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Chapter [...]

LIMITATION OF RIGHTS

(Revised draft prepared by Professor Peter Schlechtriem in the light of the discussions of the Working Group at its 3<sup>rd</sup> session held in Cairo, 24-27 January 2000)

Rome, December 2000

## INTRODUCTORY REMARKS

At its third session held in Cairo from 24 to 27 January 2000, the Working Group has discussed of a revised draft Chapter on Limitation of Rights by Prescription which took into account the decisions taken by the Group at its second session held in Bozen. The draft provisions set out below take into account the discussions the Group had on both documents in Cairo (UNIDROIT 1999, Study L - Doc. 64 and 2000 Study L - Misc. 22, paras 4-345).

In order to highlight the changes made to the previous draft the rapporteur has reported them in his notes.

## Article 1

**(1) Rights of parties governed by these Principles can no longer be exercised by reason of the expiration of a period of time. Such a period of time is hereinafter referred to as »limitation period«.**

*Note by the Rapporteur:*

The formulation »rights governed by these Principles« was the result of a lengthy discussion in Cairo and it was based finally on a proposal by Prof. Farnsworth (see Summary Records (S.R.) no. 50, 54). The comments should make it clear that the term »rights« covers all claims and actions - as phrased in the rapporteur's previous draft -, which may arise under the Principles, whether they are precontractual or contractual, caused by a breach of contract or its invalidity, whether the parties are direct contractual partners or third parties beneficiaries, etc. The term »rights« also should avoid sophisticated discussions about the dogmatic qualification of claims etc. (see S.R. no. 53).

**(2) The limitation rules herein shall not affect a particular time-limit within which one party is required, as a condition for the acquisition or exercise of his rights, to give notice to the other party or perform any act other than the institution of legal proceedings.**

*Note by the Rapporteur:*

This para. was proposed in response to concerns that the limitation rules could be misunderstood as colliding with cut-off provisions in connection with notice requirements. Proposals to add a provision defining the »reasonable period of time« as a period of three weeks (see S.R. no. 60) were not taken up.

**(3) In these rules**

**(a) an »obligee« means a party who asserts or may assert a claim, whether or not such a claim is for a sum of money or any other performance, or who may exercise any other right under a contract;**

**(b) an »obligor« means a party against whom an obligee asserts or may assert a claim or a right;**

**(c) »legal proceedings« include judicial, arbitral and administrative proceedings;**

**(d) »person« includes corporation, company, partnership, association or entity, whether private or public, which can sue or can be sued;**

**(e) »year« means a year according to the Gregorian calendar.**

*Notes by the Rapporteur:*

The para. is based on Art. 1 (3) UN Limitation Convention.

It was left to the final stage of drafting whether the term »obligee« has to be defined.

In the light of the later discussion on suspension by ADR it should be considered whether a definition of »Alternative Dispute Resolution« should be added. The rapporteur tends to omit a definition because ADR appears in many forms which could hardly be covered by a satisfying definition.

## Art. 2

*Preliminary remarks of the rapporteur:*

The crucial question of any set of limitation rules is the length of the limitation period. The working group had opted in Bozen for a two-tier system, i.e. a combination of a shorter period of time commencing on knowledge or constructive knowledge of the obligee of its right, and a longer period of limitation commencing upon »accrual« of the right. In addition to determining the length of the two periods of limitation, suspension and interruption are of great importance. The discussion in Cairo, therefore, was not only quite heated in regard to the respective lengths of the two limitation periods but was also sometimes a bit confused by notions of suspension and interruption. At the end, however, the group had agreed to adopt a short three-year period and a ten-year period as the absolute time limit (see S.R. no. 96).

**(1) The regular period of limitation is three years. It begins to run from the day after the day the obligee knows or ought to know the facts on which the right has become due.**

*Note by the rapporteur:*

The commencement of the shorter period of time was discussed at length, in particular, whether knowledge (or constructive knowledge) of the right itself or its having become due should be decisive. The latter was agreed upon (see S.R. no. 119., 122.). It was also discussed at length what exactly was meant by »has become due« and its relation to the exercise of rights. It was, however, agreed that it would be enough to explain in the comments that »has become due« means that a right could be exercised effectively (see S.R. no. 138).

