducting the study to assess more clearly what is present in the current Principles, what is missing, where there are gaps that should be filled, etc.

In sum, if the possibility of a fourth edition of the UNIDROIT Principles (or the augmentation of the 2010 Principles) is to be contemplated, it is my view that there should be study of long-term contracts as an integrated whole. Such a study would evaluate what is currently in the Principles and what is missing in order to decide whether more comprehensive treatment of long-term contracts is advisable and, if so, what that treatment should be. Without prejudging the results of such a study, I think that it is reasonable to predict that it would conclude that at least some aspects of long-term contracts are in need of more extensive treatment. In such a case, UNIDROIT can perform a service to the international legal community by addressing the matter in a systematic and thoughtful way.

## Justice Paul Finn

[...]

The *Principles* in its present form is an achievement in which UNIDROIT justifiably should take pride. Nonetheless it is, in my view, an incomplete work. In their coverage the Articles and the Comments address appropriately sales contracts, as the Secretariat's comments suggest. The same cannot be said of the treatment given explicitly to long term contracts in general and to relational contracts in particular, notwithstanding that these are pervasive species of commercial contracts. While examples in the Comments relate, on occasion, to long term contracts, explicit commentary relating to such contracts is sparse indeed.

In my seventeen years on the Federal Court of Australia, I dealt with quite some number of long term, relational and joint venture contract cases. These exposed issues which are recurrent in common law jurisdictions and, I would venture, civilian systems. Authoritative guidance and comment on them in the *Principles* would be invaluable.

The following illustrations are from cases I have decided and I give the citations of the principal examples of each of them. The illustrations have some reflection in the examples given in the Secretariat's comments.

1. Many projected long term contracts fail to eventuate after lengthy periods of preliminary negotiations, preparatory work, etc. often at great cost to one party. The examples are many in common law jurisdictions and involve projected distributorships or franchises, contractual joint ventures, leases of buildings to be constructed, lengthy but unsuccessful tender bids, etc. They can give rise to issues as varied as 'bad faith negotiations' (Art 2.1.15), 'inconsistent behaviour' (Art 1.8), preliminary contract, and unjust enrichment/restitution: see e.g. *Gibson Motorsport Merchandising Pty Ltd v Forbes* (2006) 149 FCR 569 (Aust); *Hughes Aircraft Systems International v Air Services Australia* [1997] FCA 558.
2. Even though parties address at length what are to be the terms of their contract, their conduct over time often deviates from those terms and for quite explicable reasons in some instances. This asymmetry can, in common law countries, be a cause of acute difficulty when disputes arise. The rules on variation, waiver, 'inconsistent behaviour' and 'no oral modification' clauses (Art 2.18) can collide unhappily: e.g. *GEC Marconi Systems Pty Ltd v BHP Information Technology Pty Ltd* (2003) 128 FCR 1.
3. Relatedly, the question of what is the actual contract between the parties from time to time can be quite controversial when the parties themselves acknowledge that the contract is an evolving one which, for example, is likely to require additional clauses, re-negotiation etc. The issue of what already has been agreed and what needs to be, or remains to be, agreed is commonplace: eg *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541.
4. The difficulty involved in terminating a long term contract because of breakdown of mutual trust and confidence between the parties is one frequently encountered. I have attached the first five paragraphs of a judgment I gave in 2010 which exposes my views on this matter.
5. It hardly needs to be said that 'good faith' and 'cooperation' have uncommon importance in practice in relational contract settings in particular. I need say no more on this other than that the *Principles* (Art 1.8) is quite muted in recognising this.
6. The above examples do not exhaust the difficulties/ issues to which long term contracts commonly give rise. They simply are ones I have encountered with some frequency.

It would, in my view, give greater balance and cohesion to the *Principles*, if it dealt much more explicitly with issues such as I have noted above. In saying this I am not necessarily suggesting a separate chapter for long term contracts — although I do consider that a separate article dealing with 'termination for just cause' should be a real priority. Much that concerns me could, I consider, be

achieved by additions to the Comments by way of explanation and by significant cross-referencing of Comments where a 'family' of Articles might potentially apply in a given instance.

