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**Item No. 5 on the agenda: International Commercial Contracts –  
Long-term contracts**

(prepared by the Secretariat)

<i>Summary</i>	<i>Developments related to the work on long-term contracts in the context of UNIDROIT Principles of International Commercial Contracts</i>
<i>Action to be taken</i>	<i>See paragraphs 5 and 6</i>
<i>Mandate</i>	<i>Work Programme 2014-2016</i>
<i>Priority level</i>	<i>High</i>
<i>Related documents</i>	<i>UNIDROIT 2014 – Study L – Doc. 126; UNIDROIT 2015 – Study L - Misc. 31</i>

1. 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.

2. 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 specific issues that might 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 the Principles with a view to covering the special needs of long-term contracts.

3. The Working Group that was set up is composed of Michael Joachim BONELL, Emeritus Professor of Law, University of Rome I, Consultant UNIDROIT (*Chairman of the Group*); Catherine CHAPPUIS, Professor of Law, Faculty of Law, University of Geneva, Member of the *Groupe de travail Contrats Internationaux*; Neil COHEN, Jeffrey D. Forchelli Professor of Law, Brooklyn Law School, New York; François DESSEMONTET, Emeritus Professor of Law, University of Lausanne; Paul FINN, Former Judge, Federal Court of Australia, Adelaide; Paul-A. GELINAS, Avocat aux Barreaux de Paris et de Montréal, Paris; Sir Vivian RAMSEY, Former Judge, Technology and Construction Court, Royal Courts of Justice, London; Christopher R. SEPPÄLÄ, Partner, White & Case LLP, Legal Advisor to the FIDIC Contracts Committee; Reinhard ZIMMERMANN, Professor of Law, Director at the Max-Planck-Institut für ausländisches und internationales Privatrecht, Hamburg.

4. The Working Group held its first session in Rome from 19 to 22 January 2015. The session, which was attended also by a number of observers representing international organisations and other interested bodies,<sup>1</sup> was devoted to the examination of a position paper on “The UNIDROIT Principles of International Commercial Contracts and Long-term Contracts” prepared by Professor M.J. Bonell and containing a list of issues with related proposals and/or questions, for further consideration by the Working Group.

5. After a careful examination and lengthy discussion the Working Group decided to focus on the following issues, and the conclusions reached with respect to each may be summarised as follows:<sup>2</sup>

a) *Notion of “long-term contracts”*

- To amend Comment 2 to the Preface to highlight the fact that the new edition of the Principles gives due consideration to the special needs of long-term contracts.
- To provide a definition of the notion of long-term contracts in Article 1.11 (or in a new Article 1.13) and to include in the comments cross-references to the articles and/or comments which are either expressly or impliedly related to long-term contracts.
- To replace in Comment 1 to Article 7.3.6 the words “contracts under which the characteristic performance is to be made over a period of time” with “long-term contracts”, and to delete the last 2 sentences of the first paragraph.
- To replace in Article 7.3.7 in the title and in the text the words “contracts to be performed over a period of time” with “long-term contracts”, and to amend the Comment 1 accordingly.

*(drafts to be prepared by M.J. Bonell and N. Cohen)*

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<sup>1</sup> Cyril EMERY, Legal Officer, UNCITRAL Secretariat, Vienna; Pilar PERALES VISCASILLAS, Professor of Law, Universidad Carlos III de Madrid, Member of the CISG Advisory Council; Don WALLACE, Jr. Chairman of the International Law Institute, Washington, DC; Giuditta CORDERO MOSS, Professor of Law, University of Oslo, Member of the Norwegian Oil & Energy Arbitration Association; Pietro GALIZZI, Legal Affairs Department, Senior Vice President, ENI SpA, Milan.

<sup>2</sup> For a more articulated report on the discussions on the various issues by the Working Group, see the Report on the January session of the Working Group prepared by the UNIDROIT Secretariat, UNIDROIT 2015, Study L – Misc. 31.

b) *Contracts with open terms*

- To add in paragraphs 1 and 2 of Article 2.1.14 a reference to the possibility that the missing term be determined by one of the parties, and to amend Comment 2 to Article 2.1.14 accordingly.
- To replace in Article 5.1.7 (3) the words “cannot or will not” by “does not” so as to use the same formula as adopted in Article 2.1.14 (2)(b), and to amend Comment 3 to Article 5.1.7 accordingly.
- To add in Comment 3 to Article 5.1.7 a sentence to the effect that the parties are free to fix a standard by which the third party must comply and, if it does not, then the parties can challenge that determination.
- To add in Comment 3 to Article 5.1.7 a sentence to the effect that the parties may wish to fix differing standards depending on whether the task of the third party was to determine missing contract terms or to assess mere facts.
- To make any further amendment to the comments to Articles 2.1.14, 4.8, 5.1.2 and 5.1.7 necessary to take account in particular of long-term contracts.

