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**Working Group for the preparation of  
Principles of International Commercial Contracts (3rd)  
Drafting Committee  
First session  
Hamburg, 3 – 6 March 2008**

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**Minutes  
of the Meeting of the Drafting Committee  
(Hamburg, 3 - 6 March 2008)**

Working Group for the preparation of  
Principles of International Commercial Contracts (3<sup>rd</sup>)  
Drafting Committee  
Hamburg, 3-6 March 2008

**Session 1:**  
**Pluralities of Obligors and/or Obligees**

(Unidroit 2008 Study L – WP.14)  
Reporter: Marcel Fontaine

Minutes

Present:

Prof. Joachim Bonell  
Prof. Marcel Fontaine  
Prof. Michael Furmston  
Prof. Roy Goode  
Prof. Reinhard Zimmermann

Keeper of the Minutes: Dr. Sonja Meier

1. Zimmermann welcomes the participants. Bonell expresses his thanks to the Max-Planck-Institute for acting as a host and to the reporters of the drafts. Bonell points out the importance of having complete drafts with black-letter-rules and comments at the next meeting of the whole group in Rome. Furmston explains that the comments in his draft on illegality are meant to be explanatory remarks for the working group and should not be regarded as a draft for the final version of his chapter. He indicates that the form of his draft is due to the special problems of illegality and to his own approach on the matter. The question is deferred to the discussion on the chapter on illegality.

2. Fontaine introduces his draft on pluralities. The comments should be understood as being explanations for the working group, not as a draft for the comments in the final version.

## Section 1: Plurality of obligors

### Definitions (Art. 1.1)

#### *Draft Art. 1.1*

*When several obligors undertake the same obligation towards the same obligee:*

- 1) the obligations are separate when each obligor is bound only for its share;*
- 2) the obligations are joint and several when each obligor is bound for the whole obligation.*

3. Fontaine explains that there is no requirement that the obligations have been undertaken by “the same contract”. There is no such requirement in any national legal system. The comments will explain that the obligations are usually undertaken under the same contract, but they will also give examples of other cases.

4. Fontaine explains that it had been previously decided not to include communal obligations. There is general agreement on this decision.

5. As to terminology, Zimmermann points out that the PECL, the CFR and the present draft use different terms, which might be confusing. The PECL speak of “solidary” and “separate” obligations (Art. 10:101), the CFR of “solidary” and “divided” obligations (III - Art. 4:102), whereas the draft uses “joint and several” and “separate” obligations. The question of terminology has, however, already been discussed and decided by the group.

6. It is agreed that further rules on separate obligations are not needed.

7. The question arises whether the actual wording of the beginning of the article may lead to misunderstandings concerning separate obligations (Zimmermann). Can one speak of “the same obligation” when there are separate obligations where each obligor is only bound for its share? According to Fontaine, “the same obligations” is intended to mean “the same substance of obligation”. It is discussed whether cases where each obligor undertakes his own obligation towards the obligee (and possibly also obligations towards the other obligors) are covered by Art. 1.1, i.e. whether one can speak of “the same obligation”, or whether the article should start with “when several obligors undertake obligations towards...” (Furmston). According to Zimmermann, it might be better not to include a superstructure in form of a general statement (“undertake the same obligation”) covering both forms of pluralities. The PECL avoid this problem by saying: “Obligations are solidary when..., Obligations are separate when...”.

It is agreed that Art. 1.1 shall define the scope of application of the Principles. It is also agreed that the wording of the first line in Art. 1.1 in its present form should not be included, but that the line cannot be simply deleted. The best solution may be to follow the model of the PECL (Obligations are joint and several when..., Obligations are separate when...). The fact that there is a plurality of obligors has to be mentioned. A question for consideration is whether, in case of joint and several obligations, the right of the obligee to receive the performance only once should be mentioned.

It is also agreed to change the sequence and firstly mention the joint and several obligations (being more important in practice), secondly the separate obligations.

## Sources of joint and several obligations (Art. 1.2)

### Draft Art. 1.2

(1) *When several obligors undertake the same obligation towards the same obligee, they are deemed to be jointly and severally liable, unless the circumstances indicate otherwise.*

8. This presumption of joint and several obligations had already been agreed on in Rome. The rule does, contrary to Art. 10:102 I PECL, not mention contractual terms excluding joint and several obligations. It is understood that such a contractual term is included in “unless the circumstances indicate otherwise”. It is discussed whether such contractual terms should be specifically mentioned or whether there should be a general indication that all rules in this chapter are of a non-mandatory character.

*[(2) Joint and several obligations also arise when several persons are liable for the same damage.]*

9. This rule was discussed in Rome. There has not yet been any decision on it.

It is discussed whether this rule is needed.

A rule of this kind can be important in cases of multiple tortfeasors. It is however, pointed out that the Principles do not deal with tort claims (Bonell, Goode).

The question arises whether the rule could be useful for cases of damages for breach of contract. Where joint and several obligors under the same contract are responsible for a damage (loss) arising from a breach of contract, their joint and several obligations to pay damages arguably follows from the fact that they are joint and several debtors, so that a special rule is not needed for this case.

Zimmermann points out that there may be situations where several persons are contractually liable for the same damage (loss) without there being a common contract. This is the case where breaches of different obligations arising from different contracts lead to a single damage (loss). Example: The obligee who intends to have a house built engages a building contractor and, by a second contract, an architect. The building contractor works defectively and thereby causes a loss. The architect neglects his contractual duty to supervise the building contractor; if he had supervised him, the loss would not have happened. It seems that both are liable for the same damage, albeit their obligations arise from different contracts.

German law regards this as a case of solidarity. According to French law, the obligations of the building contractor and the architect are *obligations in solidum*, which is not the same as, but similar to, contractual solidarity (*solidarité*) (Fontaine).

Goode and Furmston point out that according to English law this is not a case of joint and several obligations because the sources of the obligations are different. They argue that there is not “the same obligation” but simply independent obligations, which should not be governed by the Principles’ provisions on joint and several obligations. If the obligee concludes a settlement with the building contractor, this should arguably not affect the position of the architect (Furmston). In cases where several persons are liable for the same damage, there may be a joint and several *liability*, but not joint and several *obligations* (Goode).

Bonell argues that debtors liable for the same loss could be liable in different amounts, which is not compatible with the notion of joint and several obligations.

According to Zimmermann, the technical English rules on joint and several obligations need not be a model for the Principles. There is a discussion on whether the PECL would regard the case of the architect and the building contractor as a case of solidary obligations. According to Zimmermann, the building contractor and the architect have to pay the same amount of damages for a single loss and therefore have to render “the same performance”

under Art. 10:101 (1) PECL. According to Goode, “performance” in this article means only the performance contractually owed (building, supervising), not an obligation to pay damages. It appears that there is fundamental disagreement on the notion of “joint and several obligations”, in particular on the question whether joint and several obligations can only arise under the same contract. The Drafting Committee has no authority to decide this question (Fontaine).

Bonell asks whether these different views lead to different results. It seems that there are indeed differences, in particular concerning contribution and prescription.

Regarding this discussion, it is feared that Art. 1.2 (2) may lead to uncertainty (Furmston). According to Bonell, cases of liabilities from different sources (architect and building contractor) are rare and do not justify a rule leading to fundamental disputes.

The majority is in favour of deleting the rule. The question should be dealt with in the comments. The final decision on the notion of joint and several obligations is left to the next Rome meeting.

*[(3) Joint and several obligations also arise when the promised performance is indivisible.]*

10. Fontaine explains that rules on indivisibility can be found in various legal systems. In France and Belgium these rules form a certain kind of duplication of the rules on solidarity. In German law, cases of indivisible performances are governed by the rules of solidarity. A typical case of indivisibility is the sale of a horse by co-owners. Rules on indivisibility are needed if the general default rule for pluralities of obligors is separate obligations, for one cannot split obligations with indivisible objects. The Principles have, however, opted for a default rule of joint and several obligations. This default rule applies to all kinds of obligations, independently of whether the performance is divisible or indivisible. Special rules on indivisibility are therefore not needed in the Principles.

All agree to delete the provision of Art. 1.2 (3).

### **Obligee’s right against joint and several obligors (Art. 1.3)**

*Draft Art. 1.3*

*When several obligors are jointly and severally liable, the obligee may require the whole performance from any one of them, until full performance has been received.*

11. The content of the rule is not disputed.

There is discussion whether this rule should not be merged with Art. 1.1. According to Zimmermann, Art. 1.1 could be drafted following the model of PECL: “Obligations are joint and several if all obligors are bound for the whole obligation and the obligee may require the whole performance from any one of them, until full performance has been received”. Then Art. 1.3 would not be needed. It is discussed whether Art. 1.3 is an unnecessary duplication and whether it provides any rule not already being part of Art. 1.1. According to Fontaine, Art. 1.3 says that the obligee has a right of choice and that he can, after having chosen one debtor, still choose another. He also points out that the question of merging Art. 1.1 and Art. 1.3 has already been discussed in Rome. Putting the major rules on joint and several obligations into just one article can make it difficult to understand the concept.

Accordingly, the rule is retained.

## **Defences of joint and several obligors in general (Art. 1.4)**

### *Draft Art. 1.4*

*A joint and several obligor who is sued by the obligee may assert all the defences that are personal to it or that are common to all the co-obligors, but this joint and several obligor may not assert defences that are purely personal to one or several of the other co-obligors.*

12. Goode suggests to insert after “defences” “rights of set-off”. It is agreed that the right to set-off should be regulated by Art. 1.4 (Art. 1.5 dealing only with the effect of a set-off). It is discussed whether the term “defence” includes a right of set-off. Bonell points out to Art. 9.1.13 PICC, which distinguishes between defences and rights of set-off. Accordingly, it is agreed that this terminology is binding and that Art. 1.4 should specially mention rights of set-off.

13. Zimmermann suggests to change the order of the Articles by putting Art. 1.4 behind Art.1.10. He argues that the special rules on set-off, release, limitation, judgement etc. should appear before the general rule of Art. 1.4. Reading this article, one wonders whether it also covers special defences such as release, limitation etc., only to learn some articles later that they are not covered. Fontaine answers that this sequence had been agreed on in Rome. As Fontaine expresses a slight preference for the actual sequence, it is retained.