What is obvious is that quite some attention needs to be given to how long term contracts can be given greater centrality in the scheme of the *Principles*. I do not suggest that, apart from termination, there is a need for a separate body of Articles dealing with such contracts. Rather some of the existing Articles have a greater importance for long term, and particularly relational, contracts than others. The scheme of the *Principles* should reflect this openly.

**Professor Marcel Fontaine**

[...]

As to the issues to be considered, Document C.D. (92) 4 (b) certainly covers most of them.

Possible additional suggestions :

- A long term contractual arrangement is often implemented by a group of linked contracts, either simultaneous (e.g. distinct contractual arrangements about financing or technical assistance) or successive (e.g. a a basic framework contract to be implemented by the future conclusion of specific contracts). There are aspects to be considered concerning such inter-relations.
- It sometimes occurs that the perspective of regular adaptations leads to the creation of a permanent specific structure, such as a "contract management committee", dedicated to follow the evolution of the contract in time and to suggest adaptations that may appear to be advisable, even beyond major disturbances such as force majeure or hardship.
- On the subject of interpretation, the references in art. 4.3 to the "practices which the parties have established between themselves" and to "the conduct of the parties subsequent to the conclusion of the contract" are especially relevant in long-term contracts.
- Post-contractual obligations are only marginally referred to in the Principles, as in art. 7.3.5 (3). They tend to be more developed when the parties' relationship has lasted for a long time.

[...]

## Professor Reinhard Zimmermann

[...]

The most important issue, in my view, is “termination for cause”. In this case, the introduction of an additional rule appears to be required, in line with a number of national legal systems. The topic was already on the work programme of the third Working Group. The decision of that Working Group to abandon its work on that topic was not based on any feeling that the drafting of a rule in that respect might not be necessary, or feasible.

[...] An additional issue that a new Working Group might like to consider – in either the “black letter” rules or the comments – is mediation clauses which appear to be introduced, more and more often, into business contracts. The issue appears to be particularly relevant with regard to long-term contracts. It may be envisaged to tie renegotiations to mediation in order to “save the contract”, as far as possible, in line with the notion of private autonomy.

[Furthermore] the regulation contained in Art. 2.1.14 needs to be seen, as far as determination of the contractual content is concerned, in connection with Art. 5.1.7. I think that it is an unfortunate solution to deal with the same issue in two different places. In addition, it may be asked why Art. 5.1.7 is confined to the question of price determination. On both points, the PICC differ from the other model texts (see, most recently, Art. 75 CESL), and they do so, I would like to submit, without good reason. In addition, the relevant provisions in the PICC – just like those in the other model texts – are fragmentary. They implicitly take for granted that the parties are bound by the determination. They do not deal with the standards to be observed by the third person nor with procedural requirements. The PICC also do not say what happens if determination by the third person is manifestly unreasonable; nor do they say what is to happen in the case of a failure of the mechanism, e.g. if the third person does not make the determination: Is the court or arbitral tribunal then empowered to make a determination? Or may the court substitute the third person by someone else?

Finally, it is to be regretted that the PICC are silent on a related matter which is of great practical importance: what is to happen if the third person is not required to determine a term of the contract but to assess certain facts which, for lack of experience, the parties cannot assess themselves? In Germany, this is discussed under the heading of “*feststellendes Schiedsgutachten*”, indicating that what the third party does is of a merely declaratory character; cf. also Art. 7:904 and 7:906 (2) BW providing the same rules for both “*feststellendes Schiedsgutachten*” and determination of a contractual term by a third person – in England both are discussed under the heading “expert determination”. (For an enlightening essay dealing with the problems relating to determination by a third person in the international model texts [including PICC], see Jens Kleinschmidt, *RabelsZ* 76 [2012], 785-818; cf. by the same author *Contractual Terms, Subsequent Determination*, in: Basedow, Hopt, Zimmermann [eds.], *Max Planck Encyclopedia of European Private Law*, 2012, 396-401. But there is more legal literature that should be taken into account in this context, e.g. the Vogenauer/Kleinheisterkamp commentary.)

[...]

UNIDROIT 2009 – Study L – Doc.109 (Excerpts)

**Position Paper with Draft Provisions  
on  
Termination of Long-Term Contracts for Just Cause**

by

Professor Francois Dessemontet, Swiss Arbitration Association

[...]

