Chapter 5: PERFORMANCE

Section 3: Hardship

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CHAPTER 5

PERFORMANCE

Section 3: HARDSHIP

Article 1
If the performance of a contract is rendered more onerous for one of the parties, he is nevertheless bound to fulfill his obligations.

Article 2
(1) In case of hardship the disadvantaged party is entitled to request renegotiations, insofar as the contract does not provide for any other remedy.
(2) The disadvantaged party has to exercise his right to request renegotiations without undue delay. The request shall indicate the grounds on which it is based.

Article 3
There is a case of hardship where:
(a) Circumstances arise which either make the performance of one party substantially more onerous or have the effect that a presupposition which is implicit in the very nature of the contract ceases to exist, and
(b) these circumstances arise or become known to the parties after the conclusion of the contract and could not reasonably have been taken into account at the time of the conclusion of the contract, and
(c) these circumstances are beyond the control of the parties, and
(d) these circumstances relate to a long-term contract and the performance affected has not yet been rendered.
Variant: add "and"

(e) these circumstances are not the result of risks taken over by the disadvantaged party".

Article 4

(1) On failure to open renegotiations, or in default of agreement within a reasonable period, the disadvantaged party is entitled to terminate the contract.

(2) The non-disadvantaged party may avoid termination according to paragraph 1 by making the disadvantaged party a reasonable proposal to adapt the contract without undue delay.

(3) Where the disadvantaged party does not accept the proposal according to paragraph 2, or where the non-disadvantaged party rejects termination according to paragraph 1, which he shall do without undue delay, the disadvantaged party may claim without undue delay to have the validity of the termination stated by the court.

(4) The court may decide, whether the contract shall be maintained in its original terms, or adapted pursuant to the terms as eventually proposed by the non-disadvantaged party, or whether the termination is valid.

(5) Where the termination is valid and upon request of one of the parties the court has to determine to what extent the performances rendered have to be paid and the money has to be repaid, taking into account to what extent the performances rendered can be used by the one or the other party and to which party's advantage the contract is terminated.
COMMENT(*)

Article 1

This article should make it clear that hardship "is not simply a question of changed circumstances, but of an extraordinary change of circumstances leading to imbalance beyond the normal risks of the contract" (see UNIDROIT 1986, P.C. - Misc. 9, p. 14).

It is intended to contribute to determine which risks are to be borne by the disadvantaged party and, therefore, cannot form the basis for invoking hardship.

On the other hand, it might be argued that the provision is superfluous, either because the principle is covered by Art. 1 of the chapter on performance (UNIDROIT 1985, Study L - Doc. 34), or because this latter provision could be improved accordingly. In any case, the idea belongs in that context. The risks taken by the disadvantaged party could be covered by a special provision (Art. 3 lit. (e) in the present draft), which would make the idea even clearer.

Article 2

It seems to be preferable to make a distinction between the definition of hardship (now Art. 3) and the operative provision dealing with the principal legal consequences of hardship (Art. 2). The concept of hardship is so complex and requires the consideration of so many criteria that to have both the determination of these criteria and the legal consequence of hardship in one provision would make the latter too complicated.

The first legal consequence of hardship is the right of the disadvantaged party to renegotiate.

This does not exclude that also the other party may propose an adaptation in order to ensure that the contract affected by unforeseen circumstances will nevertheless be performed. But it does not seem necessary to grant the non-disadvantaged party a right to this effect. Where the other party refuses adaptation he is bound by the original terms of the contract.

(*) For general remarks see UNIDROIT 1983, Study L - Doc. 24, pp. 1-7
The right to renegotiate may be excluded by the contract either expressly or, mainly concerning certain hardship cases, by the establishing of other remedies such as, for example, automatic adaptation clauses for the contract price.

While the former case is self-evident, the latter one has been mentioned expressly.

Paragraph 2 specifies the requirements of time and form of the right to renegotiate. In order to clarify the situation as fast as possible, and to avoid that the right to request renegotiation becomes an object of speculation, this right must be exercised without undue delay. The disadvantaged party is induced to do so also by Art. 3 lit. (d). It seems impossible to determine a precise period of time within which this right must be exercised, all the more so as the reasons for hardship may develop gradually, with the result that no exact date for that period to start can be established, and a complex assessment of the whole situation becomes indispensable. The indication of the grounds is intended to enable the non-disadvantaged party to judge for himself whether or not the request is justified. Article 2, para. 2 is inspired by the drafting suggestions for hardship provisions of the ICC (Doc. 460/INT.167, para. 2).

Article 3

Article 3 defines hardship by listing certain conditions which are intended to be cumulative.

Lit. (a) describes the most important conditions by specifying two main cases. The first one concerns a severe disturbance of the equilibrium of the contract, in other words, the performance of one party becomes substantially more onerous. The word "substantially" indicates that certain grievances, and not only those of a minor nature, shall not count. But the increase several times over of the price of raw materials should be covered as should new safety regulations which require far more expensive technical solutions. Since in practice each single case may be very different, an exact or quantitative description is neither possible nor advisable. The second case relates to situations where the purpose of the contract cannot be attained any more (e.g. the plant which was to be constructed according to the contract has been destroyed by an earthquake, etc.).
In such cases one could say that a presupposition which is implicit in the very nature of the contract ceases to exist. The assumption here is that both parties are aware of this presupposition. It does not suffice that one party has a particular motive for making the contract, and that this motive, which is unknown to the other party, no longer exists as a result of the later development of events (e.g. one party buys something for reexportation into a third country, but this reexportation, which was unknown to the seller, is later on prohibited in the context of embargo measures).