14. It is discussed whether the last part of the article, beginning with “but this joint and several obligor” may not be superfluous or whether the article could not be shortened in another way. It may be sufficient to state that an obligor may assert the defences personal to him and the common defences (Bonell, Fontaine), or to state that an obligor must not assert defences purely personal to another obligor (Zimmermann). It is agreed that the article should be shortened in one or the other way.

Later, when discussing Art. 2.4, the group agrees to delete the words “this joint and several obligor” in Art. 1.4.

## **Performance, set-off and merger of obligations (Art. 1.5)**

### *Draft Art. 1.5*

*(1) Performance or set-off by a joint and several obligor or set-off by the obligee against one joint and several obligor discharges the other obligors in relation to the obligee to the extent of the performance or set-off.*

15. There are no comments or objections.

*(2) Merger of obligations between a joint and several obligor and the obligee discharges the other obligors only for the share of the obligor concerned.*

16. Concerning the question whether “merger of obligations” or “merger of debts” is more appropriate, Goode confirms that “merger of obligations” is a technically correct expression. According to Bonell, the rule may be too short to be intelligible. Merger is not regulated anywhere in the Principles. Goode objects that “merger” or, in French, “confusion” is a general legal notion meaning the same everywhere. Regarding the fact that merger is not mentioned in the Principles except in this article, it is asked whether the rules on pluralities should regulate merger at all (Zimmermann). Apart from the law of inheritance, mergers

happen in cases of mergers of companies. This is, however, a rare case. It is therefore agreed to delete subsection (2) and mention the rule in the commentary.

## **Release (Art. 1.6)**

*Draft Variant 1:*

*(1) Release of one joint and several obligor discharges all the other obligors, unless the obligee has reserved its rights against them.*

*(2) In the latter case, the other obligors' obligations are reduced by the amount of the release.*

*Draft Variant 2:*

*(1) Release of one joint and several obligor discharges all the other obligors for the share of the released obligor, unless the obligee intends to release them totally.*

*(2) When the other obligors are discharged for the share of the released obligor, they have no more contributory claim for that share against the released obligor under article 1.12.*

17. It is agreed that the Drafting Committee cannot now deal with every particularity, but should confine itself to the basic rules. It is also agreed that there is no problem if the obligee grants a release to all obligors. The question is rather the effect of a release between the obligee and one of the obligors.

The discussion refers to a model case: A, B and C are joint and several obligors, owing 300 to the obligee X. The internal shares of A, B and C are 100 each.

If X grants a total release to A (with the effect that A owes nothing to X), there are 3 possible solutions.

### Solution A

The release discharges all debtors.

### Solution B

A is discharged. The obligations of B and C are reduced by the amount of A's share, i.e. B and C are joint and several obligors to the amount of 200. Questions of contribution do not arise.

### Solution C

A is discharged towards X. B and C remain fully liable, i.e. for 300. If B or C pays 300 to X, he can claim contribution from A in the amount of 100.

One could think of a 4<sup>th</sup> solution: A is discharged. B and C remain fully liable (for 300) and cannot claim contribution from A. It is, however, agreed, that this solution should not be possible, because X should not be able, by way of contract with A, to prejudice B and C.

The question is whether the proposed rule in the Principles should mention solutions A, B and C or only solution A and B, and which of these solutions should be the default rule.

Both variants of Art. 1.6 mention only solution A and B. In Variant 1, A is the default rule, in Variant 2, B is the default rule.

Against solution C, it is argued that it does not correspond to the normal expectations of business parties (Fontaine). With solution C, the release does not present any advantage to A. If B and C are solvent, he has to pay 100 in the end, with or without release.

It is objected that even with solution C, the release is advantageous to A (Goode). Without release he may be forced to pay 300 to X and thereby carry the risk of B's and C's insolvency; if both are insolvent, he loses 300. With a release according to solution C, he cannot be forced

to pay more than 100 (via contribution to B or to C), so he need not carry the insolvency risk of B and C.

It is agreed that all 3 solutions should be mentioned in Art. 1.6.

18. Concerning the choice of the default rule, national legal systems differ. In French law, solution A is the default rule. In German law, C is the default rule. In English law, A is not the default rule. In the PECL and the CFR, solution B is the default rule.

It is suggested not to have solution A as default rule (Zimmermann, Furmston, Goode). If X intends to discharge all obligors, he can do so in express terms. If he grants a release, not to everybody, but to A, it should not be presumed that he intends to release them all, in particular in a case of a commercial contract.

Fontaine suggests to have solution B as default rule.

There is a discussion about the advantages and disadvantages of solutions B and C.

Solution C may lead to a circuity of actions (Goode). After the release of A, X can claim 300 from B. B then can claim 100 (contribution) from A. A may then have the right to claim 100 from X, if the contract between A and X can be interpreted in a sense that A has a right vis-à-vis X to be discharged completely.

On the other hand, questions of risk distribution may speak in favour of solution C (Goode). Here, the risk of A's later insolvency is carried by B and C (they risk having to pay 300 to X without being able to claim contribution from A, when A is insolvent), not by X. With solution B, the obligors B and C do not carry the risk of A's insolvency. But this is a risk they have undertaken to carry when becoming joint and several obligors.

Against solution C, it is argued that a release should be understood as a complete release, i.e. a release also from contribution claims (Bonell).

In the end, Goode, Furmston and Zimmermann prefer solution C as default rule whereas Bonell and Fontaine prefer solution B.

19. It is agreed to present different solutions to the working group in Rome. The default rule could be solution B or solution C. Regarding the fact that having solution A as a default rule represents French law, and that it was also supported in the last Rome meeting, there should also be the proposal of solution A as default rule. Accordingly, Fontaine is asked to present 3 possible rules to the group. All proposals should contain solutions A, B and C, but the default rule should be either A or B or C.

### **Settlement (Art. 1.7)**

#### *Draft Art. 1.7*

*(1) Settlement offered by the obligee concerning the whole joint and several obligation is effective only towards obligors who have given their consent.*

*(2) If the obligee grants a settlement reducing the share of one obligor,*

*a) the other obligors' joint and several obligations are reduced by the full initial amount of the settling obligor's share;*

*b) the other obligors have no more contributory claim against the settling obligor.*

20. There is a discussion on the relationship between subsection (1) and subsection (2). Does it matter whether the obligee intends/offers to conclude a settlement with all obligors (then subsection 1) or only with one obligor (then subsection 2)?



Fontaine explains that the rule in subsection 1 can be found in the Italian Civil Code. The consent of the other obligors is necessary because the obligation forming the consideration (counter-performance) cannot be extended to them without their consent. B and C have to give their consent, not to the reduction of A's liability, but to being subjected to the settlement agreement.

The question is raised whether a rule of this kind is necessary. If the settlement contains rights and duties for all the obligees, then it follows from general rules that all obligees have to give their consent. Therefore, the majority is in favour of deleting subsection (1).

21. The remaining question is then the effect of a settlement between the obligee and one obligor concerning merely the liability of this obligor.

The discussion turns on the question whether it is possible or desirable to have different rules on release and on settlement. It may be difficult to distinguish a settlement from a partial release. If (taken the example discussed above) X agrees with A that A should owe 1 instead of 300, is that a settlement or a partial release? (Goode)

According to Fontaine, it is indeed possible to distinguish between release and settlement. The fundamental difference is that in cases of settlement, there is a consideration (counter-performance) given for the reduction of liability.

Furmston points out that the difference between release and settlement may not be obvious to lawyers from different legal backgrounds. If the draft proceeds from the assumption that there is only then a "release" when the obligor does not give consideration, then this assumption should perhaps be clearly expressed. (See also Art. 5.1.9 PICC.) In English law every release has to be agreed on in the form of a settlement because of the consideration rule.

According to Bonell, if the difference between release and settlement is not familiar to common lawyers, different rules for release and settlements can cause confusion. There is the danger that lawyers from different legal backgrounds have different views on what is a release and what is a settlement.

There may also be the danger that in practice the parties evade the rule of Art. 1.6 by agreeing on a peppercorn consideration (Zimmermann).

22. The question whether to have a special rule for settlements depends on the content of the rule in Art. 1.6, which has not yet been agreed on.

If Art. 1.6 will provide for a reduction of B's and C's liability (solution B, above), then in cases of settlements the question arises whether these liabilities should be reduced by the full initial amount of A's share (as Art. 1.7 presently provides for) or merely for the amount A performed to X.

If Art. 1.6 will provide that a release of A leaves the liabilities of B and C intact (solution C, above), there should arguably be a different rule for cases of settlements, for it may be difficult to justify why A, who by way of settlement gave some consideration to X, should nevertheless be subjected to a duty of contribution (Bonell). If solution C is applied for settlements, the settlement does not present any advantage for A (Fontaine). It is objected that the problem is the same with releases. If solution C is adopted in Art. 1.6, why not choose the same solution for settlements?

23. It is agreed that the new draft should show the connection between the solutions for Art. 1.6 and the solutions for Art. 1.7. The best way might be to present the 3 possible solutions concerning releases (above) and show for each solution which consequences would ensue if the respective solution is applied for settlements and whether there is a need for a different rule for settlements. Regarding the difficulty of distinguishing releases and settlements, there is a preference for a solution that does not require this differentiation (Bonell, Zimmermann).

### **Waiver of joint and several liability (Art. 1.8)**

#### *Draft Art. 1.8*

*An obligee who waives joint and several liability in favour of one of the obligors retains its joint and several claim against the other obligors for the whole obligation.*

24. This rule had been suggested at the Rome meeting. Contrary to what is said in the draft, the PECL do not contain a rule on waiver of joint and several liability.

The question is raised whether such a rule is necessary and whether a waiver of joint and several liability can be distinguished from a partial release.

Fontaine explains that there is such a difference. In the example of A, B and C owing 300 to X discussed above, X could waive joint and several liability in favour of A, or C could grant a partial release to A so that A shall owe merely 100 instead of 300. In both cases, A owes 100 to X. If it was a waiver, B and C would still owe 300, but could claim contribution from A. If it was a partial release, B and C would owe 200 under solution B of Art. 1.6 (or 100, if solution A is chosen).

According to Goode, it may be difficult to decide whether a certain agreement or declaration is a waiver or a partial release.

Bonell points to the fact that the Unidroit Principles do not have regulations on waivers and that it may be odd to have a rule on waiver here. According to Furmston, “waiver” is a difficult and controversial topic in English law. The question is raised whether waivers of joint and several liability really occur in practice.