1. INTRODUCTION

During its 29 through 31 May 2006 meeting in Rome, the Working Group debated whether a new provision or set of provisions on the termination of contract for just cause should be introduced in the UNIDROIT Principles on international commercial contracts. There was a consensus for starting work on this topic, notwithstanding the admonition of Members of the Group who were concerned that, should a new provision in this regard appear as a weakening of the principle "*pacta sunt servanda*", some practitioners might less willingly make reference to the Principles in international commercial contracts.

In his concluding remarks, the Chairman of the Group presented the following observations:

- a) There appears to be a general interest for this topic
- b) A position paper together with a preliminary draft might be prepared for the next session of the Group
- c) The scope of the proposed provision or provisions should be examined with care
- d) A careful consideration of the notion of just cause is necessary
- e) Particular attention should be devoted to the articulation of the provision on termination for just cause with the already existing provisions on remedy for breach of contract and hardship
- f) The possibility of imposing renegotiation and/or revision of the contract should be discussed together with the remedy of terminating it for just cause.

The following report is to be understood as a short preliminary study of the main issues that are raised by a provision on the termination or revision of contract for just cause without any further discussion of the issue of the adaptation or revision of the contract. Although the existing § 314 BGB<sup>1</sup>

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<sup>1</sup> § 314 German Civil Code: *Termination, for just cause, of contracts for the performance of a recurring obligation*

- (1) Either party may terminate a contract for the performance of a recurring obligation on notice with immediate effect if there is just cause for doing so. There is a just cause if, having regard to all the circumstances of the specific case and balancing the interests of both parties, the terminating party cannot reasonably be expected to continue the contractual relationship until the agreed termination date or until the end of a notice period.
- (2) If the just cause consists in the infringement of a duty under the contract, the contract may be terminated on notice only after a specified period for remedial action has expired or notice of default has been given to no avail. § 323 (2) applies *mutatis mutandis*.
- (3) The person entitled may terminate only if he gives notice of termination within a reasonable period after becoming aware of the cause for termination.
- (4) The right to claim damages is not precluded by the termination.

appears to have played an important role in the discussion of the Working Group on the advisability of exploring the possibility to draft a similar provision for the Principles, the Report does not merely propose to take up the German legislative solution. It rather derives from the consideration of cases of diverse countries and arbitral experience a set of independent proposals that are presented as a first draft.

## 2. DEFINITIONS

As they are used in the present Report and the draft provisions, the following words are defined as below:

- a) *long-term contract*: a contract for the performance of a recurring, positive obligation; the definition is not identical with the concept of long term contract as has been used in the comment no. 5 to Article 6.2.2 on hardship, which defines long term contracts as “those where the performance of at least one party extends over a certain period of time”. Terminological harmonization could be sought once the scope of the provisions are better defined.
- b) *termination*: an end to the contract with effects for the future, with no restitution of the payment and no retransfer of goods or services which have already taken place in the performance of the contract
- c) *just cause*: a serious ground for modifying or ending the contractual relationship because the terminating party cannot be expected in justice, equity and good conscience to continue the contractual relationship until the agreed termination date or until the end of a notice period
- d) *compensation*: indemnification of damages includes lost profits
- e) *sphere of risks*: the type of risks that are assumed by one or the other party or parties to the contract under the agreed terms and conditions of the specific contract, including implied terms and conditions.

## 3. SCOPE OF THE PROPOSED PROVISIONS

### A) *Termination for Just Cause as Distinguished from Other Excuses from Performance*

The proposed provisions address extraordinary changes of circumstances which substantially affect a party's ability (or the ability of several parties to a multilateral agreement such as a joint venture with more than two partners) to continue to perform under an unchanged contract.

The proposed provisions do not collide with the force majeure provision of Article 7.1.7 because the force majeure provision addresses a temporary or definitive *impediment to performance* which could not have been expected at the time of the conclusion of the contract. However, the proposed provisions attempt to harmonize the system of applying the remedy by imposing to serve a notice to the party or parties that are not affected by the change of circumstances just as the provision on force majeure does (Art. 7.1.7 (3)).

The proposed provisions do not collide with the hardship provisions of Article 6.2 ff. because the test for just cause is not whether the performance of the contract becomes *too onerous* in view of the equilibrium of the contract as it is for hardship (see Article 6.2.2), but whether the performance can still be expected from the terminating party in spite of the changed circumstances and without having regard to the value of the performance to be received from the other party.

