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PROGRESSIVE CODIFICATION OF INTERNATIONAL TRADE LAW

Proposed Rules on Hardship

with

Introduction and Explanatory Report

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INTRODUCTION

The problems with the consequences of essentially changed circumstances has for many years played a certain role in the law of contracts of different countries, have been applied for their solution. Currently this phenomenon is gaining increasing importance; especially for international commercial contracts. The rationale is extensive. First they relate to the nature of the contracts and second to the features of political, economic and social development on the international level, which is characteristic of our time.

Concerning the first group of reasons we mention

- the time horizon of contracts has prolonged (contracts on joint ventures, successive deliveries, management)

- the subject matter of contracts has become more complex (turn key contracts, contracts product in hand)

- for the achievement of certain economic aims often a whole network of contracts becomes necessary. This relates in the first line to the contractor who is often compelled to create a consortium but sometimes also to the employer (mining and similar contracts).

- the importance of the fulfilment of certain contracts is growing, not only for the contractor and employer, but also for their respective countries.

In relation to the second group of reasons it is quite obvious that rapid inflation, drastically increasing interest rates, abrupt changes in and demand of, technology are examples of events influencing certain existing contracts, not to mention political and even natural events. The characteristics of modern international economic contracts make them especially sensitive to change in circumstances.

Of course, the above mentioned peculiarities relate to a rather few, but very important contracts. This makes it worth while to develop special regulations covering this problem. In drafting and discussing this problem only these few but important contracts have been taken into consideration, especially long term contracts with a complex subject matter of extreme value.

It is true that the cause which requires modifications of the contract or even its avoidance may go back to the process of formation of the contract. This does not only relate to the classic problems of validity of contracts (mistake, error, fraud, threat), but also to unequal bargaining power and unconscionability to which attention has started to focus only more recently. (See Proposed Rules on the (Substantive) Validity of International Contracts (excluding Illegality) prepared by U. Drobnig and O. Lando, UNIDROIT 1980 Study L - Doc. 17, p. 19 et seq.).

Problems of the latter kind have reached a special importance in connection with contracts made between developing countries and transnational corporations in a situation where the developing country could not but accept an unequal bargain. (See O. Lando Renegotiation and Revision of International Contracts, German Yearbook of International Law, vol. 23, Berlin (W) 1981, p. 38 et seq.) These situations as well as some of the legal consequences used in hardship cases are discussed more and more frequently, as revision or adaptation of the contract. Nevertheless this paper is focussed on contracts where there is no dispute as to the process of their formation. What matters here is how to overcome influences on existing contracts, changing the initial situation, that means the situation at the time of the formation of the contract -herinafter called interferences. The main interferences occurring during the performance of the contract are breach of contract, intentional gaps and impediments to contract.

The breach of contract cases are characterized by the fact that the nonfulfilment of the contract is attributable to one party. The criterion for this attribution is rather diverse. Objective responsability, with the possibility of exemption (especially in cases of force majeure) and fault are used most frequently.

The scope of the breach of contract cases does not solely depend on this but also on the exact determination of the parties obligations or, in other words, on the description of the breach. On one hand a party either by law or more frequently by contractual stipulation may take over a risk of which he normally would be exempted. On the other hand a party may reduce its risks by excluding such events for which he would normally be responsible. The same effect can be attained if the obligations are vaguely described leaving a certain flexibility for the debtor (e.g. determining a period rather than an exact date for the fulfilment of the obligation) or an option is conceded to the debtor to choose the mode inwhich to fulfill his obligation (e.g. the quality standard with the corresponding modifications for the price). By these methods the debtor may be put into the position to solve some problems he may be confronted with in the process of performance without becoming liable for breach of contract. (Cf. D. Maskow H. Rudolph, Die Anpassung von Aussenwirtschaftsverträgen und Vetragsstörungen als Aufgabe der Vertragsgestaltung, Recht in der Aussenwirtschaft, Supplement to Sozialistische Aussenwirtschaft 7/1972, p. 17 et seq.)

If a breach of contract occurs the creditor may rely on traditional remedies; in particular specific performance (at least in most civil law countries), claims on compensation (damages, penalties, liquidated damages) and termination of the contract.