It is agreed to delete Art. 1.8.

25. Then the question is raised whether the draft, as agreed by now, has rules on partial releases. A partial release would be an agreement between X and A having the result that A owes 100 (or 50 or 200) instead of 300. It is agreed that the rules on release and settlement should also cover the cases of partial releases. Therefore, the first decision to be made in Rome is whether to adopt solution A, B or C in cases of full releases. Only then the question can be decided whether the rule for full releases can also be applied for partial releases or whether it needs modifications. The same holds true for settlements. The rules on releases/settlements should also cover the cases where the obligor promises not to sue a certain obligee (*pactum de non petendo*).

### **Expiration of limitation period and effect of judgement in the relationship between obligors and obligee (Art. 1.9 (a) and 1.10 (a))**

#### *Draft Art. 1.9 (a)*

*Expiration of the limitation period of the obligee’s right against one joint and several obligor does not affect:*

*(a) the obligations to the obligee of the other joint and several obligors.*

#### *Draft Art. 1.10 (a)*

*A decision by a court as to the liability to the obligee of one joint and several obligor does not affect:*

*(a) the obligations to the obligee of the other joint and several obligors.*

26. The content of both rules is not disputed. The question is raised whether they can be deleted as being self-evident. However, regarding the fact that the PECL contain rules along

similar lines, the lack of these rules in the *Undroit Principles* could give rise to an *argumentum e contrario*. Therefore, it is agreed to retain Art. 1.9 (a) and Art. 1.10 (a). Art. 1.9 (b) and Art. 1.10 (b) will be discussed when discussing Art. 1.14.

### **Death of an obligor – Winding up or splitting of a company**

27. There is agreement that there should be no rule on this matter.

### **Apportionment between joint and several obligors (Art. 1.11)**

#### *Draft Art. 1.11*

*(1) As between themselves, joint and several obligors are liable in equal shares unless the circumstances indicate otherwise.*

*[(2) If two or more debtors are liable for the same damage under article 1.2. 2°, their share of liability as between themselves is determined according to the law governing the event which gave rise to the liability.]*

28. Subsection (2) falls away, as Art. 1.2 (2) has been deleted.

Subsection (1) follows Art. 10:105 (1) PECL, except that “contract or law” is substituted by “circumstances”.

Fontaine explains that in some cases the obligors are joint and several obligors in relationship to the obligee while under their internal relationship, one obligor may not have an interest in the matter, acting merely as a surety for the other obligor. Some codifications specifically mention this case. According to Fontaine, it does not seem to be necessary to provide a specific rule for these cases. If the obligor A has an interest in the matter whereas the obligor B undertook the obligation merely to give security, the “circumstances provide otherwise”: A’s internal share is 100 % whereas B’s internal share is 0 %. If A pays the whole amount to the obligee X, he has not paid more than his share and therefore has no claim under Art. 1.12 against B. If, instead, B pays to the obligee, the whole amount is “more than his share”, so he can claim the whole amount from A.

There are no objections to subsection (1).

29. The question is raised whether the present draft covers cases of suretyship.

According to Goode, cases where B gave a security with the consent of A may have to be treated differently from cases where B gave the security without the consent of A. In the latter case, B may merely be entitled to be subrogated to the obligee’s claim against A, whereas in the first case he may have an own right of recourse. The rules agreed by now may not fit to cases of suretyship.

It is agreed that Fontaine shall review the rules of the draft in order to see whether they can be applied to suretyship. Goode points out that the hard cases are those where the original obligor did not consent to the addition of a second obligor or of a security. The present rules may not fit to this kind of cases.

The provisional view is that the rules should make clear whether they apply to suretyship. The basic rule should probably include suretyship. In this case, rules not applicable to suretyship have to state expressly that suretyship is not governed by them.

### **Extent of contributory claim (Art. 1.12)**

#### *Draft Art. 1.12*

*A joint and several obligor who has performed more than its share may claim the excess from any of the other obligors to the extent of each obligor's unperformed share [, together with a share of any costs reasonably incurred].*

30. Furmston, Zimmermann, Goode and Bonell suggest to state the non-mandatory character clearly in the rule. It is generally understood that all rules in this chapter are non-mandatory. However, if Art. 1.11 says “unless the circumstances provide otherwise” whereas Art. 1.12 does not contain such a restriction, there may be the danger of an *argumentum e contrario* according to which the parties could not exclude contribution at all, which, as all agree, would be clearly wrong.

Fontaine answers that a provision according to which “a recourse happens unless the circumstances provide otherwise” would produce a host of litigation. The basic rule for joint and several obligations is that there is a recourse. The parties are certainly free to exclude it in their contract. This would simply be a case of a contract rule replacing a rule of the Principles and does not need to be expressly provided for. Contrary to that, in Art. 1.11 the circumstances providing otherwise need not be a different contractual rule but may be all kinds of factual circumstances giving rise to the inference of unequal shares.

31. It is agreed that the Principles do not regulate questions of costs and that the last part of Art. 1.12 (“together with a share of any costs reasonably incurred”) shall be deleted.

### **Rights and actions of the obligee (Art. 1.13)**

#### *Draft Art. 1.13*

*A joint and several obligor to whom article 1.12 applies may also exercise the rights and actions of the obligee, including accessory securities, to recover the excess from any of the other obligors to the extent of each obligor's unperformed share.*

32. The rule is approved of without further discussion.

**Effects of defences, expiration of limitation period and court judgement on the claim for reimbursement (Art. 1.9 (b), Art. 1.10 (b), Art. 1.14)**

*Draft Art. 1.9 (b)*

*Expiration of the limitation period of the obligee's right against one joint and several obligor does not affect:*

*(b) the rights of recourse between the joint and several obligors under Art. 1.12.*

*Draft Art. 1.10 (b)*

*A decision by a court as to the liability to the obligee of one joint and several obligor does not affect:*

*(b) the rights of recourse between the joint and several obligors under Art. 1.12.*

*Draft Art. 1.14 (Defences)*

*A joint and several obligor sued for reimbursement by the co-obligor who has performed the obligation may raise any common defences that have not been asserted by the co-obligor against the obligee; it may also assert defences which are personal to itself, but not those which are purely personal to one or several of the other co-obligors.*

33. It is agreed to include in Art. 1.14 “and rights of set-off” behind “defences”.

34. According to Art. 1.9 (b), obligor A, sued for reimbursement by obligor B who had performed the obligation, may not raise the defence that the limitation period of the obligee's claim against him (A) has expired. However, according to Art. 1.14, A may assert all defences which are personal to himself. There may be a contradiction between Art. 1.9 (b) and Art. 1.14 (Zimmermann). This contradiction could be avoided by limiting Art. 1.14 to common defences or by changing the rule of Art. 1.9 (b).

The same problem arises with regard to Art. 1.10 (b).

35. The rule of Art. 1.9 (b) is discussed. The case is taken that A und B are joint and several obligors and that B, having performed, claims reimbursement from A.

a) The limitation period of the obligee's claims both against A and B was expired when B performed.

There is agreement that B should not have a right to reimbursement against A.

b) The limitation period of the obligee's claim against B, but not of the obligee's claim against A, was expired when B performed.

After some discussion, the view prevails that B should have a right to reimbursement against A because B discharged A from an existing and enforceable liability.

c) The limitation period of the obligee's claim against A is expired when B seeks contribution.

The view prevails that B should have a right to reimbursement against A although A cannot be sued by the obligee. When A undertook to be joint and several debtor together with B, he also undertook the risk to be subjected to a reimbursement claim in a situation where he would not be subjected to a claim by the obligee. This is the risk A voluntarily assumed (Goode).

36. It follows (from case c) that the expiration of the limitation period cannot be meant by “personal defences” in Art. 1.14. The same holds true for a favourable court decision.

It is agreed that Art. 1.14 is needed for common defences that have not been asserted against the obligee by the obligor now suing for reimbursement. The obligor sued for reimbursement should be able to raise those defences in order to escape liability.

The question is then whether Art. 1.14 should also cover personal defences. In this case, it would have to be made clear that the expiration of the limitation period and a decision by a court are not covered by the provision.

The notion of “defence” is discussed. There is no agreement on whether incapacity or avoidance is a defence (Bonell) or not (Zimmermann, Furmston, Goode).

In order to avoid uncertainty, it is decided to restrict Art. 1.14 to common defences by deleting the last part beginning with “it may also...”. The comments should say something about personal defences.

Art.1.09 (b) and Art. 1.10 (b) shall be retained in their present form.

### **Insolvency of a co-obligor (Art. 1.15)**

#### *Draft Art. 1.15*

*If a joint and several obligor who has performed more than that obligor’s share is unable, despite all reasonable efforts, to recover contribution from another joint and several obligor, the share of the others, including the one who has performed, is increased proportionally.*

37. The rule is approved of.

## Section 2: Plurality of obligees

### Definitions and default rule (Art. 2.1 and 2.2)

#### *Draft Art. 2.1 (Definitions)*

*When several obligees can claim performance of the same obligation from the same obligor:*

- 1) the claims are separate when each obligee can only claim its share;*
- 2) the claims are joint and several when each obligee can claim the whole performance.*

#### *Draft Art. 2.2 (Sources of joint and several claims)*

*(1) When several obligees can claim performance of the same obligation from the same obligor, they are deemed to be joint and several obligees, unless the circumstances indicate otherwise.*

*[(2) Joint and several claims also arise when the promised performance is indivisible.]*

38. Zimmermann suggests to include third category of “joint” or “communal” claims: the obligor has to perform to all obligees and any obligee may require performance only for the benefit of all.

Joint claims are the most common form of plurality of creditors in German law, whereas cases of joint and several obligees are extremely rare. Joint claims are mentioned in the PECL (“communal claims”, Art. 10:201 (3)) and in the CFR (“joint rights”, Art. 4:202 (3)).

According to Goode, joint claims are also known in English law.

39. It is discussed whether the rules in the existing draft cover the main cases of pluralities of obligees. The following cases are mentioned:

- 1) A, B and C undertake to do building work for X. The contract provides that payments by X shall be made into a certain account.
- 2) A and B are partners in a partnership and have a common account with the bank X. The bank can only make payments or transfers if authorised by both A and B.
- 3) A, B and C are co-obligees. A (but not B and C) has the right to collect the whole performance and to sue the obligor.