The proposed provisions do not collide with the initial or subsequent impossibility of the performance which the terminating party is under an obligation to make because the impossibility is seen as an *absolute impossibility of fact or law* to make the performance which is due under the contractual obligation, whereas the termination for just cause is based on an appraisal of the extraordinary circumstances of the case and a balance between the interests of both or all parties which make of the basically possible performance an intolerable burden for the debtor.

The proposed provisions do not collide with the *contractual provisions* which the parties may have adopted to face the possibility of a change of circumstances, such as the right to terminate the contract in case of a merger of one of the parties with a competitor, the winding up of the joint venture in certain circumstances of fact or law, or the termination on notice of material default. The



proposed provisions are not to be seen as yet another remedy for material breach of the contract but as supplementing the common will and intent of the parties in the cases where the terminating party could not take into account the modification of circumstances at the time of the conclusion of the contract. Parties are free to provide that the termination for just cause will be excluded or to provide for other remedies such as renegotiation or judicial adaptation of the contract only within given parameters.

*B) Scope of the draft provisions as to the contracts to which they should apply*

The long term contracts which are open to a termination for just cause are those which impose an obligation to do something positive, and not those which entail only a duty to abstain from doing something. For example, a 99-year lease on fee is not subject to the termination for just cause under the draft provisions, because on the main it does not entail the duty to perform positive acts. A prohibition of competition during 10 years is not subject to the termination for cause (although in certain jurisdictions it may be deemed in restraint of trade to enforce it in given circumstances, after some years, against former employees).

To the contrary, the primary target of those draft provisions are the agreements that entail positive duties of cooperation between the parties, such as the joint marketing of products or services, the exchange of sensitive information, the opening of the books for checking figures on which royalties must be computed or common efforts of research and development for new products or new processes.

Under some systems of law, those contracts could be characterized as *relational contracts*, because they institute a long term relationship of some degree of trust and confidence between the parties, without evidencing all the characteristics of a partnership or of a fiduciary relationship. In other systems of law, some of those contracts could be termed to be concluded *intuitu personae*, that is concluded in consideration of the person or persons undertaking to perform the positive acts that require mutual confidence and trust. However, it is not necessary to find that a specific confidential relationship has existed under the law applicable, such as is sometimes required for the protection of trade secrets. The finding of a confidential relationship may be subject to particular requirements that are best explained by the equitable remedies that may be available if such a relationship is found to exist, for example the accounting for the profits unduly made by the defendant (as opposed to the profits lost by the claimant which are but an element of his damage). Such stringent tests as are applicable for confidential relationship under the common law of some jurisdictions are not entirely relevant here, although the recognition of those specific relationships is part of the developing body of law on relational contracts.

Further, the contracts that are subject to a termination for cause are those which entail a continuing performance, or a periodical performance, or a repeated performance due after that some time has elapsed since the prior performance. The duration of those contracts cannot be fixed in the absolute by giving a number of years, although it is unlikely that a contract of a duration inferior to three to five years could benefit from the draft provisions. The court or the arbitrator will have to consider the investments that have been made or are still required to be made and the economic risks which have been assumed or should be assumed in the future under the contract the termination for just cause of which is alleged to be admissible.

#### 4. NOTION OF JUST CAUSE

*A) General Observation*

The draft provision should not be understood as allowing a termination for convenience in case of any change of circumstances, be it ever so slight. Rather, the changed circumstances are *significant changes* that have not been taken into account by the parties when apportioning the risks under the contract at the time of the conclusion of the contract. The change of circumstances is significant when it substantially affects a party's ability to rely on a reciprocal confidence and good faith in the performance of the contractual obligation.

### *B) Decided Cases of Selected Jurisdictions*

The following cases of jurisdictions which already know the termination for just cause best explain the sort of circumstances that may be invoked by the terminating party:

In Switzerland, the loss of mutual trust between the parties to a licensing agreement due to late performance of the inventor who had to reach the industrially mature stage for the invention was considered as a just cause for instant termination of the contract by the licensee.<sup>2</sup>

In another case, the Swiss Federal Tribunal found that the sudden dramatic diminution of the financial capacity of a lessee was sufficient for the latter to terminate the lease agreement for just cause<sup>3</sup>.