*(drafts to be prepared by Sir Vivian Ramsey)*

c) *Agreements to negotiate in good faith*

- To amend the last paragraph of Comment 2 to Article 2.1.15 by deleting the word “expressly” before “agree”, by replacing “all the remedies” by “all appropriate remedies” and replacing “for breach of contract” by “for non-performance of the agreement”.
- To mention in that same Comment 2 that the duty to negotiate in good faith means a duty to negotiate seriously, with an intent to conclude an agreement, and that in particular in the context of complex long-term contracts parties might wish to further define such duty, e.g. by describing the procedure to be followed, by agreeing on a time table, etc.
- To point out that for the determination of the content of the duty to negotiate in good faith reference should in any event be made to Article 1.8 on the prohibition of inconsistent behaviour, to Article 2.1.16 on the duty of confidentiality and to Article 1.9 in the sense that parties should stick to practices established between themselves and relevant trade usages.
- To add in the comments to Article 5.1.4 a new paragraph mentioning that in international contract practice, especially in the context of long-term contracts, it is quite common to speak, instead of a “duty to negotiate in good faith”, of a “duty to use best efforts” with a view to finding a commonly acceptable solution, and that even in the absence of such language the duty to negotiate in good faith amounts to a duty of best efforts.
- To point out that especially in the context of complex long-term contracts a duty of best efforts to find commonly acceptable solutions may be stipulated not only with respect to the formation of the contract but also, if not even more frequently, with respect to unexpected difficulties that may arise in the course of the performance.
- To make a cross-reference to Article 5.1.4 in all the relevant provisions of the UNIDROIT Principles, i.e. not only in Comment 2 to Article 2.1.15 but also e.g. in Comment 3 to Article 6.2.3, emphasizing their particular relevance in the context of long-term contracts.

*(drafts to be prepared by N. Cohen)*

d) *Contracts with evolving terms*

- To add a new Comment 3 to Article 4.3, which under the heading “Practices established between parties and conduct subsequent to conclusion of contract particularly relevant in interpretation of long-term contracts” states that in view of the fact that long-term contracts often involve performances of a complex nature and are “evolutionary” in nature, i.e. require adaptations in the course of performance, the criteria in sub-paragraphs (b) and (c) are particularly relevant with respect to these types of contract. Since such contracts involve repeated performance (and repeated opportunity for a party to object if the party is displeased), especially the conduct occurring after the conclusion of the contract can provide the basis for inferences as to what the parties believe their obligations are and, thus, be a useful tool in contract interpretation.
- At the same time that Comment should point out that according to Article 4.3 (c) the subsequent conduct of the parties can only be an interpretative tool, i.e. be used to explain or amplify, but not to contradict, the terms of the contract as originally agreed between the parties.
- The Comment should further mention the possibility to set up a special organ (e.g. an “auditing committee” composed by representatives of each of the parties) with the task of monitoring the developments in the course of performance and possibly submitting to the parties suggestions for revision of the contract terms.
- To replace the present Comment 3 to Article 4.3 by a new Comment 4 which under the heading “‘Merger’ and ‘No oral modification’ clauses” states that parties that wish to limit or totally exclude any relevance of subsequent conduct might include in their contract so-called “merger clauses” and “no oral modification clauses”, and refer as to their meaning and effects to Articles 2.1.17 and 2.1.18, respectively.

*(drafts to be prepared by M.J. Bonell)*

e) *Supervening events*

- To add a new Comment 5 to Article 7.1.7 with the heading “Force majeure and long-term contracts”, which opens with the general statement that in the context of 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, parties may wish to make in their contract not only for the case of hardship but also for the case of *force majeure* provision for the continuation, whenever possible, of their business relationship, and to envisage termination only as a last resort.
- The same Comment could then indicate that 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 and subject to the question of who is to bear the costs, 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 specified period of time (e.g. 30 days, one year, etc.) after receiving notice of the impediment.
- Finally, parties may also wish to consider whether 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 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.

- Moreover, the parties may wish to consider providing in their contract for the establishment of a permanent body (e.g. a so-called “dispute review board” composed of one or three persons with special expertise), with the task of aiding them in resolving any kind of disagreement and dispute that may arise in the course of performance by issuing either mere recommendations or making veritable decisions, and that only if such recommendations or decisions are not accepted by the parties, may they resort to arbitral or judicial proceedings.

*(drafts to be prepared by N. Cohen)*

f) *Cooperation between the parties*

- To split 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 cooperation for all kinds of contract, 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.
- To state in Comment 1 that the duty of cooperation 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).
- To move Illustration 1 in the present single Comment to Article 5.1.3 to Comment 1 to Article 7.1.2.
- To state in Comment 2 that in the context of long-term contracts, especially those involving performance of a complex nature and ongoing relationship between the parties, there might be required a higher degree of cooperation (or “co-operativeness”). Comment 2, in stressing the special importance of the duty of cooperation 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.), always of course within the limit of reasonable expectations (for further examples, see Study L - Misc. 31, paras. 61 and 63). Should such duties go beyond that limit and imply not insignificant expenses, the creditor may either refuse or be entitled to compensation.