In cases 1-3, one cannot say that each obligee can claim the whole performance. These cases might, however, be regarded as cases of joint and several claims where the parties have made special contractual arrangements.

Cases 1-3 could be regarded as cases of joint claims. The payment into an account named by all obligees in case 1 may be regarded as a performance for the benefit of all obligees. In case 3, if the obligor is contractually allowed or required to pay to A, this payment to A could be regarded as a performance to the benefit of all obligees.

According to Fontaine, although the bank in case 2 may only be allowed to pay to both A and B, it is another question who can sue the bank if it does not perform. Bonell points out that in this case A and B can only sue together.

Fontaine argues that in cases where the obligees wish one of them to sue in the name of all, or to collect the money for all, they can provide for this by the rules of mandate. Concerning joint claims, the right of each obligee to sue does not fit to the fact that a single obligee does not have the right to receive the performance. Cases where each obligee has a right to sue should principally be regarded as cases of joint and several obligations.

According to Bonell, the rules on joint claims may appear in the Principles, but should not form the default rules because they are too complicated.

40. It appears that 2 kinds of joint claims are conceivable:

Joint claims variant A:

Performance has to be made to all obligees together, but each obligee alone has the right to sue and claim performance to the benefit of all (this is the model of PECL and CFR).

Joint claims variant B:

Performance has to be made to all obligees together, and only all obligees together can sue the obligor.

The question is whether one or both kinds should be included into the draft and whether one of them should form the default rule.

41. Goode and Zimmermann argue that a right of each obligee to collect the performance (as is the case with joint and several claims) must not be presumed. If the obligees want that one of them or each of them should have the right to receive the performance, they can grant such authority to one of them or each of them. Without such authority it should not be assumed that a single obligee has the right to collect the performance. This is too dangerous for the other obligees, as the collecting obligee may disappear or become insolvent.

In practice it seems that usually every obligee has both the right to sue and the right to receive the performance. This may be an argument in favour of a presumption of joint and several claims. On the other hand, the obligees have usually the rights to sue and to collect the performance because they are given such authority by their co-obligees (Goode).

According to Furmston, a default rule is only important in cases where the parties did not make any arrangements concerning the rights of the obligees. In these cases, a right of each obligee to collect the performance should not be presumed.

A default rule in favour of joint and several claim does not seem to exist in any national or international law. The PECL do not contain any default rule. The default rule in the CFR is separate claims.

42. Bonell suggests to have separate claims as a default rule.

Goode objects that in cases of a single obligation separate claims should not be presumed: there is a presumption of indivisibility. The case of a syndicated loan is mentioned. Here, every obligor has a right to a certain amount of money, and an agent (perhaps one of the obligees) collects the money for all. According to Goode, this is not a case of a single obligation; it is therefore not covered by Art. 2.1 at all.

Fontaine suggests not to have any default rule at all.

Goode, Zimmermann and Furmston suggest to have joint claims (variant A or B) as a default rule.

Concerning the choice between A and B, a rule that only all obligees together can sue may be impractical and should perhaps not be presumed. On the other hand, if parties want each of them to have a right to sue, they can arrange so. For this reason, Goode, Zimmermann and Furmston prefer to have joint claims variant B as a default rule.

43. It is agreed to include a number 3) into Art. 2.1:

“3) the claims are joint when the obligor must perform to all obligees”.

Concerning terminology, “joint” seems to be better understood than “communal”.

The article should be re-drafted in the same way as Art. 1.1. The first 14 words should be deleted. Accordingly, Art. 2.1 may have the following form:

“Claims are joint and several when... Claims are separate when... Claims are joint when...”.

44. Concerning the default rule, all agree that in the vast majority of cases the parties will have made arrangements so that a default rule is not necessary. According to the majority, in



those rare cases where there is no agreement a right of each obligee to receive the performance cannot be presumed. The default rule should therefore be joint claims.

Goode suggests to have such a default rule only “when an obligation is expressed as a single obligation”. Zimmermann and Bonell object that this may be too difficult to understand. In cases where there is a plurality of obligations (syndicated loan) the “circumstances will indicate otherwise”, so that joint claims will not be assumed.

45. Art. 2.2 should read like this:

“When several obligees can claim performance of the same obligation from the same obligor, they are deemed to be joint obligees, unless the circumstances indicate otherwise.”

Art. 2.2 subsection (2) of the draft shall be deleted for similar reasons as in the case of Art. 1.2 (3).

The draft has to be amended by rules on joint claims.

### **Effects of joint claims (Art. 2.2 bis)**

46. The effect that the debtor has to perform to all obligees can already be found in the new Art. 2.1 and need not be repeated here. The only question to be decided here is whether every obligee has a right to sue (variant A) or whether the obligees have to sue together (variant B). If there are no arrangements by the parties, the presumption should be that all have to sue together unless the circumstances provide otherwise.

### **Effects of joint and several claims (Art. 2.3)**

*Draft Art. 2.3*

*(1) Performance of an obligation in favour of one of the joint and several obligees releases the obligor towards the other obligees.*

47. As Art. 1.3 contains the main effects of joint and several obligations, this article should contain the main effects of joint and several claims. Therefore, a new subsection should be included:

“(1) Any of the joint and several obligees can claim the full performance from the obligor.”  
Subsection (1) of the draft shall become subsection (2).

*(2) The obligor has the option of performing the obligation in favour of any of the joint and several obligees, provided the obligor has not been sued by any of them.*

48. The question is raised whether this rule is needed.

According to Bonell, the rule is self-evident. Others object.

Furmston raises the question whether the rule is justified. Why should an obligee deprive the obligor of his right of choice by suing him? According to Bonell, the obligee who takes the initiative should not be deprived of his right to performance. The rule is required by reasons of efficiency.

Another solution might be to regard the rule as a procedural rule not to be included into the Principles.

The majority regards the rule as justified but not self-evident. Therefore subsection (2) of the draft shall become subsection (3). It shall be reformulated in order to focus on the restriction of the obligor, e.g. “when the obligor has been sued by a joint and several obligee, he can no longer perform to the other obligees”.

Fontaine is asked to see whether Art. 2.1 and Art. 2.3 are adjusted to each other.

### **Defences against joint and several claims (Art. 2.4)**

#### *Draft Art. 2.4*

*(1) The obligor who is sued by one of the joint and several obligees may assert all the defences that are personal to its relationship to the suing obligee or that it can assert against all the co-obligees, but this joint and several obligor may not assert defences that are personal to its relationship to one or several of the other co-obligees.*

49. It is agreed to include “and rights of set-off” after “defences”. Fontaine explains that in cases of plurality of obligees one cannot speak of “common defences”.

The question is raised whether the rule could not be stated in a shorter form. In the same way as had been suggested to Art. 1.4 (see above), Art. 2.4 could read: “The obligor who is sued by one of the joint and several obligees may assert all the defences that are personal to its relationship to the suing obligee or that it can assert against all the co-obligees”; or “The obligor who is sued by one of the joint and several obligees may not assert defences that are personal to its relationship to one or several of the other co-obligees”.

Eventually it is agreed only to delete “this joint and several obligor” both in Art. 1.4 and in Art. 2.4.

The wording of Art. 2.4 (1) should be: “The obligor may assert against any of the joint and several obligees all the defences that are personal to its relationship to that obligee or that it can assert against all the co-obligees, but may not assert defences that are personal to its relationship to one or several of the other co-obligees.”

*(2) A release granted to the obligor by one of the joint and several obligees has no effect on the other obligees.*

50. This rule can also be found in the PECL, Art. 10:205 (1). The question is raised why an obligee who has the right to collect the performance and thereby bring the other claims to an end should not have the right to grant a release binding all. The majority prefers having different rules for collecting the performance and for granting a release. A obligee collecting the performance can be presumed to act to the benefit of the other obligees, while granting a release is detrimental to the other obligees.

The question whether there should be additional rules on settlements depends on the decisions to be made in the context of plurality of obligors (see discussion to Art. 1.7).

*(3) The rules of articles 1.5, 1.7, 1.8, 1.9 and 1.10 apply, with appropriate adaptations, to joint and several claims.*

51. There is no discussion on this rule. It is assumed that the application of the respective rules on joint and several obligations will fit to cases of joint and several claims.

### **Defences against joint claims (Art. 2.4 bis)**

52. The article should read as follows: “The obligor may assert against the joint obligees only the defences that he can assert against all the joint obligees.”

The comments should make clear that the obligor cannot assert defences that are personal to its relationship to the suing obligee.

A release by only one of the obligees has no effect at all.

Fontaine is asked to check whether other rules (comparable to those found in Art. 2.4) may be necessary for joint claims.

### **Allocation between joint and several and between joint obligees (Art. 2.5)**

*Draft Art. 2.5*

*(1) Joint and several obligees are entitled to equal shares, unless the circumstances indicate otherwise.*

*(2) An obligee who has received more than its share must transfer the excess to the other obligees to the extent of their respective shares.*

53. There are no objections to the article concerning joint and several claims.

The question is raised whether a similar rule is necessary for joint obligees, as the obligor has to perform to all obligees anyway. The majority prefers to have an allocation rule.

According to Fontaine, the question of the size of the shares has to be regulated. There should be a rule similar to the rule of Art. 2.5 (1), whereas a rule similar to Art. 2.5 (2) is not needed.

Goode suggests to have a common rule governing both joint and several claims and joint claims. The rule expressed in Art. 2.5 (2) should also be applicable for joint claims.

Accordingly, it is decided to include “joint obligees” into Art. 2.5, which then will begin as follows: “Joint obligees and joint and several obligees are entitled...”.