In cases of clear breach of contract sometimes renegotiation with the aim of adaptation of the contract is agreed upon as a consequence, most often without removing the traditional remedies. Where e.g. the employer in a plant contract fails to render the necessary assistance as agreed upon in the respective contract this may result more or less in the traditional consequences of breach of contract. Furthermore the contractor is exonerated as far as the orderly fulfillment of his obligations is impeded by such acts of the other party. In certain cases the contractor is required to fulfill by himself the obligations of the other party in order to continue the performance of the contract. Finally renegotiation may be foreseen in the contract, since in many cases the exoneration only of the contractor would not meet his interests. Obstacles caused by the employer often do not only effect such obligations of the contractor which are directly affected, but may have consequences for further parts of the contract. E.g. If the contractor is compelled to defer his assembly work because the employer has not yet completed the foundation work. This may also affect the price since the costs have increased in the meantime.

It is also possible that renegotiations are agreed upon for the case of breach of contract by the contractor.

The contents of renegotiations as a consequence of a breach of contract of either party has its peculiarities since one party is responsible for the situation and in general, has to bear the consequences. Nevertheless some similiarities with other renegotiation cases might be identified, but this question has not been analysed in this paper.

Intentional gaps occur because of lack of information (the parties do not know all relevant details for drafting necessary stipulations), because of lack of time or even of agreement (in due time, before the preparations for the performance of the contrat have to be started). They may relate either to individual conditions (programm for the performance test of a plant) or to more comprehensive parts of the contract (regulation of the assembly of a plant). Occasionally complete contracts may be necessary to fill the gaps. In these cases the original contract assumes a precontractual character.

Most intentional gaps require a supplement to the contract, but not a change or adaptation of it. It is clear from the beginning which items are concerned, and the fact that completion has to take place is agreed upon by the parties. It is therefore possible for the parties

to determine the criteria for the completion, since they know exactly which items have to be made more precise; but this option is not often used.

In spite of these special features of intentional gaps the procedure for completion of contracts can be formed similar or even identical to, that which should apply to hardship cases. This may have consequences for the document on the Progressive Codification as a whole. In the 1979 draft of chapter 1 (UNIDROIT 1979, Study L - Doc. 15) the completion of contracts had been dealt with in articles 3 and 4 paragraphs 1 and 2. This solution does not seem to be fully adequate and some of the provisions proposed below should be checked with a view to applying them as well to completion cases.

The impediments to contract, as the last kind of interferences to be dealt with here are not attributable to one party like the intentional gaps, but unlike them they occur after the formation of the contract. The impediments to contract taken into consideration in contractual practice are manifold and here only some important categories can be identified. One of these categories is formed by impediments making wholly or partially impossible the fulfilment of the contract either temporarily or permanently. In contractual practice such impediments are covered frequently by the force majeure clauses. The main purpose of these clauses was and still seems to be exemption in cases of breach of contract. This sometime means that there is no breach of contract in case of force majeure. But at least certain consequences of breach of contract are excluded in case of force majeure. More recently force majeure clauses besides the fulfilment of this function foresee special legal consequences aimed at overcoming the consequences of force majeure on the contract inter alia by adaptation of the contract (Cf. Ph. Kahn, Force majeure et contrats internationaux de longue durée, Clunet 3/1975, p. 467 et seq.). This is the main reason to deal with force majeure in this connection. Although the preconditions differe from that in hardship-clauses in respect to the procedure for the solution of the problems and certain future consequences they may be similar if not identical. This may have consequences for other parts of the work on the Progressive Codification. In particular for the chapter on non-performance, but that shall not be elaborated on here. It is true, that not all force majeure clauses contain the aspect of adaptation.

A further category are impediments, though not making impossible the performance of the obligations affected, make them much more burdensome so that the equilibrum of the contract, as determined initially, is drastically disturbed or makes the performance useless for one party (the demand for products of a plant to be erected has disappeared, since substitute products are now available). The first case typically will occur with the debtor of the non-money-performance, the second one with the debtor of the money-performance.

Insofar as a distinction can be made between cases, where the concrete kind of impediment can be envisaged and therefore the consequences as well, and cases, where either the impediments are not foreseeable or their effects on the contractual obligations of the parties.