In a recent Swiss case, the loss of trust between a lender and the lendee was found to be sufficient for the former to terminate the contract for just cause. The loan was granted without interest because of the close relationship between the parties<sup>4</sup>.

The German Supreme Court held that the termination of the main agreement between the principal and the main contractor was a just cause for the latter to terminate the contract with the subcontractors for just cause<sup>5</sup>.

In another case, the German Supreme Court stated that not any and every disturbance of the mutual trust is sufficient for a party to terminate the contract for a just cause. The disturbance has to be serious to the extent that the continuation of the contractual relationship until the end of the ordinary period for termination cannot be reasonably expected<sup>6</sup>.

According to the case law of the German Supreme Court, the actual risk of imminent insolvency of the borrower constitutes a just cause for the lender instantly to terminate the contract<sup>7</sup>.

On the main, the courts recognize as just cause the circumstances which would necessarily entail a loss of the confidence of the terminating party towards the other one when one considers the position of reasonable parties placed in the same situation. This is therefore a more objective test than whether the terminating party did really lose his or her confidence. For example, the case has been cited of one party to an advertising joint venture implying the lease of many billboards placed on public grounds and belonging to townships: when the main foreign partner of the local party was placed under arrest in a third country under suspicion of bribery of public officials of that country, the local partner could legitimately terminate the contract since the continuation of that contract would have ruined the credibility of the joint venture vis-à-vis public authorities. The example shows that the factual basis of the indictment against the foreign partner and his degree of fault were less relevant than the loss of business due to the public opinion.

## 5. NOTICE FOR TERMINATING THE CONTRACT

### *A) Purpose of the Notice*

The draft provisions require the terminating party to serve a notice of termination. The purpose of that notice is two-fold.

First, it is necessary to put the party against whom the termination is requested on notice that the contract will no longer be performed by the other party. Investments must be avoided in relation with the terminated contract and new investments are to be made in order to seek new business with third parties.

In most cases of breach a contract, a reasonable time limit must be fixed to the breaching party in order to cure the breach. This has been said to be a common principle of European private law, for example in an Award ICC No 4496, Summary by S. Jarvin, in LES Nouvelles 1988, p. 23.

<sup>2</sup> Decision of the Swiss Federal Tribunal, ATF 92 II 299.

<sup>3</sup> Decision of the Swiss Federal Tribunal, ATF 122 III 262.

<sup>4</sup> Decision of the Swiss Federal Tribunal, ATF 128 III 428.

<sup>5</sup> Decision of the German Supreme Court, III ZR 293/03.

<sup>6</sup> Decision of the German Supreme Court, KZR 19/02.

<sup>7</sup> Decision of the German Supreme Court, XI ZR 50/02.

However, the termination for just cause is not a termination for breach. Although the fixing of a time limit to cure the just cause if it is susceptible to be changed by the party against whom the contract is terminated may not harm the terminating party, it should not be seen as a prerequisite for the validity of the notice.

#### *B) Immediate Termination*

The case law of several countries admits the immediate termination of the contract when exceptional circumstances justify it. For example, the merger of the licensee with a third party immediately endangers the confidentiality of the licensed technology. No new development should then be disclosed to the licensee and the licensee should, to the extent feasible, give back the information disclosed on paper or software. In exchange, the royalties are no longer due from the date of the terminating notice.

Nevertheless, the necessity of protecting the investments made during the contract may also lead to admit a different solution, with a transitional period allowing the licensee to look for some other licensor or buy some different technology.

Distribution agreements often provide that the distributor should be able to finish selling its inventories even after the termination. Even then, exceptional circumstances can lead to an immediate termination of the contract, for example if the distributor is charged with a criminal indictment relating to the performance of the contract—for instance, forging immatriculation papers for an automobile in order to get a commission for a sale which did not happen in fact.

#### *C) Effects of the Notice*

The Principles cannot precisely determine in which case the notice of termination will take effect only after three or six months, and in which case it should have an immediate effect. The mention of immediate effects in extraordinary circumstances should suffice to give guidance to the courts.