**(2) Unless para. 1 applies, the period of limitation is ten years. This period of limitation commences on the day after the right accrued.**

**(3) The limitation period in para. 1 also applies to ancillary claims [such as claims for interests].**

*Notes to para. 3 by the rapporteur:*

If the principal of a debt becomes due on a certain date, but the debtor does not pay, the creditor's claim will be barred in most cases under para. 1 after three years. Nevertheless, since the debtor was in default, claims for interest arise continually at least until the limitation period for the principal has ended. Likewise, the creditor might have incurred costs and losses by the debtor's default. The question, therefore, is whether these claims which accrue later than the claim for repayment of the principal should be time-barred at the same time as the principal. The latter is the solution of the Zimmermann-draft (Art. 17:119). The Group has decided to the contrary: Since - e.g. - the last interest might have accrued shortly before the limitation period for the principal has ended, the creditor would have only a very short time before losing his interest claim under the Zimmermann proposal (see decision of the Group at S.R. no. 160).

Although the most important »ancillary« claim would be for interest in case of breach, e.g. default to pay, it could also be interest agreed upon by the parties in case of delayed repayment. »Ancillary« claims also include the claims for liquidated damages or a penalty, e.g. where the penalty increases with every month or year of delay in (re)payment or other performance.

**(4) The parties can modify the periods of limitation. They cannot shorten the period of limitation in para. 1 to less than one year from the time on the obligee knew or ought to have known of his right, and the period of limitation in para. 2 to less than 4 years from accrual. The parties can also prolong the period of limitation in para. 2 up to 15 years.**

*Notes by the rapporteur:*

The shortening of the limitation period of para. 1 by agreement to no less than one year was agreed upon by the Group (S.R. no. 171). It was also discussed, whether the »day after« phrase should be used in this context, but the majority regarded this as unnecessary (see no. 198). The prolongation up to 15 years was agreed upon by the Group (only) for the ten-year period in Art. 2 (2) (see S.R. no. 196).

The Group has also discussed, whether similar to Art. 22 (2) UN Limitation Convention the debtor should be allowed to extend the period of limitation by a (unilateral) declaration in writing to the creditor. The reporter was asked to give some thoughts on this topic. My proposal would be that besides consensual modifications within the limits of Art. 2 (4) a unilateral »declaration« of the debtor should be covered (only) by Art. 4 (1), dealing with the effects of an acknowledgement by the debtor/obligor (see S.R. no. 201 et seq.).

### Art. 3

**The limitation periods under Article 2 can be suspended or interrupted. A »suspension« of the limitation period means that during a suspension the limitation period ceases to run for the time of the existence of the event causing suspension,**

**while »interruption« causes the limitation period to begin again at the time stated in the special provisions on interruption.**

*Note by the rapporteur:*

The final drafting of this provision was left to the drafting group (see S.R. no. 207); the remark by Bonell as to the usefulness of definitions (no. 208) should be considered.

#### Art. 4

**(1) Where the obligor, before the expiration of the limitation period, acknowledges the right of the obligee, a new limitation period [under Art. 2 (1)] shall commence to run from the date of such acknowledgement.**

*Notes by the rapporteur:*

While the provision in substance was agreed upon by the Group, it was left to the rapporteur whether a specification of the new limitation period was needed (S.R. no. 219). In addition, the distinction of an agreement of the parties and the unilateral acknowledgement should be made clear in the comments. The rapporteur proposes two comments:

a) The interruption by acknowledgement should refer only to the short (3 year) period of limitation of Art. 2 (1): It was a basic policy decision of the Group that the obligee should have a chance to pursue his right, i.e. the short limitation period should begin to run (only) on actual or constructive knowledge of the respective right. If the obligor/debtor »acknowledges« the right, this at least lets the obligee know about his or her right so that now there is a fair and reasonable three-year chance to pursue the respective claim. The rapporteur, therefore, proposes to insert the words »... a new limitation period *under Art. 2 (1)* ...«.

As to the relationship between an acknowledgement and a promise (see S.R. no. 220), the parties are always free under Art. 3.2 of the Principles to create a new obligation by novation, regardless of whether the original right is already barred by the statute of limitation or not. It is, however, a matter of interpretation of an exchange of communications between the parties whether they only meant an »acknowledgement« of a disputed claim, thereby interrupting the running of the period of limitation, or whether they wanted to create a new obligation.