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Working Group for the preparation of  
Principles of International Commercial Contracts (3<sup>rd</sup>)  
Drafting Committee  
Hamburg, 3-6 March 2008

## **Session 2:**

### **Unwinding of Failed Contracts**

(Unidroit 2008 Study L – WP.15)  
Reporter: Reinhard Zimmermann

#### Minutes

Present:

Prof. Joachim Bonell  
Prof. Bénédicte Fauvarque-Cosson  
Prof. Marcel Fontaine  
Prof. Michael Furmston  
Prof. Roy Goode  
Prof. Reinhard Zimmermann

Keeper of the Minutes: Dr. Walter Doralt

#### **Morning, March 4 2008**

1. Zimmermann opened the discussion and pointed to the issues open since the Rome meeting, namely avoidance and termination. He recalled that the discussion in Rome had focused on termination. Zimmermann suggested to deal first with termination, then with avoidance because this would be easier to agree on after having settled the rules for termination. Zimmermann explained that as for issues relating to Termination, there are on the one hand contracts of sale and on the other hand contracts to be executed over a period of time. He recalled the terminology used by G. Treitel who uses the terms instantaneous and successive contracts. Zimmermann said that terminology was still an open issue but that in any case successive contracts are very important for commercial practice. Therefore, he suggested to first deal with these. He referred to the summary of his exchange with Goode, printed in the handout of the participants (Appendix E). Zimmermann then pointed to the current rule 7.3.6 (1) essentially dealing with sale and (2) dealing with contracts extending over period of time, for which the restitution consequences should arise only *pro futuro*, not for the past. Zimmermann recalled the four examples provided by Goode which are included in the handout and commented on these examples. Zimmermann expressed his view, that all these situations seemed to be adequately covered by the current rules. Goode agreed.

2. Zimmermann asked to get back to the four examples and whether anyone saw other points needing to be dealt with, aside from what is already be covered by 7.3.6. Furmston asked about the possibility of recovering the equipment in example A. Zimmermann and Goode said, that the equipment has to be returned, if still in the possession of the other party. Furmston asked if equipment is to be given back, what damages could be recovered. When B

stops the payment, recovery equipment is only be a first step, and only after that does the question of damages arise. Furmston also asked whether that mattered at all and if it had any impact on the sums coming out differently.

3. Goode mentioned that the entitlement to keep what had been paid is only one side, while the other is the entitlement for what had not been paid and for accrued debt. He suggested the draft should not be going into damages as it would then also have to deal with questions like mitigation duties.

4. Fontaine mentioned his understanding, that the group should be reviewing the current state of the principles and therefore look at possible other situations the drafters may want to cover, if any. Zimmermann agreed with Fontaine and said there should be a general system and only then should the group deal with other points. He also mentioned that in Rome his draft was considered to go too much into the direction of sales contracts and not enough into contracts extending over a period of time. Bonell drew the attention to the fact that it was yet undecided if a unitarian approach for unwinding all contracts will be chosen in the end or if a set of different rules for different types of contracts will be adopted. The discussion in Rome had focused too much focused on sales and not enough on contracts extending over period of time, of which Goode had been especially critical. Bonell said he could imagine 7.3.6 (2) and (1) to be drafted as dealing equal problems, not one as the exception and the other as a rule. Fontaine pointed out, that it is first necessary to asses if a majority wants to review 7.3.6.

5. Goode mentioned again, that in spite of the importance of sales, contracts extending over a period of time are even more important or at least as important. He also pointed out that in most commercial contracts parties do not expect having to give back the benefits they have received; outside the field of transfer of property it is hardly conceivable to see parties giving back accrued benefits. He thought that the current rule may give a wrong impression.

6. Zimmermann asked if the participants thought the substance of 7.3.6 covers the problems Goode raised. Zimmermann also asked if there is an agreement that more than the current 7.3.6 is needed and that both types of contract should be put on an equal level. Goode said it is not clear to him whether anything different is needed. Zimmermann made suggestions for amendments and gave his example of the contract regarding the service of the fire engine, where the service had not been duly performed (p. 9 of Zimmermann's paper) The current rules only cover restitution *pro futuro* while in his example this seemed unjust. Payments should be dealt with because one party got the benefit without having delivered his service. Goode mentioned that under English law no remedy is given in such a situation. Zimmermann asked if that solution was fair. Fauvarque-Cosson asked if this situation would be covered by the suggested qualification and mentioned that under French law damages might be awarded even without a loss because of the windfall profit made by underperformance. Furmston asked what the Unidroit principles currently provide for. Zimmermann answered they only cover a *pro futuro* restitution and that no damages would be awarded if there is no loss. Furmston said that probably the approach of English law is not to give a remedy if there is no loss and asked Bonell if damages could be recovered in such a situation under Unidroit. Bonell pointed to 7.4.2. (2) under which a recovery by way of damages might be possible. Zimmermann asked if an escape clause is wanted so as to accommodate cases such as his example; then services must be valued. Goode thought that restitution would then be the general rule, which did not seem the best option to him. Zimmermann said he would drop this point if this is the general view, but as a consequence a solution including damages will be necessary.

7. Bonell suggested that terminology should be dealt with at this point, as some of the substantive issues were intertwined with terminology. His preference is not to speak of sales contracts specifically.

8. Zimmermann suggested that 7.3.6. (2) starting with “However, if performance of the contract has extended over...” should be redrafted and the “However” deleted. The result would be a draft with two situations encompassing all situations.

9. Goode mentioned the difficulty with the rule regarding instantaneous contracts from an English point of view when a transfer of property takes place. Zimmermann pointed out, that a long term contract can also be about the transfer of property, to which Goode agreed.

10. Zimmermann suggested as for the terminology to have “contracts extending over a period of time” and “other contracts”, to which Goode agreed. Fauvarque-Cosson said the decisive point should be the time, not the type of obligation.

11. Zimmerman suggested to first draft a rule dealing with performance over a period of time, then one for the other contracts, then to see where instalment contracts fit in. Bonell suggested to start with instantaneous contracts. Goode said he would not mind, if terminology can be agreed upon and if both provisions are at an equal level. Divisibility of the contracts can be a feature of both categories. The PECL mention divisibility, which is not necessarily only a feature of contracts extending over a period of time, as the same may be said for instantaneous contracts, eg for down payments or instalment sales.

12. Zimmermann said he thinks instalment sales fit in the category of contracts extending over a period of time. Fauvarque-Cosson suggested to give these contracts a third category and therefore a third name. She pointed out the difference being that performance is not extending over a period of time for one of the parties.

13. Zimmermann asked about contract under which one person terminates for an instalment sale and asked what should be done regarding the return of the objects? Bonell mentioned that performances made should be distinguished from what is to be returned and that payment is different from performance of goods by instalments. Goode said a sale with instalment payments does not raise any problem currently not covered, but that the performance of delivery of goods in instalments is a difficult issue. He asked if an entire contract can be terminated because of one instalment that not having been performed and therefore raising restitution issues for the entire contract.

14. Zimmermann said the current problem is termination. Goode said it is also an issue of restitution. A breach may be considered fundamental enough to affect the entire contract and he prefers not getting into it. Furmston said the primary question is whether one could terminate the contract. Goode said it is also about what can be terminated: One instalment, or the entire contract? He prefers not dealing with it.

15. Zimmermann went back to instantaneous contracts and contracts extending over a period of time (ie including those, where the characteristic performance extends over a period of time). He explained that contracts where payment is to be performed over a period of time fall into the category of instantaneous contracts.

16. Goode and Fauvarque-Cosson objected to this view and said they would include the contract with payments extending over a period of time into the category of contracts

extending over a period of time. Goode then mentioned the issue of acceptance of goods and the refusal because of non acceptable goods. Bonell said that the Principles do not have the term of acceptance. Furmston made an example, with a contract under which 1000t of coffee beans should be delivered in Jan and only 900t were actually delivered on Jan 1. He said that the seller, under English law, has a second chance because he still has all of Jan to perform. That would therefore not be a case of termination. He asked what the solution is under the principles. Bonell answered that the terminology of acceptance is not used by the Principles and also not by CISG. But in Furmston's example, the buyer is obliged to give a second chance to the seller; termination follows only after the second chance. Goode said that the party in breach gets a second chance no matter if there is a fundamental breach or not and if there is termination, restitution of delivered goods follows.

17. Zimmermann explained that he understands 7.3.6 (1) to cover the situation in which the seller transfers ownership and the buyer pays the price. Goode agreed and then gave a different case in which goods are sold and the buyer does not pay. According to Goode, the seller can not get the goods back, because terminating the contract is not possible if ownership has been transferred. There is only a claim for the price. Sales law does not permit termination and a claim for goods.

18. Zimmermann asked why this example should be treated differently from his example and Goode answered that the difference is that the goods did not conform in the first example so that restitution follows. Bonell pointed out that this solution is not the one adopted by CISG, to which Goode replied that CISG does not deal with property. Bonell said that it dealt, however, with termination and restitution. Bonell and Zimmermann then said that termination is possible under CISG and also under German law for default in payment and that the seller gets the goods back, as restitution follows after the termination of the contract.

19. Furmston and Goode then said that this clearly is a fundamental difference between common law and civil law and CISG because common law does not permit the recovery of the goods. Goode suggested that given these difficulties different examples should be taken. Zimmermann said this would mean the drafting of a rule will not be possible regarding (1), but Goode thought it is possible at least for most cases.

20. Bonell pointed out that the solution has to be adopted within the framework of the principles. The principles left no doubt about the possibility of termination, allowing the seller to terminate the contract if payment fails. Even if the common law systems exclude termination in these circumstances, this solution has to be adopted.

21. Goode went back to the question of terminology and asked why a contract under which the buyer performs over a period of time but not the seller is considered an instantaneous contract. Zimmermann said the terminology was not settled yet, but that restitution has to follow and therefore the contract falls in the category of instantaneous contracts. Fontaine said that a redrafting will be necessary and that the mere inversion of (1) and (2) is not sufficient. Goode said he found it easier to first deal with the category of contracts extending over a period of time and then with all other contracts.

22. Bonell asked about contracts under which the seller delivers over a period of time and Zimmermann responded that their classification could be clarified in the comments. Fauvarque-Cosson asked if the solution is a good solution from a policy point of view, as the seller usually does not want the goods back. She pointed out that even if the divide along the lines of the characteristic performance is logical, it does not seem practical. Zimmermann

pointed to III.-3:512. DCFR in this context and asked if this solution is an exit for the impasse reached in the group. Goode said the question is whether the entire contract can be terminated. Bonell said the right of termination is the crucial point. Both pointed to the fact that the current comments of the principles permitted termination only in case of a fundamental non-performance and that it applied to non performance of instalments just as well.