In order to deal with impediments of the former kind, clauses can be used which allow an automatic adaptation of the contract to such changes, like various clauses which maintain the value of the price, but in a certain sense also the "government take clause" and the "first refusal clause", as mentioned by Oppetit (L'adaptation des contrats internationaux aux changements de circonstances: la clause de "hardship" (Clunet 4/1974, p. 796; see also M. Fontaine, La clause de l'offre concurrente du client le plus favorisé et la clause de premier refus dans les contrats internationaux, D.P.C.I. 4/1978, p. 185 et seq.).

These clauses are applicable to cases where a hardship, as to be described below, has not yet occurred as well as to hardship cases.

Impediments of the latter kind can only be covered by the so called "hardship" clauses which are also applicable to impediments of the former kind, presupposing that they have reached the quality of a real hardship.

Having determined the position of hardship in the system and the means to overcome interference occurring in the course of the performance of an international commercial contract the general feature of a possible regulation of hardship shall be analysed.

First a terminological remark. The task of this paper as set out in UNIDROIT 1981, P.C. Misc. 3 is to propose rules on adaptation. As explained above adaptation may be required in different cases. This paper is confirmed to adaptation in hardship cases, though its results may be also useful in other adaptation cases. The denomination for such rules can of course be chosen in characterising either certain important aspects of the presuppositions (according to the respective legal concept as e.g. hardship, imprévision, Veränderung der Umstände) or of the legal consequences, as adaptation. The first choice seems to be preferable since the presuppositions are of an individual nature while the consequences are of a more general nature as just explained. Furthermore the term adaptation does not even exhaust all possible consequences of hardship.

A hardship regulation must comprise the following elements:

- The definition of hardship.
- The procedure to establish whether hardship has occurred, and, in the affirmative, which consequences shall apply, including the determination of the competent instances to take necessary decisions.
- The repercussions of a claim based on hardship on the contract, as long as the decision on the legal consequences is pending.

In order to ensure the practicability of a hardship regulation it should reflect the typical step by step behaviour of the parties, in other words develop a kind of algorithm to solve hardship cases. Some special problems like the consequences of avoidance or termination may be dealt with separately. They do not necessarily arise in every hardship case and eventually can also be cincluded into more general norms, e.g. on avoidance or termination in general.

The general approach to the drafting of proposals for the Progressive Codification has been described by Bonell according to UNIDROIT 1981, P.C. Misc. 3 as to "be based on current trade practice as reflected in international conventions or in instruments of purely private character such as general conditions or standard forms of contract, rather than on the principles traditionally adopted by the various national laws;" (p. 16).

This approach is of special importance in respect of hardship. In the legal regulation on the national and international level most problems of breach of contract are rather well elaborated. Quite the opposite in the case in respect to the problems of international gaps and of impediments. Some countries have regulations or established court practices covering elements of these problems (see M. Fontaine, "Les clauses de hardship Aménagement conventionnel de l'imprévision dans les contracts à long terme, D.P.C.I. 2/1976 P. von Ommeslaghe, "Les clauses de force majeure et d'imprévision (hardship) dans les contrats internationaux" Revue de Droit international et de Droit comparé, 1/1980 p. 7 et seq., in particular p. 13 et seq.; O. Lando, "Renegotiation and Revision of International Contracts", German Yearbook of International Law, vol. 23, Berlin (W) 1981, p. 37 et seq., in particular p. 48 et seq.; besides these regulations and the case law analyzed in these articles see also paragraph 295 of the International Commercial Contracts Act (GIW) of the GDR and Art. 107 of the Algerian Civil Law Code). International conventions are rather reluctant to deal with the problem of hardship.

This is especially true for the Convention on the International Sale of Goods. The same can be said of the model contracts and guides of the ECE, and even the FIDEC-conditions are confined to certain aspects of hardship, and so are the UNIDO draft model contracts on fertilizer plants. Only ICC has drafted a "Suggested hardship clause".

Apart from these few official documents on a governmental or a non-governmental basis the dollowing proposals are based on the analysis of the reported contractual practice (see in particular M. Fontaine, op.cit. p. 7 et seq., UNCITRAL, document A/CN.9/WG. V/WP.4/Add. 5, p. 19 et seq.)