*(drafts to be prepared by M.J. Bonell)*

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

- To amend Article 5.1.8 so as to make it clear that, once a contract for an indefinite period has been ended, as far as restitution is concerned the rules laid down in Articles 7.3.5 and 7.3.7 apply.
- To change the title of Article 5.1.8 into “Termination of contracts for indefinite period” and to replace in the text the words “may be ended” by “may be terminated”.
- To revise the comments to Article 5.1.8 accordingly.

*(drafts to be prepared by R. Zimmermann)*

h) *Termination for compelling reasons*

- To add in Chapter 6 a third Section entitled “Termination for Compelling Reasons” and composed of one (or more) Article(s) stating that
  - “Long-term contracts may be terminated by either party for compelling reasons. There is a compelling reason if, having regard to all the circumstances of the specific case and balancing the interest of both parties, it would be manifestly unreasonable to expect the terminating party to continue the relationship.”
  - “The right to terminate the contract for compelling reasons is exercised by notice to the other party.”
  - “With respect to the effects of termination for compelling reasons Articles 7.3.5 and 7.3.7 apply with appropriate adaptations.”
- To state in the Comments, among others, that
  - termination for compelling reasons constitutes an exceptional remedy, applicable in particular, though not exclusively, in the context of so-called relational contracts, and to be distinguished from the termination of contracts for an indefinite period (Art. 5.1.8), termination for fundamental non-performance (Arts. 7.3.1 et seq.) and hardship (Arts. 6.2.1 et seq.).
  - for there to be a compelling reason for a party to terminate, it is neither required, nor sufficient, that the other party has been at fault, the decisive tests being the balancing of the interests of the parties and the manifest unreasonableness of continuing the relationship (with examples of cases in which there are compelling reasons and of cases in which there are no compelling reasons for termination: for such examples, see Study L - Misc. 31, paras. 84, 85, 86, 87, 88).
  - as to the effects of termination for compelling reasons, Article 7.3.5(2) preserving the right to damages for past non-performances, and Article 7.3.7 excluding restitution of past performances, do not provide a satisfactory solution where no party has been at fault, but one party has incurred considerably higher expenses in the performance of the contract or has acquired, in the interest of the common purpose pursued by the contract, goods or services from third parties: in such cases the rules laid down in Arts. 7.3.5(2) and 7.3.7 might have to be adapted, e.g. by granting that party a sort of compensation for its higher expenses or by setting up a sort of “liquidation” of all assets and debts of the contractual “joint venture” entered into by the parties (for an example see Study L - Misc. 31, para. 101 fn. 4).
  - if a party gives notice of termination for compelling reasons without there being such compelling reasons, this constitutes a case of anticipatory non-

performance (Article 7.3.3), giving the other party the option either to terminate the contract for fundamental non-performance and claim damages, or to keep the relationship alive and resort only to the remedy of withholding its own performance (Article 7.3.4) in the hope that the matter might be resolved in one way or another at a later stage.

- finally, the provision(s) on termination for compelling reasons is(are) of non-mandatory character, and parties may exclude its(their) application altogether or indicate in their contract specific cases of termination for compelling reasons.

*(drafts to be prepared by Sir Vivian Ramsey and R. Zimmermann)*

*i) Post-contractual obligations*

- To amend Comment 3 to Article 7.3.5 by adding a new paragraph stating that
  - so-called post-contractual obligations are particularly frequent in the context of long-term contracts and may be of two different kinds, i.e. they either relate to the winding up of the past relationship, or they already existed before the end of the contract and survive in the future for a certain period of time (for examples of both types, see Study L-Doc. 126, paras. 44 and 45 and Study L- Misc. 31, paras. 111, 112 and 114)
  - to point out that if the contract is silent on this issue, to determine which obligations, if any, exist even after the end of the contract is a question of contract interpretation
  - to avoid any unnecessary uncertainty in this respect parties may wish to indicate in their contract specifically which obligations, if any, exist even after the end of the contract, what is their precise content and whether they are binding on one or both of the parties, what are the remedies in case of breach, their compatibility with applicable mandatory domestic rules, etc.

*(draft to be prepared Christine Chappuis)*

6. A second meeting to finalise the proposed amendments and additions to the black-letter rules and comments to the Principles with a view to their submission to the UNIDROIT Governing council for adoption in 2016 will be held at the *Max-Planck Institute for Comparative and International Private Law* in Hamburg, at the kind invitation of that Institute which will cover most of the costs associated with the meeting. The meeting will be held 26-29 October 2015.