**(2) The obligor can acknowledge expressly or by conduct. Express acknowledgement can be orally or in writing.**

*Note by the rapporteur:*

The Group decided that such a rule would be helpful regardless of the meaning of »conduct« in the context of offer and acceptance (see S.R. no. 233). The Group had decided, however, to omit examples of relevant conduct in the black-letter rule and mention them only in the comments. Acknowledgement by conduct can be expressed by part-performance, payment of interest, by

providing of adequate security etc. A conditional acknowledgement should operate only as an interruption if the condition is met. A part-acknowledgement interrupts the running of the period of limitation only in regard to the acknowledged part of the claim (see discussion S.R. at no. 234, 235).

#### Art. 5

**(1) The limitation period shall cease to run when the obligee performs any act which, under the law of the court where the proceedings are instituted, is recognized as commencing judicial proceedings against the debtor or as asserting his claim in such proceedings already instituted against the obligor, for the purpose of obtaining satisfaction or recognition of his claim. [The exact date of the commencement of judicial proceedings is determined according to the law of the court where the proceedings are instituted].**

*Note by the rapporteur:*

The Group had discussed at length whether the commencing of court proceedings should cause an interruption or a suspension of the period of limitation; it was finally decided to adopt the suspension solution (no. 268). There was also support for the formula in Art. 13 UN Limitation Convention (see S.R. no. 267); the rapporteur, therefore, has assimilated the phrasing to the UN Convention's text. The second sentence (in brackets) is proposed as a clarification.

**(2) Where the parties have agreed to submit to arbitration, para. 1 applies accordingly; the exact date of commencement of the arbitral proceedings is determined by the applicable rules of arbitration.**

**(3) In the absence of regulations for an arbitral proceeding or provisions determining the exact date of the commencement of a judicial or arbitral proceeding, proceedings shall be deemed to commence on the date on which a request that the claim in dispute should be adjudicated is delivered at the habitual residence or place of business of the other party or, if he/she has no such residence or place of business, then at his/her last known residence or place of business.**

**(4) Suspension under para. 1 or 2 lasts until a final decision or award has been issued by the court or arbitration tribunal, or until the case has been otherwise disposed of, e.g. by settlement or by withdrawal of complaint or an application for an award.**

*Notes by the rapporteur:*

- a) The Group had at first discussed whether the wording should correspond more to Art. 14 (1) and (2) of the UN Limitation Convention. There were also proposals to replace »accordingly«

in (2) by rephrasing Art. 5 (2) as follows: The same effects apply where the parties have agreed ... (see S.R. no. 270).

b) The para. 4 was proposed by the rapporteur in his draft submitted to the Cairo meeting, but - according to the minutes - not discussed.

c) The discussion had, before settling all problems on drafting turned to ADR and whether it was advisable to add a provision on suspension by (commencement of ?) mediation, alternative dispute resolution and the like. There was obvious reluctance of the majority to propose a respective provision because ADR is still a rather amorphous enterprise, regulated only in a few countries (Japan has, to the knowledge of the rapporteur, an act on ADR), so that it would be hazardous to attach legal consequences on a »procedure« widely diverging from country to country, unclear in its structure and scope, etc. From reading the minutes the rapporteur got confirmation of his conviction that ADR should (only) have effect on the running of a period of limitation if the parties agree so. The Group had not objected to the proposal of the rapporteur that Kronke and Herrmann should send preliminary drafts on a black-letter provision dealing with the effects of ADR and conciliation proceedings; these proposals did not come in so far. Following the proposal of Farnsworth (S.R. no. 292), this rapporteur tentatively drafted the following rule:

**(5) Where the parties have agreed to alternative dispute resolution, mediation or any other comparable proceedings to resolve their dispute, they are presumed to have suspended the limitation period by their agreement; each party can unilaterally terminate the suspension orally or in writing.**

#### Art. 6

**(1) Where, as a result of a circumstance which is beyond the control of the obligee and which he could neither avoid nor overcome, the obligee has been prevented from causing the limitation periods to cease to run, the limitation periods shall be extended so as not to expire before the expiration of one year from the date on which the relevant circumstances ceased to exist.**

#### *Notes by the rapporteur:*

a) The new formulation of Art. 6 (1) is taken from Art. 21 UN Limitation Convention (see S.R. no. 303).

b) A slight change seems to be necessary, however, since the UN Limitation Convention provides only for one limitation period, while our draft is based on the two-tier system. It has to be decided, therefore, whether the ten-year period should also be prolonged if the obligee was prevented from claiming. This is a policy decision, probably not within the competence of the drafting group. The rapporteur, nevertheless, taking into account the basic decision the for two-tier system, namely, that the shorter period of limitation is justified, if and in so far as the obligee had a chance to pursue his claim, regards it as logically compelling that the ten-year period must



also be prolonged, if circumstances beyond the control of the obligee prevent him/her from pursuing the unknown right, even if he/she would have known it.