23. Zimmerman then asked how, in the light of this discussion, the rule should now be drafted and what terminology should be adopted. Fontaine reiterated his suggestion to delete “however” in (2). Goode’s suggestion of contracts to be performed “over a period of time” and “at a particular point in time” was considered as ambiguous by Fauvarque-Cosson, as contracts performed over a period of time also need to be performed at specific dates. Goode mentioned the importance of the sequence of the rules again. Together with Furmston he prefers to have contracts to be performed over a period of time first and then instantaneous contracts, while Bonell, Fontaine and Fauvarque-Cosson prefer the inverse order. Goode then said finds the sequence not crucial if the terminology is settled in a good way. Bonell, Fauvarque-Cosson and Fontaine agreed to the terminology suggested by Goode.

#### **Afternoon, March 4 2008**

24. Zimmermann summed up the previous discussion and its results. Regarding the terminology the group has agreed on “contracts to be performed at a particular point in time” (rule 1) and “contracts to be performed over a period of time” (rule 2, along the lines of 7.3.6. sub 2).

25. Goode mentioned that the reference on divisibility in the rule has not been agreed upon yet and Fontaine thought this important issue should not be left out. Zimmermann said he always understood that divisible means the performance could be divided, whereas the discussion in the morning focussed on performances that were already divided. Goode said he thought about it as separate phases of performance.

26. Bonell asked Fontaine and Furmston to give examples of situations where the outcome would be different if the following part of the provision would be deleted: “if the contract is divisible”. Fontaine mentioned the transfer of know how under a contract where a partial performance is worthless. The termination would only impact the future. Goode made an example of a construction contract with a down payment; after partial performance the contractor stops and the contract is terminated. Furmston said he considers a construction with payments at different stages to be a divisible contract. Bonell disagreed because he thinks a building was either completed or not. Furmston and Goode, however, held that it is divisible if instalments are to be paid at certain stages for certain parts of the performance.

27. Bonell then asked if the rule can not be applied as it is now. Furmston said the cost to the employer is typically higher than the part still not paid to the constructor and therefore the question of damages arises. He argued the contractor keeps what he had received. Fontaine made an example with driving lessons, all paid upfront, then after three hours the teacher is unable to perform further lessons. He said this contract is indivisible, because the three hours alone are entirely useless. Zimmermann replied that he considered this contract as divisible. Fontaine then pointed to an Encyclopaedia subscription as indivisible. Goode suggested keeping the reference of indivisibility in for now and Fontaine agreed.

28. Zimmermann said two examples are already in the commentary and maybe further examples can be added. Zimmerman summarized the discussion and it was agreed to leave



rule 2 with the divisibility in (regarding contracts to be performed over a period of time) and therefore the rule stands as it is without a need for amendments (except for the deleting the “however” at the start). Zimmermann recapitulated that a contract where only the payments are to be made by instalments is a category 1 contract (to be performed at a particular point in time) and asked if this is the understanding of the participants. The present participants agreed but Fauvarque-Cosson again pointed out that the seller does not want his goods back after two years and that in the DCFR he had a choice. Goode replied that he can just as well claim damages instead of the goods, therefore the doubts of Fauvarque-Cosson are unfounded. Zimmermann summed up the discussion to this point and it was agreed that both parties may claim restitution of what they have performed under the contract, as already laid down in rule 7.3.6 (1). He then suggested to keep the current wording regarding “concurrently” in spite of the DCFR using “reciprocal”. This was also agreed upon by the participants. He then asked if there should be a specific provision on partial termination.

29. Bonell said CISG expressly provides a case of partial termination for instalments and Zimmermann mentioned the case he thought of, namely two books are being sold and one is defective leading to a termination by the buyer with regards to only one book. Zimmermann suggested to include the reference to partial termination in the comments; Bonell and Goode agreed.

30. Zimmermann then moved on to situations where restitution in kind is not possible and where an “allowance” should be made according to the current principles. He said he does not know what an allowance is and it would need to be clarified in the comments if subjective or objective value is meant. He also mentioned that a majority in Rome wanted to keep “allowance” in the text, but that this makes it necessary to specify what is meant by it. It was agreed to leave the term allowance because a change would complicate the process.

31. Zimmermann pointed to the discrepancy between 7.3.6. calling for an allowance “*wherever reasonable*”, while in 3.17 “*wherever reasonable*” is not mentioned. It was decided to retain *wherever reasonable* and extend it to avoidance when it would be dealt with.

32. Zimmermann then asked if the rule should be extended to situations where restitution in kind is not appropriate (7.3.6.). In the light of the official comments on p 230 he does not see a reason to have “*not appropriate*” included in the wording. It was, however, decided to keep “appropriate” in the text.

33. Zimmermann moved on to the topic of the duty to return what had been performed including benefits derived from the performance. His examples are included in appendix C and he mentioned that Prof. Chappuis has helped with providing these examples.

34. Goode said he would prefer not to include a provision on benefits, as it may entail litigation and complicate matters. Zimmermann replied that all civil codes he knew have such provisions and pointed in addition to CISG and the DCFR, both having provisions for this issue. Also, Zimmermann mentioned he had been asked specifically to provide examples for these issues at the meeting in Rome. Goode reiterated his concerns and said it would be useful to have input from businesses and practicing lawyers. Bonell agreed to ask Christine Chappuis to gather information at her next meeting.

35. Zimmermann thought it seems unfair to deprive the party of interests in restitution after having made the payment according to the contract if only the other party has not performed. The restitution can in some cases take place years after the payment and interests

would make up for it. Zimmermann then said that the rule regarding benefits that can be derived from the performance, as a consequence, may also be dropped.

36. Goode again raised doubts about granting interests that have perhaps, in the specific case, not been derived and that they are in any case be difficult to calculate, as it can be hard to assess what payments went in and out of a bank account. Furmston objected and said it is not be difficult to calculate interests. Bonell agreed and said it can very well be an abstract calculation.

37. Goode said that if a benefit rule is drafted, it would be best to put down some sort of interest rate as a matter of simplicity. Furmston pointed out that interest rates vary and this has to be taken into account. Bonell then said it apparently causes difficulties to reach an agreement for a rule even for money but probably even more so for property when it is about what could have been earned instead of what has been earned. He also saw the risk of too much litigation and asked if the two benefit rules can be split up. Zimmermann explained that a benefit rule without the rule on benefits that might have been received is possible, but not inversely. Fontaine said both rules should be included, but Goode, again, objected.

38. Bonell and Zimmermann said it is logical to have both rules and they pointed to the fact that excessive litigation does not seem to have arisen under CISG which contains a benefit rule.

39. Bonell then said he was not certain if the point was worth the difficulties arising from it and therefore pleaded to abandon the issue. Zimmermann pointed out it would be difficult for him to justify, as he had specifically been asked to provide examples and there was considerable support for it in Rome. Furmston agreed and said the majority view can not be dropped without discussion. Goode on the other hand said Zimmermann should simply point to the complications the group has and therefore ask for further guidance before finalising a text.

40. Zimmermann then summed up the discussion and said he can submit a draft to Rome without these parts but with an appendix on these problems. However, Bonell objected to the appendix. Zimmermann replied he is under a mandate to provide examples.

41. Zimmerman raised the risk question and made the following example: A & B have concluded a contract about the sale of a car for 50.000 and a retransfer is necessary but the car has been destroyed. A has to give its value and B 50.000. He said this solution is, however, not fair where the destruction (or deterioration) is attributable to A and explained the suggestions made in his paper. Goode agreed to the solution proposed by Zimmermann, who also pointed out that there had been no opposition to it in Rome. Fontaine agreed but asked if the provision could not be improved by saying “if the impossibility is attributable to the other party” instead of the proposed formulation. Zimmermann agreed to this suggestion and the formulation was accepted by the participants.

42. Zimmermann then asked about cases in which restitution in kind is too costly, such as in the example of the unpaid fresco that could only be removed with excessive costs. Fauvarque-Cosson asked if the text should not rather say onerous instead of appropriate, if onerous was what was meant. Zimmermann pointed out that the choice had been deliberate in Rome and that there may be other cases than onerous. He said he will think about further cases.

43. Zimmermann raised the issue of the destruction of the goods that would also have taken place had the goods still been with the seller, but said he prefers not to regulate it.

44. Zimmermann then asked if a rule on “expenses linked to the *performance*” should be included and Fauvarque-Cosson said this depends on whether a rule on benefits is adopted. Zimmermann said that expenses are probably a different issue because they only happen sometimes. Fauvarque-Cosson agreed, but asked how much detail was actually wanted. She said a rule on expenses could be had even if no rule on benefits was adopted. Bonell said that expenses would in any way not create additional litigation, as they are either incurred or not and have to be proven. Zimmermann said that the committee in Rome had agreed to it, therefore it should be kept for the time being. Bonell agreed and mentioned that in the light of the risk rule, the party bearing the risk should be encouraged to make expenses if necessary. Zimmermann then said the rule may therefore now be kept with its original wording, tailored to sales. However, Fontaine, Bonell and Fauvarque-Cosson preferred a broader phrasing regarding expenses relating to the performance.

45. Zimmermann then mentioned that avoidance had a slightly different regime from the one adopted for termination and asked if the differences should be retained. It was decided he should make a new draft in the evening for the next day, trying to have a common regime for both termination and avoidance.

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46. Zimmermann opened the discussion and first asked Goode if he agrees to change the wording of contracts to be performed “at a particular point in time” as it seemed cumbersome. Goode suggested “at a particular time” and the participants agreed to the amendment.

47. Zimmermann said he had added “or part of it terminated”, because it follows logically. Goode found “On termination of a contract or part of a contract” is more coherent at the start of the rule. Bonell asked why there should not be a separate rule as for avoidance and Goode said he also favours one. Zimmermann suggested to look at 3.16. to see if a draft inspired by it is possible. Zimmermann pointed to his two books example once more.

48. Furmston said it this is an important question and probably a rule should be adopted, but said the two book example might be too simple. He thought it ought to be tackled but he is not sure if it should be at this point already. He also mentioned that there should be partial termination as there is already partial avoidance. Bonell explained how CISG deals with the issues and said partial termination remains an open question. Furmston mentioned that there may be cases where a party only wants to terminate part of a contract, not all of it. He made the example of the acquisition of a petrol station linked to the buying the petrol from the petrol company for 21 years. After a serious breach by the petrol company the buyer may be happy to keep the station, but no longer wants to buy the petrol from the company. A decision would need to be made in such cases. Goode said a separate rule would be too clumsy. Bonell suggested to delete “or part of it” as it is too difficult to draft a rule right now.