PROGRESSIVE CODIFICATION OF INTERNATIONAL TRADE LAW

CHAPTER 3

PERFORMANCE

Section X (last section): HARDSHIP

Article a: Hardship as a Presupposition to Claim Renegotiation

(1) Where circumstances existing at the time, when the contract was formed have changed beyond the control of the party concerned and beyond the risks taken by him, with the result that the attainment of the aims recognizably persued with the contract by this party has been substantially injured (variant: has become impossible) in a manner which he could have neither foreseen nor avoided (hardship) and where this changement has occurred before the performance has been rendered, this party (the disadvantaged party) is entitled to claim renegotiation from the other party (the non disadvantaged party), inasfar as the contract does not foresee any other remedy for this situation.

(2) Where the disadvantaged party only exercises his right to claim renegotiation after a reasonable period after the date where the presuppositions for its exercise have occurred the other party is entitled to claim compensation for the damages caused by the delayed exercise of the right to claim renegotiation.

(3) The right to claim renegotiation expires if, after the presuppositions for its exercise have occurred, the non disadvantaged party has prescribed to the disadvantaged party a reasonable period for the exercise of his right to renegotiation and he does not claim renegotiation within this period.

Article b: Contents and Procedure of Renegotiation

(1) Apart the cases of subarticle 2 the parties have to renegotiate with the aim to adapt the contract to the hardship.

(2) Where (Variant: it is impossible for) the disadvantaged party is substantially injured to attain the aim pursued by him with the contract even with an adaptation of the contract he is entitled to claim renegotiation with the aim of a full or partial avoidance of the contract. Where it cannot reasonably be expected that the non disadvantaged party will agree upon the adaptation of the contract he is entitled to claim avoidance of the contract in the course of renegotiation, inasfar as the other party insists on such an adaptation.

(3) Where adaptation is sought commercial custom at the time of renegotiation has to be taken into consideration as well as all circumstances of the contract including the aims pursued by each party to the contract and good faith.

(4) Where avoidance is sought in considering the principles of article d) both parties have to strive for an avoidance of the contract which is connected with as little loss as possible for both.

Variant 1

(5) Where renegotiation does not succeed within (2-3) months after the disadvantaged party has exercised its right to renegotiation or avoidance and where the parties have not agreed upon a prolongation of this period either party is entitled to claim for adaptation or avoidance of the contract, as the case may be with the organ competent for the decision of litigations arising out of the contract.

Variant 2

Like variant 1, but insert after "... entitled to claim ..." "a recommendation"

Variant 3

Continue after "... either party is entitled" "to terminate the contract".

This has to be considered in Art. d) as indicated.

Article c: Contract during renegotiation

(1) Where the disadvantaged party is the obligee of the non-money performance he is entitled to claim from the other party the suspension of performance from the date of the exercise of his right to renegotiation up to the decision upon the hardship and its consequences inasfar as that may save expenses under the aspect of the consequences of hardship intended by the disadvantaged party.

(2) Where the disadvantaged party is obligor of the non-money performance he is entitled to suspend his performance from the date of the exercise of his right to renegotiation up to the decision upon the hardship and its consequences inasfar as this is possible without detrimental effects for the performances already rendered.

(3) Inasfar as the disadvantaged party does not attain the aims pursued with the exercise of his right to renegotiation he is responsible for the damages caused by his claim to suspend the contract according to sub Art. 1 or by his suspension of the contract according to sub Art. 2.

Article d: Settlement of Avoidance (variant: or Termination) because of Hardship

(1) Where a contract is avoided according to Art. b (2) (variant: or terminated according to Art. b (5)) only the non disadvantaged party is entitled to claim compensation of his expenses in respect of his non-money performances not yet rendered inasfar as he cannot use these performances otherwise. In respect of the non-money performances already rendered the non disadvantaged party is entitled to claim payment according to the conditions of the contract and the disadvantaged party to claim payment inasfar as the other party is in a position to use these performances, and restitution of the non-money performances at his expenses inasfar as the other party is not in a position to use them.

(2) Money paid, but not used for the payment of performances according to sub Art. (1) and also not set off has to be restored.

(3) Sub Arts (1) and (2) apply in a corresponding manner for partial avoidance (variant: and termination)

Remark: Termination has to be taken into consideration, if at b variant 3 is chosen.