**(2) Para (1) also applies to cases where the right of the obligee could not be pursued because of incapacity or death of the obligee. The suspension ceases when a representative for the incapacitated or deceased party or its estate has been appointed or a successor inherited his position; the additional one-year period under para. (1) applies respectively.**

**(3) Para. (1) and (2) apply respectively in cases of death or incapacity of the obligor from the time the obligee is effectively prevented from pursuing his/her right.**

*Notes by the rapporteur:*

Both paras were approved, see S.R. no. 305.

**(4) In case of bankruptcy of the obligor, the dissolution or liquidation of a corporation, company, partnership, association or entity being the obligor, the running of the limitation period shall be suspended when the obligee has asserted his/her right in such proceedings for the purpose of obtaining satisfaction or recognition of the right, subject to the law governing the proceedings; the suspension ends with a final decision or award in these proceedings.**

*Note by the rapporteur:*

There was a lengthy discussion only on the question whether in addition to the suspension an additional period of Art. 5 (4) should be added; this was finally declined (see S.R. no. 316).

#### Art. 7

**(1) Expiration of the limitation period entitles the obligor to invoke this expiration in any legal proceeding as a defence against any claim or action based on the expired right.**

**[(2) Notwithstanding the expiration of the limitation period, a party may rely on the right as a defence or for the purpose of set-off against a claim asserted by the other party, provided that in the latter case this may only be done ...]**

**[(3) Where the obligor performs a right after the expiration of its limitation period,**

**the obligor shall not on that ground *alone* be entitled to claim restitution even if he/she did not know at the time of performance that the limitation period had expired.]**

*Notes by the rapporteur:*

In discussing the rapporteur's proposal of Art. 7 the debate revolved around three issues:

a) Whether the expiration of the period of limitation should cause an extinction of the right or only a defence against claims stemming from that right. From the minutes a tendency of the Group could be derived that the solution of Art. 24-26 UN Limitation Convention should be followed, which is based on the notion that the right is not extinguished, but only claims arising from the right could be repulsed by invoking the defence of expiration of the period of limitation. Consequently, the right could still be used as a defence or even for the purpose of set-off (see Art. 25 (2) UN Limitation Convention); since the provisions on set-off have not yet been laid down, the respective limitation provision is proposed here incomplete and only in brackets.

b) A second issue was whether the court should take the expiration of the period of limitation into account *ex officio*, or whether it is a defence that must be *invoked* by the defendant. Although no express vote was taken on this issue, the rapporteur dares to read between the lines of the minutes that the defence must be raised by the obligor in order to be considered by the courts.

c) The issue of restitution of a performance after the period of limitation has expired was not decided, but there seemed to be a strong opinion in favour of the solution of Art. 26 UN Limitation Convention. The rapporteur, therefore, has proposed a respective provision in brackets. His hesitancy to deal with this question in his first draft was caused by the deep division between continental and English law on the question of the decisive »unjust« factor for unjust enrichment claims. Under continental law, where the lack of an obligation is the decisive unjust enrichment factor, it is only consequent to bar restitution if after expiration of the period of time the right is still existing, but (only) not enforceable: If the obligor performs voluntarily, nevertheless, he cannot claim back, because the obligee received what was owed under his/her right to him/her. Where, however, the operative »unjust factor« is some error of the payor, matters might be different, if the payor did not know that the period of limitation has lapsed. Despite being a policy question, it should be considered, however, to include a rule like Art. 26 UN Limitation Convention in the present text; therefore, the rapporteur has proposed a respective provision in brackets. There was, however, concern by the rapporteur that in certain situations where the payor has paid on account of fraud, undue influence, coercion etc. of the payee, the payor should not be excluded from restitution, despite that he/she paid after the period of limitation has expired. Although reluctant to draft a respective black-letter rule, the rapporteur followed the suggestion of Farnsworth (no. 338) to chose a formula that leaves open restitutionary claims in case of performance induced by fraud etc. This was tried by the rapporteur by including the words »alone« and striking the words »in any way« from Art. 26 UN Limitation Convention.