49. Zimmermann said this brings it out of tune with avoidance and it seems harmless to keep it in. However, he asked if it should really be inserted in three places in the provision. Goode suggested “On termination of the contract or part of the contract”, to which Zimmermann agreed. Fontaine was, however, reluctant to keep a reference to part termination in the provision and found it not necessary to have a rule only because there is a provision on partial avoidance. He asked for a decision on whether to have partial termination.

Zimmermann said that in his book example or in some other situations all agreed that there has to be partial termination and that it is a clear case even without a provision. This should be mentioned here so as to acknowledge the existence of these cases. Goode agreed that it should be possible to deduce from the principles that one can terminate in part. Zimmermann pointed out that there is no rule like 3.16 on termination and therefore currently no basis on partial termination in the principles. Goode asked if it can not be derived from the principles already, to which Zimmermann replied, that it may follow from the facts in some points. Fontaine then said that the example given by Furmston really is on partial termination, while the book example was not. Zimmermann said that a rule would be necessary because the problem needed to be solved. Bonell said that for consistency and coherence there should be a rule, because there is a rule on partial avoidance. Goode agreed but said a reference without a rule is strange. Zimmermann then asked how the problem should be tackled and Bonell said it could not be dealt with in 2009 as there was already a heavy agenda. He asked to postpone the final decision on this point. Zimmermann concluded that in Art 1 (1) “or part of it terminated” will be deleted in both places where it is currently included.

50. Zimmermann went on to instalment contracts and Bonell asked if it has been settled that an instalment contract falls under category (2) where delivery is in instalments. Fontaine said these issues are different and that the use of the same wording may cause (1) misunderstandings. He said the same terminology should be used as in 6.1.2. first two sentences. Fauvarque-Cosson and Goode agreed. Zimmermann disagreed and argued these are different cases, but that he is willing to give in to a majority. Bonell said these are different in his view as well but that ultimately it is the same meaning regarding instantaneous contracts and others.

51. Furmston said that contract to stay a hotel for a week is a contract to be performed over a period of time while a contract with an airline for a flight is a single performance. Bonell disagreed but said the performance is not divisible in the flight case therefore the rule does not apply. Furmston asked if the contract for the train journey is divisible in Bonell’s view and Bonell answered it is, as a passenger can be ordered to get off if he behaves badly. Zimmermann asked if Art 2 should apply in these cases with restitution only for the future. Goode thought the issue is one of divisibility of the contracts, not one of time or a period of time. Zimmermann said this is even more difficult than a distinction based on the performance at one time or over a period of time. He concluded that the rule now read as on the handout without the “of the part of it terminated”:

#### **Restitution following termination**

Art. 1 Contracts to be performed at a particular point in time

- (1) On termination of a contract to be performed at a particular point in time either party may claim restitution of whatever it has supplied under the contract, or the part of it terminated, provided that such party concurrently makes restitution of whatever it has received under the contract, or the part of it terminated.
- (2) If restitution in kind is not possible or appropriate, an allowance has to be made in money whenever reasonable.
- (3) The recipient of the performance does not have to make an allowance in money, if the impossibility to make restitution in kind is attributable to the other party.
- (4) Compensation may be claimed for the necessary expenses linked to the performance received. Compensation for other expenses linked to the performance received may be claimed as far as the other party is enriched by them.

Art. 2 Contracts to be performed over a period of time

On termination of a contract to be performed over a period of time restitution can only be claimed for the period after termination has taken effect, provided the contract is divisible.

52. Zimmermann pointed to the text sometimes saying “an allowance”, sometimes just “allowance” and thought it would be better to have “an allowance”. Goode agreed to this point.

53. Zimmermann said he had inserted “has to be made” instead of “should be made”, which was accepted by Goode and Bonell. Zimmerman presented (3) as a result of what had been discussed the previous afternoon and Goode suggested to delete the comma before “if”, which was accepted. Then Zimmermann presented (4) which was also accepted.

54. Zimmermann then discussed Art 2 which was accepted by the participants as well.

55. Zimmermann suggested turning to avoidance and to go through the articles and test them. The rules for avoidance, he said, are very similar to the rules of termination and it should be tried to apply the termination rules also for avoidance. He mentioned that the DCFR applies principles of unjust enrichment to avoidance and that this is not an option here, as no rules on unjust enrichment are available, but there were rules on termination. He asked if it is thought that in cases involving avoidance, the restitutionary consequences should not apply to the past, but only to the future. He also mentioned that the German system unravels everything for the past in case of avoidance, unless this is very inconvenient (doctrine of “faktische Verträge”). Fontaine said special rules are necessary for contracts to be performed over a period of time for termination, but not for avoidance, as it will usually arise soon, not generally leading to the problems of restitution after termination. Zimmermann asked about mistake, to which Fontaine replied that it is an unusual circumstance. Goode said he favours a simple rule to unravel everything from the start. Furmston objected as he thought it would not fit all cases. Bonell suggested the solution may be found in 3.17 and the formula now available in Art 1 (2): “not possible or appropriate”. Furmston said a rule for Art 2 is not necessary and that one can focus on Art. 1. Zimmermann concluded that avoidance can be based on the wording of his proposed Art 1 and suggested to go through (1) – (4) to see what adaptations will be necessary. Goode agreed and thought it would be nice to have one set of rules for avoidance and termination. Zimmermann said this would be his ideal solution, but that there is special rule for termination of contracts to be performed over a period of time, a rule on partial avoidance, but no rule on partial termination except maybe in the commentaries. Bonell said that in Art 3.17 the effects of avoidance and restitution are being dealt with, while for termination the effects and then the restitution consequences are being distinguished. Goode said he does not know why the same rules can not be applied.

56. Bonell raised the problem of the *principe de l'autonomie des clauses*, according to which even if the contract was avoided, the arbitration clauses are still valid.

57. Zimmermann said that one could envisage the rules now agreed upon for avoidance as general restitution rules and take them into account where needed (illegality, conditions, etc). 3.17. could then be deleted without disruption of the numbering. Zimmermann then presented his draft for such a concept:

#### **Restitution**

##### Art. 1 Restitution following avoidance

- (1) On avoidance either party may claim restitution of whatever it has supplied under the contract, or the part of it avoided, provided that such party concurrently makes restitution of whatever it has received under the contract, or the part of it avoided.
- (2) If restitution in kind is not possible or appropriate, an allowance has to be made in money whenever reasonable.
- (3) The recipient of the performance does not have to make an allowance in money, if the impossibility to make restitution in kind is attributable to the other party.
- (4) Compensation may be claimed for the necessary expenses linked to the performance received. Compensation for other expenses linked to the performance received may be claimed as far as the other party is enriched by them.

##### Art. 2 Restitution following termination

- (1) Art. 1 also applies to termination of a contract to be performed at a particular point in time.
- (2) On termination of a contract to be performed over a period of time restitution can only be claimed for the period after termination has taken effect, provided the contract is divisible.

58. Zimmermann said it needs to be changed from “Art. 1 Contracts to be performed at a particular point in time” to “at one time”. Bonell said in Art 2 “also” can be deleted. Zimmermann and Goode said it should be “applies too”. Zimmermann suggested as an alternative “On termination of a contract to be performed at one time, Art 1 applies”, which was accepted by Bonell and Goode. Zimmermann said another alternative is “...applies accordingly”, or “with appropriate modifications”. Goode and Fauvarque-Cosson asked “according” to what. Zimmermann said he also found this formulation odd, but that is used in the principles. So it was agreed to draft the provision with “applies accordingly”.

59. Zimmermann suggested to have a look at conditions, while Fauvarque-Cosson was still present. Fauvarque-Cosson asked if a special Article is needed for it and why there should not be an Art 1 saying this chapter applies to avoidance, termination, illegality and conditions. Zimmermann replied that there may be cases not falling under these categories, like termination after hardship, or dissent.

60. Goode asked about the application to suspensive conditions and Bonell said he does not think they should be covered. Zimmermann agreed and said it can only apply to resolutive conditions. Goode thought the same about it. Zimmermann made an example about the sale of a house under a resolutive condition and deducted there has to be restitution. Goode raised doubts because he saw the common law problem of transfer of property and pointed out that there is no retrospectivity. Fontaine said the only case where he can think of restitution is when the parties do not know about the resolutive condition occurring and still perform. Zimmerman mentioned that the principles said the goods have to go back. Furmston said it was not self evident that the price to pay must be the original price. Goode thought this was a recurrent problem of focusing on sale. He doubted if one should give back the property while the money will no longer be worth as much and said the drafting should not be dominated by sales.

61. Bonell then mentioned a license contract to produce a drug, subjective to the resolutive condition that the drug is not taken off the market. Or, as Goode added, condition to the administrative license being revoked. He also said that resolutive conditions are very much the exception in this context and that it is fine from his point of view that there is no retroactivity. Furmston said it seems odd to say there was no retrospective effect and then provide the result of retrospectivity. Fauvarque-Cosson said one should distinguish restitution and restrospective effect, but Goode thought the effects were nearly the same.

62. Zimmermann suggested to look at a realistic example. Goode reiterated the license example with resolutive condition that the drug authority approval is not revoked. Fontaine provided an example of a franchise coming to an end and said that what has been loaned needed to go back. Goode said that this is not a restitution issue but a contract issued. Zimmermann asked if that meant Goode applies Art 2 (2) in such a case, meaning there will be consequences in restitution only for the future. Goode said this is indeed his point of view but also, that the parties should agree upon what they wanted themselves. Zimmermann, however, pointed out that the principles are default rules and Bonell said the problem remains, even if cases of retroactivity are rare. Goode said the percentage of contracts containing resolutive conditions is very small and the percentage of those without contractual solution even smaller. Zimmermann asked what follows from that and Goode said the issue could be solved by just giving examples. Zimmermann said that the draft needs to have a rule for the termination of the condition and asked if it should refer to Art. 2 sub (2). Goode was in favour of it. Zimmermann said that as a consequence, a rule in Fauvarque-Cossons chapter should

refer to it. Fauvarque-Cosson said that in case of outsourcing a resolutive condition may not be as rare.