EXPLANATION

Article a

This article tries to define hardship in determining the presuppositions for renegotiations as the primary legal consequence of hardship leading in its turn to different results. It also deals with the period for hardship claims.

Para. 1

This paragraph describes the most important feature of hardship that means, the relevant alteration of circumstances. These types of circumstances are not specified, though some clauses try to identify them. The ICC suggested Hardship Clause refers to economic, political (including modifications of legislation or administrative matters) or technical circumstances.

The relevant circumstances are characterized primarily by their effects. The effect must be that the aim which at least one party intended to achieve through the contract can no longer be attained. The party which is impeded in achieving his purpose is called the disadvantaged party. The other party is called the non disadvantaged party. Where both parties are affected by the alteration of circumstances both parties are the disadvantaged party and can rely on the respective rights. The proposal takes as a starting point that each party has pursued their own interests or aims by entering into the contract and therefore does not refer to the purpose of the contract as a whole, since this would require establishing a common purpose of the parties the proof of which may be difficult. Regularly the aim of the obligor of the non money performance is to make profit and the aim of the obligor of the money performance is to get a performance which is beneficial to him. The latter is true for both parties where they exchange non money performances.

In analysing the typical cases it is evident that the attainment of the aim of the obligor of the non money performance can mainly be disturbed by an increase in his costs (inflation) so that it becomes impossible to make a profit in fulfilling the contract, on the contrary, he will incur losses. That means that the original economic equilibrum of the contract is heavily disturbed. The same result occur, where the contract currency is devaluated.

The attainment of the aim of the obligor of the money performance i.e. the obligee of the non money performance, can be empeded primarily by events making the non money performance useless to him (the factory where

the machines bought shall be installed is destructed by an earthquake, the supply of certain raw materials becomes superfluous since indigenous sources have been discovered). The definition covers both cases. Under some aspects the proposal has to deal with them separately (see below).

Usually these general aims of each party are recognisable to the other party. However, in order to avoid that quite unique aims besome surprisingly relevant, the respective test has been added (aims recognisably pursued).

Alterations with minor consequences shall not be taken into consideration. Though the nature and importance of the events as such is not relevant their consequences for the contracts must be decisive. That means alterations which lead to a certain reduction of the profit expected or even to a certain loss are irrelevant. The consequences must be serious, e.g. the performance must be a substantial burden or useless as the case may be for either party. The importance of the alterations for the contract is described in an abstract manner in order to cover all relevant cases. Two variants are offered (the attainment of the aims has been substantially injured or has become impossible), the latter one being mire rigid than the former one. It has to be kept in mind that the impossibility to attain the aim pursued with the contract does not necessarily mean, that the fulfilment of the respective obligation has become impossible as well; as in force majeure cases.

The word "circumstances" shall indicate that event surrounding the contract are meant. Changements in such circumstances do not lead to hardship cases where they are influenced by the disadvantaged party or where this party is responsible for the changement, especially where he has taken over special risks in the contract. This will prevent mistakes in commercial speculations being declared as hardship.

Since the point of gravity to determine hardship cases according to the given definition consists in the description of the effects of the alterations of certain circumstances this idea has also been extended to the test of foreseeability. Therefore it should not been decisive, whether the alteration of the circumstances is foreseeable. This is often the case. It should be relevant, whether the consequences for the attainment of the aims of the parties are foreseeable (according to objective criteria). It goes without saying that the disadvantaged party has to use his best efforts to overcome the consequences of a changement in circumstances.

The alteration must have occurred in the time between the making and the performance of the contract. The time of the formation of the contract shall be the time of its signature, and not of its taking effect where this is dependant on a third person (governmental licence). An alteration of circumstances which has occurred before the formation of the contract, but has not been known by the party affected at that time accordingly does not lead to a hardship case.

On the other hand the change must have occurred before performance. That means alterations of circumstances can only be considered inasfar as they relate to performances not yet rendered. This limitation is necessary in order to avoid that performed contracts are discussed anew. This is so self evident that most contractual provisions do not even foreese this case. Nevertheless for a more general regulation this does not seem to be superfluous. Where performance has only been partially rendered, renegotiation may only relate to the part not yet rendered. It is true in case of termination because of hardship a solution has to be found for the performance already rendered (see Art. d). As well where only the money performance is still outstanding (wholly or partly) renegotiation because of hardship would only be possible in cases of striking devaluation.