The notice for termination is considered as a “constitutive” declaration of will in some systems of law, for example of the Germanic family. Therefore, it might be argued that the serving of one and a sole notice of termination will exhaust the right of the terminating party. No particular wording of the Principles could avoid the arguments that a party may derive from such a characterization of the notice, but it may be useful to put into the commentary that international business usages do know the practice of repeating a notice of termination when the conditions for the exercise of the right to terminate appear doubtful at the time of the first notice, and more certain at the time of the second or a subsequent notice. It might also happen that the first notice is a notice of material default and the second notice a notice of termination for just cause, and this should not impede the court to adjudicate the claims deriving from those different notices each on its merits.

#### *D) Grounds for Termination to be Mentioned in the Notice*

The last important issue relating to the notice is whether the terminating party can rely only on the grounds that are mentioned in the notice or on further grounds that would come later to the attention of the terminating party. A distinction has to be drawn between the grounds that could not be known by the terminating party and the grounds which she knew or ought to have known at the time of serving the notice. The necessity to indicate all the grounds known to the terminating party at the time the notice is served derives from the protection of the interests of the party against whom the contract is terminated. That party must be put in the situation to know whether the grounds are serious and can be established in case of a dispute. It might appear to be unfair to allow the terminating party to retain information which is essential to the question whether the contract should continue or not. Similarly, if the terminating party enforces the right to terminate before the courts, it might be unfair against the respondent if the court could accept that the termination is valid because of some other reason or reasons than the ones that were given at the time.

Yet there may be cases in which complete information about the changing circumstances and about the reasons for the disappearance of the reciprocal confidence between the parties is uncovered only after some delay or after discovery. This could be the case, for example, where a joint venture is undermined by clandestine manoeuvres of a partner, which attempts and succeeds to take an operational controlling majority in the joint company through the interposition of businessmen or business entities. It sometimes happens that only a report by a public authority such as the Security and Exchange Commission will determine who are the real shareholders of the shell entities that were used to acquire the majority. Then, the terminating party, which did not know about the scheme, could later allege it in the proceeding, even if it were not mentioned in the notice for termination.

In this regard, the Principles should not give too many details, as the matter is best left to the courts to consider according to their traditions.

Second, the notice may fix the exact date on which the contract ceased to be binding on the parties, at least for the main obligations. Ancillary obligations such as the duty to keep information confidential, or to refer the case to some alternative dispute resolution may survive the termination. Similarly, assets which were affected to the joint performance of some bilateral or multilateral contracts that are akin to a partnership or a joint venture may have to be liquidated and receivables may have to be cashed or guaranteed, which may last some months or some years. However, unless otherwise provided in the contract, the service of the notice of termination determines until when the profits are to be shared, even if the losses may be apportioned as under the contract after that date.

#### *E) Other Specificities*

Some systems of law require a court to decide on the termination, so that the notice has only a declaratory rather than a constitutive effect. Some other systems do not require the intervention of the court to terminate the contract. The notice then creates a new legal situation and all the rules that may be applicable to such a formative act will apply to the notice. For example, it might be maintained that under Swiss law, such unilateral act modifying the legal situation shall be exercised through an irrevocable, unconditional notice. However, it should be admissible to give a notice specifying that the contract will be terminated if certain assurances are not given or certain measures not taken (such as placing the industrial division with which the terminating party is under contract under a different umbrella than the one the merger would appear to entail at first). The UNIDROIT Principles should not take a position in this regard, as international commercial contracts may be subject to a law recognizing the validity of a unilateral termination for cause or to another law, which requires the approbation of the court.

There appears to be a need to specify that the terminating party must react as quickly as possible when the circumstances leading to a possible termination come to his or her knowledge. The terminating party should not speculate to the detriment of the other party with a "wait and see" policy and, at the same time, serve a notice in an attempt at safeguarding his rights. The principle of good faith (Article 1.7) might of course lead to an analogous reasoning, but an express provision would be clearer for all Parties.

A most delicate issue revolves around the time limit to be fixed for the contract to end.