Lit. (a) tries to identify hardship cases by describing them. A different approach would be to relate to the expectations of the non-disadvantaged party as the Netherlands Civil Code does (Book 6, Chapter 5, Section 3, Art. 11, para. 1 "of such a nature that the other party is not entitled to expect, according to standards of reasonableness and equity, that the contract should be maintained unchanged"). But this approach, though more flexible, is even more abstract.

Lit. (b) clarifies that only circumstances which arise after the conclusion of the contract can be accepted as hardship. There is only one exception, namely that the circumstances existed before, but the parties did not know of them. In practice, it is important to see whether or not the disadvantaged party knew of the circumstances. Where the other party knew them and did not inform the disadvantaged party, the former party is not allowed to rely on the fact that the circumstances were known before the making of the contract (venire contra factum proprium, lack of good faith).

But also circumstances which had not yet occurred at the time of the conclusion of the contract, but which could have been taken into account at that time, cannot be accepted as hardship. What is decisive where it has to be assessed if certain circumstances reasonably could have been taken into account, is not so much whether it is thinkable that such and such a circumstance may occur, but whether it is probable that the performance of the contract would be disturbed by the occurrence of certain circumstances, and if so to what extent. In that connection neither an over-optimistic nor an over-pessimistic approach can be taken as a yardstick.

Lit. (c) expresses something which should be self-evident, i.e. that only such circumstances which are beyond the control of either of the parties are covered. Where this is not the case, the rules on responsibility or on obstacles caused by the obligee, respectively, would come into play.
On the other hand, that the disadvantaged party is not able to overcome the consequences of the hardship cannot be made a criterion, as it is in the very nature of hardship, as distinguished from force majeure, that the consequences can be overcome, even if with unreasonable costs or other efforts.

Lit. (d) limits the concept of hardship to long-term contracts. These are contracts where the period between the making and the final performance of the contract is rather long, as a rule one year or more. The idea is that risks arising out of short-term contracts are less important and can be taken into consideration more easily, so consequently they should be borne by the party affected. Furthermore, hardship can only be invoked in relation to performances not yet rendered, i.e. the request for renegotiation must be made before performance, as by performing the aggrieved party may be considered to have overcome the hardship.

Lit. (e) could be included if Art. 1 is deleted, but even in this case the idea would appear in some other provisions as well, e.g. Art. 3, para. (a) and even (d). Therefore lit. (e) has been proposed as a variant.

Article 4

This article determines in detail the correct behaviour in case of hardship.

The normal situation is that renegotiations in accordance with Art. 2, para. 1 succeed. But they may fail, either in cases where the other party (the non–disadvantaged party) is not prepared to renegotiate at all, or where both parties cannot reach an agreement as to the contents of the adaptation. Paragraph 1 fixes no time limit for the renegotiation to succeed - this clearly depends on the circumstances. Furthermore, such a time limit does not seem to be indispensable, as the consequences of an initial failure of the renegotiations are not rigidly determined. No provision is made empowering a court or arbitral tribunal (in the following the term "court" includes arbitration) to decide as to the contents of the adaptation; only the right of the disadvantaged party to terminate the contract is provided for.

Whether or not a party, in particular the disadvantaged one, is entitled to damages where the other party obstructs renegotiation, should be regulated in the context of non-performance.
The non-disadvantaged party may accept termination. Where he does so only in principle, the settlement as to the contract may be decided by court according to para. 5. But if he does not accept termination he may proceed according to para. 2, that is to say, he may submit a concrete proposal for adaptation. The proposal must be reasonable. This solution is inspired by Art. 1467 of the Italian Civil Code.

The criterion of reasonableness is not defined in detail, which would be difficult considering the variety of possible cases. Where a yardstick is considered necessary, this may be found in the solution the parties would have chosen, if at the time of the making of the contract they had known the circumstances as subsequently changed.

Where the disadvantaged party accepts the proposal of his partner the problem is solved. The mode of acceptance, including the time limits, depends on the terms of the contract or on the applicable law relevant to the modification of the contract. Where this party does not accept he has, according to paragraph 3 the possibility to have the validity of the termination stated by a court.

In other words, he has to take the initiative and remains responsible for the performance of the contract, where the court does not confirm termination.

The same situation arises where the non-disadvantaged party rejects termination without making a proposal for adaptation. The rejection has to be exercised without undue delay. The disadvantaged party on his part also has to act without undue delay. The consequences of not complying with this provision are to be taken from the chapter on non-performance, but neither party should be deprived of the option of either rejecting termination of having the termination confirmed, as the case may be.

Where the disadvantaged party claims confirmation of the termination, the court has three options as indicated in para. 4: it may uphold the original contract, it may accept the proposal of the non-disadvantaged party, possibly as amended during the proceedings, or it may confirm the termination of the contract.

This looks rather rigid, but nevertheless the court will have certain possibilities to influence the parties so as to reach a reasonable agreement. This is particularly true where the decision is made by arbitration.
Since the court in relation to termination only has to decide whether or not it is valid, the date of termination would be the date where the original declaration of termination becomes effective. Paragraph 5 gives a rather flexible rule for the settlement of the contract where the parties have agreed upon termination in principle but did not find a solution as regards the settlement, or where the termination has been confirmed by the court. Nevertheless, some criteria seem recommendable in order to give a certain guidance to the court. In either case a special claim has to be made by one of the parties to initiate such a settlement by the court.