The proposed hardship regulation is of a general nature and shall cover cases not regulated by the contract in greater detail (e.g. clauses for the maintenance of the value of the price). On the other hand insofar as such clauses are agreed upon, hardship clauses shall not be applied additionally since in these cases the parties have determined the settlement of the problem which shall not be changed by a general clause. For these reasons the last part of para. 1 has been inserted.

It should be decided by the informal working group whether it should be one further presumption for hardship that the alteration is definite. This criterion has not been included the proposal, since it might be difficult to establish, whether it is fulfilled because this requires looking into the future and moreover it must be kept in mind that even temporary alterations may require renegotiations though of a different nature than final ones.

Likewise it does not seem to be necessary to elaborate a clause for the case of realteration of circumstances. If this happens after a decision on the original hardship has been rendered this case is to be dealt as a new hardship. Given the rather general hardship clause as proposed it seems to be too easy to foresee mainly restorage of the original contract as in the example given in the UNCITRAL-document A/CN.9/WG.V/WP.4/Add. 5. This may be justified where the hardship clause is tailored to more specified cases.

Para. 2 and 3

Para. 2 and 3 are not derived from hardship clauses used in practice, but born out of theoretical reflections.

Para. 2 is based on the fact that as a general rule there is no prescription for the exercise of the right to renegotiate according to the proposal. However, where the disadvantaged party defers his claim to renegotiation this may increase the damages of the other party especially where renegotiations result in avoidance. In general, damages are not to be compensated in hardship cases. Although in this special case compensation seems to be justified.

Para. 3 shall create the possibility for a party who is afraid that his partner will invoke hardship, to ensure, whether this other party will do so or not. This might be of great importance where it cannot reasonably be expected of the non disadvantaged party that hr will agree upon the adaptation and would claim avoidance (Art. b (2)). Of course the right to renegotiation would only expire as far as it is based on alterations which have already occurred at the time, when the non disadvantaged party has the period prescribed.

The application of both of these paragraphs will be connected with some problems in particular in respect of the determination of the relevant periods. This is especially true when hardship does not occur as a sudden event, but consists of a continuous alteration over a longer period which at a certain date, not easily determined, reaches the point where the presuppositions of a hardship case are fulfilled.

Article b

The proposal is based on a procedure where at a first stage the parties have to conduct renegotiations by themselves. This article describes the criteria which shall be followed on this occasion under different assumptions (adaptation, avoidance, termination). Where the parties do not succeed in solving the problems the second stage of the procedure may start: the decision by a neutral organ.

It goes without saying and is not mentioned in the proposal that the first question to be decided either by the parties or by a neutral organ is whether hardship has occurred.

Para. 1

This rule stresses adaptation as the most important aim of renegotiation which normally shall be envisaged. That means avoidance or termination, respectively, are limited to the cases mentioned in para. 3.

Para. 2

This paragraph describes two cases of avoidance. The first case arises where it has become impossible to attain the purpose pursued by one of the parties (regularly the obligee of the non money performance) even if the contract is adapted. The second case is typical where the original equilibrum of the contract has been disturbed. In this case the equilibrum can be reestablished by increasing the price. In the event that it cannot reasonably be expected that the other party will pay the higher price, he may then claim avoidance of the contract. This can be prevented by the disadvantaged party in reducing its claim for adaptation to such a degree that it is acceptable for the other party (accoding to objective criteria).

Para. 3

This paragraph gives some guidelines for the adaptation to be observed in the renegotiation between the parties but also for the decision by a neutral organ, if any.

In classifying the criteria used for this purpose in practice often a distinction is made between objective, subjective and hybrid approach (see e.g. A/CN.9/WG.V/WP.4/Add. 5, p. 23). But it is not always easy to determine which criteria shall be attributed to which group. The approach of the proposal according to these schemes would be a hybrid one, though greater importance is given to the objective criteria contained therein. This is especially commercial custom at the time of the renegotiation. In other words the parties shall compare their contracts to a contract which average parties could make on the same subject at the time of renegotiation. This theoretical comparision between two contracts, a real and a fictituous one may lead to further decisions of the parties. One outcome might be that at least one of the parties would not have made such a contract as the fictituous one or is not in a position to make it at the time of renegotiation and this may indicate that termination of the real contract is the best solution (see sub Art. 2).