The protection of the other party's expectations might lead in most cases to give a time limit of three months or six months, or even one year in bigger projects. In exceptional circumstances, such as are present in joint ventures for example, the structure of the contract may be such that only certain dates (closing of the accounts) can enter into consideration. In very particular cases, the termination may be immediate. This might happen when several notices to cure a breach have been served to no avail. The immediate termination then remains the only means to stop a ruinous relationship. The immediate termination will be recognized only where no other solution is thinkable. However, in most cases, an abrupt termination which is justified in its principle but not as taking place immediately will take effect three or six months later, depending on the ordinary provision for termination in the contract itself, which the court will attempt to follow to the extent possible in fact.

## 6. EFFECT OF TERMINATION

The termination for just cause entails ending of the contractual relationship for the future only. It does not retroact to the time of conclusion of the contract.

The parties are still bound by a duty to liquidate their relationship, for example through disclosure of the relevant accounts and inventory.

It has been adjudicated in several French, U.S. and Swiss cases that the sheer appearance of the existence of a valid patent on the contractual technology was an advantage for the licensee. Thus, the licensor had the right to keep the royalties paid under the contract based on that patent, although it was later found to be invalid, at least until such time as the invalidity became apparent to the parties. In a similar manner, the contract which is terminated for cause has given to the parties a real economic advantage, or at least the position they had bargained for, even if an intervening just cause leads to its end. Therefore those payments which have been received need not be restituted.

The termination of multilateral contracts raises specific questions because the terminating party cannot force the other parties not to continue the contract. The apparent end of a three-partite joint venture can mark the beginning of a two-partite venture, for example. As the assets that are put to work in both consecutive ventures are often the same, the termination of the contract is more in the nature of an exit by one of the partners. Particular rules are proposed to take into account the ensuing difficulties.

### **Draft Provisions**

[...]

#### **DRAFT SECTION 6.3 : TERMINATION OF LONG-TERM CONTRACTS FOR CAUSE**

##### **Article 6.3.1**

*(Termination for just cause)*

A contract entered into for an indefinite or definite period of time may be terminated for just cause by either party at any time in exceptional circumstances, with immediate effect if it is so warranted by the circumstances.

*Note: The termination for cause is conceived as extraordinary remedy (ultima ratio), giving to one party the possibility to terminate the lasting contractual relationship immediately. Therefore, the cause has to be an intolerable event. In contrast to hardship, where the balance of obligations is altered and where the contract may be in principle maintained with adapted obligations, the existence of a just cause leads to the termination of the contractual relationship.*

##### **Article 6.3.2**

*(Definition of just cause)*

There is a just cause, where the continuation of the contractual relationship until the agreed term cannot reasonably be expected of the party who terminates the contract, in particular :

(a) in case of a change in the circumstances, excluding non-performance and hardship, if continuation of the contract cannot reasonably be expected from the terminating party because of the importance of such change. Importance shall be defined by taking into account the nature of the contractual relationship and the circumstances of the case;

(b) in case of loss of trust between the parties, if that trust is an important component of the lasting contractual relationship.

*Note: The listing is non exhaustive and other cases are conceivable. Example of a change in circumstances: Takeover of the contractual party by the principal competitor of the other party in a joint venture or licensing agreement (change of control over one party).*

### **NEW ARTICLES TO BE ADDED IN CHAPTER 7, SECTION 3: TERMINATION**

#### **Article X**

*(Effects of termination for just cause in particular)*

(1) If termination for just cause is justified in case of loss of trust due to the other party, the terminating party remains entitled to compensation for its damage, including lost profits until ordinary expiry of the contract or until the time when the contract could have been terminated ordinarily.

(2) If termination for just cause is justified in case of a change in the circumstances, no compensation is due in principle. However, if the ground for termination lies within the sphere of risks ordinarily assumed by the terminating party, the other party may be entitled to compensation. On the contrary, if the ground for termination lies within the sphere of risks ordinarily assumed by the other party, the terminating party may be entitled to compensation.

#### **Article Y**

*(Effects of termination on multi-party contract)*

(1) The termination of a multi-party contract entails the liquidation of all assets and receivables as well as the payment of liabilities or the furnishing of appropriate guarantees.

(2) When only one or some of the parties but not all of them exit the contract or are excluded, the remaining parties do not have to liquidate assets and receivables if they assume all liabilities resulting from the common activities.

(3) Unique assets that were acquired or created in pursuance of the contract may be sold or auctioned off among all parties to the contract or to third parties.

[...]