The result of the comparision may be corrected according to the other criteria. The circumstances of the contract include also the risk assumed by each party. The reference to good faith may contribute to the prevention of formal results. It has the function of a general clause.

Para. 4

This paragraph gives few guidelines for the renegotiation with the aim of avoidance. Also in this case negotiations are required and avoidance is not constructed as a unilateral act, since in most cases regulations have to be found in relation to the preparation already completed and the performances already rendered. Some general rules are given in Art. d, to which reference is made. It is also possible to terminate only a part of the contract.

Para. 5

There is no other effective method to force the parties to lead renegotiations or negotiations on avoidance to a successsul and and to observe the rules laid down in the preceding articles than to foresee obligatory decision by a third organ would have to observe the rules just mentioned.

The period given to the parties has been left since it depends on the character of the contract, but regularly 2 to 3 months should be sufficient. This period might be prolonged by the parties, in particular where a solution seems to be attainable.

The most important question of a hardship regulation is which organ shall make this decision. The proposal prescribed that hardship cases shall be decided by the same organ which is competent for the decision on litigation arising out of this contract, that means an arbitration tribunal or a court. Thereby the involvement of two decision making bodies would be avoided which produces disadvantages where hardship problems and other litigation is interlinked. For the time being arbitration tribunals and courts are not very accustomed to decisions shaping the contract. But hardship cases are a rather new appearance and they have to get more and more familiar with them. For this purpose they can use the normal auxiliaries like experts' opinions (e.g. concerning prices, technical changes etc.). While in some countries arbitration tribunal and courts are expressly allowed to take decision shaping the contract, they are in other countries forbidden to do so. (See the General Report of René David for the 10th International Congress of Comparative Law, Budapest August 1978, topic II.A.4. La technique de l'arbitrage comme procédé de revision des contrats). In socialist countries decisions by arbitration shaping the contract are allowed (see David and in respect of the law of the GDR H. Strohbach, "Die Revision von Venträgen durch Schiedsgerichtsverfahren", Berichte zum X. Internationales Kongress für Rechtsvergleichung, Budapest vom 23. bis 20 August 1978, herausgegeben vom Nationalen Komittee für Rechtswissenschaft der DDR, p. 69 et seq., in particular p. 74). In other countries at least such possibilities exist (see e.g. for Italy M. J. Bonell, "Arbitration as a means for the Revision of contracts",

Rapports nationaux italiens au Xe Congrès International de Droit Comparé Budapest 1978, Milano 1978, p. 220 et seq.). Where it is forbidden for arbitration (our court) to shape contracts like in England (see C.M. Schmitthoff "Hardship and Intervenar Clauses", Journal of Business Law 1980, p. 82 et seq.) third party intervention has to be agreed upon in order to solve problems connected with hardship clauses.

The different approaches to the functions or arbitration raise the question of enforcement of contract shaping decisions. Though a majority seems to be in favour of applying the international conventions on arbitration also for these decisions (see David), this issue is still in discussion. Furthermore the application of these conventions would not solve any problems, since they are not drafted for contract shaping decisions (see Strohbach, p. 76).

But the enforcement of the decision by third party interveners and comparable organs likewise may raise problems since they may be opposed on the basis of national law, that means they would not be final decisions like arbitration awards (see e.g. for the law of the FRG U. Loewenheim "Arbitrage als Verfahren zur Vertragsrevision", Deutsche zivil-, kollisions- und wirtschaftsrechliche Beiträge zum X. Internationalen Kongress für Rechtsvergleichung in Budapest 1978, Tübingen 1978, p. 83).

These procedural questions of course cannot be clarified in the framework of the Progressive Codification, but they form part of their background for offering some more variants. Another reason is that decisions in hardship cases may relate to matters of tremendous economic value. Parties therefore might hesitate to have them decided by neutral organs or have difficulties to find an organ acceptable for both of them.

These problems become less severe where the respective organ is only empowered to give a recommendation as foreseen in Variant 2.

Variant 3 allows either party to terminate the contract, where renegotiations do not succeed within the fixed period. This is a new presupposition for termination and not without danger, since it means that each party could obtain termination in any case, only by refusing adaptation.

Article c

The article deals with the behaviour of the parties towards their contractual obligations, where the decision on the consequences of hardship is pending. In most hardship clauses this problem is not regulated (see A/CN.9/WG.V/WP.4/Add. 5, p. 23). The ICC rules (adaptation of contracts,

Publication no. 326, rules, apt. 10) read: "Unless otherwise provided by the parties, the action of bringing a case before the Standing Committee does not of itself have any effect on the contract until the third person has made his recommendation or taken his decision". The ICC-suggested Hardship Clause takes a similar attitude. It does not seem to be realistic to require that the parties shall continue the performance of the contract even where one of them intends to avoid it. The proposed article therefore allows suspension at the risk of the party doing so.

Para. 1

This paragraph covers the case where the obligee of the non money performance is the disadvantaged party. Most often he then will either avoid the contract or alter the non money performance (letting aside the case of sharp decline in prices). Therefore it would make no sense to continue the performance of the contract, though it may be clear that it will not be performed in the original manner. But the contract shall not be suspended inasfar as the further performance would also meet the interests of the disadvantaged party.

As long as the non disadvantaged party has to suspend the fulfilment of its duties the corresponding obligations of the other party also will be suspended (especially payment). The consequences arising out of this are to be decided during the renegotiation process.

Para. 2

This paragraph covers the problem of suspension in cases where obligor of the non-money performance is the disadvantaged party. His typical aim in claiming for renegotiation will be to increase the price. He might try to enforce this aim by suspending performance. The proposal accepts a right of suspension, but with limitations. It is excluded inasfar as the performances already rendered may suffer from suspension (since e.g. deteriorations may occur during suspension).

Para. 3

This paragraph makes it clear that the claim for suspension or the suspension are at the risk of the party exercising them as the assertion of this party that a hardship case has occurred is not justified or inasfar as the claims based on this assertion are not accepted. This party then has to compensate damages caused by the suspension. (e.g. because of delay in the performance of the contract).

Where the claims of the disadvantaged party are accepted, wholly or partly, the settlement of eventual damages could be done in this connection and would form part of the renegotiation.

Article d

This article regulates the payment and restitution respectively of performances already prepared or rendered at the date of avoidance (or termination, if Art. b (5) variant 3 should be chosen) of the contract because of hardship. The principle envisaged is that the non disadvantaged party shall be compensated for his expenses in connection with the performance of the contract and its preparation as far as he cannot use them, but not for his damages caused by non performance, while the disadvantaged party saves costs inasfar as they would arise with the further performance of the contract. Furthermore he will be paid inasfar as his performances already rendered or prepared can be used by the other party. The non disadvantaged party is therefore in a better position. The right to avoidance has been granted in the interest of the disadvantaged party. Therefore this party should bear a greater part of the losses connected with hardship, though the hardship is not attributable to him. It is also not attributable to the other party. Because of this disequilibrum in the distribution of the losses it might be useful to have this special regulation. Nevetheless in a more advanced stage of the Progressive Codification it has to be checked anew, whether at least some of the regulations for avoidance or termination in general can be used for termination in hardship cases as well. Since the parties first have to negotiate avoidance, they may well find solutions more appropriate to their problems. This article in particular is necessary where a third organ has to take a decision.

Para. 1

This paragraph elaborates the principles just explained in more detail. From the first sencente it follows that the disadvantaged party may not claim compensation for his expenses in the preparation of his performances or for the execution of the contract in general (e.g. preparations for the taking over of performance rendered by the other party). The clear distinction between disadvantaged and non disadvantaged party made in the first sentence concerning performances not yet rendered and preparations, is also taken up in the second sentence concerning non money performances already rendered.

Para. 2

Money performances already rendered will be used to settle financial claims amongst the parties and only the balance will be restored. It is expected that the question of interest will be settled generally elsewhere in the Progressive Codification.

Para. 3

This paragraph takes into consideration the fact that hardship in certain might eventually be overcome by a partial avoidance of the contract.