63. Zimmermann and Goode then suggested a reference to Art. 1 can be made for cases involving transfer of property. Zimmermann said that this should be in Fauvarque-Cosson's draft, as he was doing the general rules and special provisions in other drafts can refer to these regarding resolutive conditions. Bonell suggested that for the time being, an Art 3 regarding resolutive conditions should refer to Art 2. Fontaine and Fauvarque-Cosson did not like the idea of having a reference to Art. 2 which in turn refers to Art. 1, thus creating a double reference. Zimmermann and Bonell found the double reference clearer, even though it was not elegant. As Fauvarque-Cosson and Fontaine objected to the double reference, it was agreed that Fauvarque-Cosson and Zimmermann would each prepare a draft.

64. Fauvarque-Cosson's suggested alternative was: "Unless circumstances indicate otherwise, on fulfilment of a resolutive condition, restitution can only be claimed for the period after the fulfilment of the condition." Zimmermann suggested to invert it to: "On fulfilment of a resolutive condition, restitution can only be claimed for the period after the fulfilment of the condition, unless circumstances indicate otherwise." Goode agreed to this suggestion. It was agreed to have Zimmermann refer to it only for the time being, and that Fauvarque-Cosson would explain it in her chapter.

Working Group for the preparation of  
Principles of International Commercial Contracts (3<sup>rd</sup>)  
Drafting Committee  
Hamburg, 3-6 March 2008

## **Session 3:**

### **Conditional Obligations**

(UNIDROIT 2008 Study L – WP.16)  
Reporter: Bénédicte Fauvarque-Cosson

Minutes

Present:

Prof. Joachim Bonell  
Prof. Bénédicte Fauvarque-Cosson  
Prof. Marcel Fontaine  
Prof. Michael Furmston  
Prof. Roy Goode  
Prof. Reinhard Zimmermann

Keeper of the Minutes: Dr. Jens Kleinschmidt

1. By way of general introduction into her working paper, Fauvarque-Cosson explains that she has prepared a detailed draft because it is always easier to delete a proposal than to add new text.

#### **Title of the Chapter**

*“Conditional Obligations”*

2. At the 2007 meeting in Rome, it had already been agreed that the title of the Chapter should be “Conditional Obligations” rather than “Conditions”.

3. The pertinent article in the DCFR is entitled “Conditional Rights and Obligations” (Art. III-1:106 DCFR). Zimmermann points out that the title will depend on what is meant by “obligation”. The term can have either only a passive side or an active and a passive side. If the latter is the case, calling the chapter “Conditional Obligations” will be sufficient. Bonell and Fontaine draw attention to the usage of the term “obligation” in Chapter 9 of the PICC.

4. It is agreed that the title of the Chapter should be “Conditional Obligations”.



## **Articles 1 – 3**

### *“Article 1. Definition*

*A contractual obligation is conditional where it is contractually made to depend upon the occurrence of a future and uncertain event.*

### *Article 2. Effect of a suspensive condition*

*A suspensive condition is an event until which the creation of the obligation is suspended. Upon fulfillment of the condition, the obligation takes effect. It has no retroactive effect, unless the parties otherwise agree.*

### *Article 3. Effect of resolutive condition*

*A resolutive condition is an event on which the obligation is terminated. Upon fulfillment of the condition, the obligation comes to an end. It has no retroactive effect, unless the parties otherwise agree.”*

5. Fauvarque-Cosson reminds the group that the terminology “suspensive condition” and “resolutive condition” has already been agreed upon at the 2007 meeting in Rome.

6. It is agreed that Articles 1 – 3 should be replaced by Art. 16:101 PECL and a second article entitled “No retroactive effect”: “Neither a suspensive condition nor a resolutive condition has retroactive effect, unless the parties otherwise agree.”

### *a) Types of condition*

7. The wording of Art. 16:101 PECL is preferred since it expresses the ideas contained in Articles 1 – 3 of the Draft in a clear and concise way.

8. Although the PICC only deal with contractual obligations, the group prefers to retain the reference to a “contractual obligation” in Art. 16:101 PECL. The word “contractual” should not be deleted.

9. The fact that the chapter does not deal with conditions imposed by law, on the other hand, is sufficiently expressed by the wording “may be made conditional” which implies that the condition is of contractual origin. If further clarification of this point is needed, it can be dealt with in the comments.

10. Conditions implied by court can be left out.

*b) New article on retroactive effect*

11. The new article on retroactive effect takes up important concerns expressed at the 2007 meeting. Because of these concerns, Fauvarque-Cosson suggests to include a rule on (the lacking) retroactive effect at the beginning of the Chapter. Whereas Zimmermann thinks that the wording of Art. 16:101 PECL also covers this question, Bonell and Fontaine prefer to have an explicit black-letter rule on that matter. Art. 16:103 PECL contains such a black-letter rule.

12. However, Art. 16:103 PECL does not need to be taken over verbatim, because it partially repeats what is already expressed in Art. 16:101 PECL. Bonell therefore suggests the wording of the additional article.

13. Fauvarque-Cosson adds that the expression “unless the parties otherwise agree” should be preferred to “unless the circumstances indicate otherwise”.

14. Fontaine draws attention to possible problems of unwinding the contract if the parties agree that a resolutive condition shall have retroactive effect (compare Art. III-1:106 [5] DCFR). Zimmermann will bear this issue in mind.

**Article 4**

*“Article 4. Condition must be possible and lawful*

*A condition must be possible and lawful. A condition which rests on a thing that is impossible or unlawful is null and nullifies the contract which depends upon it.*

*However, the condition can be struck out and contract can be maintained when the condition was not a decisive reason for the parties’ having entered into the contract.”*

15. Article 4 deals with conditions the fulfilment of which is impossible, on the one hand, and with unlawful conditions, on the other hand.

16. Bonell states that at least three cases have to be distinguished: First, a distinction has to be made between impossible and unlawful conditions, and then a further distinction exists between impossible suspensive conditions and impossible resolutive conditions.

*a) Impossible conditions*

17. The group considers two examples of impossible suspensive conditions: (i) The contracting parties agree that the transaction is conditional upon an export licence being granted to the seller. The parties do not know that a licence cannot be granted because the

government has already imposed an embargo. (ii) A promises B to give him £ 100,000 if race-horse X wins a particular race. A and B do not know that the horse is dead.

18. Zimmermann explains that in the case of an impossible suspensive condition, there is no state of pendency and hence no obligation. No rule would be required to deal with this situation because it follows from the definition provided in Article 1 that there is no obligation, neither conditional nor unconditional. As everybody agrees as to this result, Zimmermann emphasizes that the remaining question is only whether this result is implied in the whole concept of condition and goes without saying or whether it should still be clarified either in the comments or in the black-letter rules.

19. The discussion reveals that in drafting a rule, further complications would have to be taken into account: These complications arise from the distinction between initial and supervening impossibility of fulfilment of the condition. (A case of supervening impossibility would be the imposition of embargo *after* conclusion of the contract but *before* the export licence on which the contract depended could be obtained.) Whereas in the case of initial impossibility, the contract will be invalid and the rules on mistake may come into play, in the case of supervening impossibility the contract will come to an end.

20. Article 4 is dropped as far as it concerns impossible conditions. The provision is regarded as unnecessary and requiring too many detailed distinctions.

#### *b) Unlawful conditions*

21. As far as unlawful conditions are concerned, there is an overlap with the Chapter on Illegality. Therefore, the group agrees to continue the discussion of Article 4 in the context of the Draft Chapter on Illegality.

### **Article 5**

*“Article 5. Condition which depends on the sole will of a party*

*A condition whose fulfillment depends upon the sole will of the party who owes the condition (debtor) is null.*

*However, such a nullity cannot be claimed when the obligation has been performed in full awareness of the situation.”*

22. The group agrees to delete this provision. It is regarded as not necessary, and a previous suggestion had encountered strong opposition at the Rome meeting.

## Article 6

*“Article 6. Undue interference with a condition*

*The parties have an obligation of good faith, cooperation and consistent behavior in the fulfilment of the condition.*

*A condition is deemed to have been fulfilled if the party who is interested in its failure has obstructed its fulfilment.*

*A condition is deemed to have failed if its fulfilment has been caused by the party who had an interest in this occurring.”*

### *a) Preliminary matters*

23. The group clarifies that, in accordance with the discussion at previous meetings, a provision on interference with a condition only applies to conditions and not to terms of the contract. Therefore, for example, the provision will not enable a seller under a contract containing an FOB clause to claim the purchase price without having to deliver the goods, in case the buyer fails to nominate the vessel.

24. The group further restates that the available remedies (specific performance/damages) are to be determined in accordance with the general rules on remedies. Therefore, if a seller – contrary to the duties of good faith and fair dealing – fails to obtain an export licence so that the goods may not be exported, “fulfilment of the condition” does not mean that the buyer must necessarily be able to claim specific performance. In this example, the buyer can only claim damages, since specific performance would be unlawful and hence excluded.

### *b) Reference to the duties of good faith and fair dealing*

25. Fauvarque-Cosson explains that para. 1 of her draft article is in line with the general duties of good faith and fair dealing of Art. 1.7 PICC.

26. Fontaine and Zimmermann suggest to delete para. 1 of the draft article. Both think that a *separate* reference to the duties of good faith and fair-dealing or co-operation is not needed.

27. Fontaine fears that the wording may seem too strong and therefore objectionable to some parties. In his view, it would be preferable to state only in the comments that this is another application of the general duties of good faith and fair dealing.

28. Zimmermann argues that the reference to the duties of good faith and fair dealing or co-operation is needed in the black-letter text of paras. 2 and 3. It is the “obstruction” that has to be contrary to these duties, since a party might also obstruct the fulfilment of a condition not-

knowingly and innocently. Otherwise the provision would go too far. Both concepts are linked together and should appear in the same sentence, as is the case in Art. 16:102 PECL.

29. The group agrees with Zimmermann and decides to take Art. 16:102 PECL as the starting point.

*c) Revision of Art. 16:102 PECL*

30. Goode suggests to delete the phrases “and if fulfilment would have operated to that party’s disadvantage” and “and if fulfilment operates to that party’s advantage” respectively, because fulfilment of a condition may well operate to both parties’ advantage or disadvantage. Fontaine adds that, if these phrases are deleted, the article would cover situations where both parties can influence the occurrence of the future event.

31. The group agrees with Goode’s suggestion to delete the phrases mentioned in the preceding paragraph.

32. Goode suggests to rephrase the article: In the case of a suspensive condition, the condition should not be deemed to be fulfilled, but the party acting contrary to good faith etc. should not be able to rely on the non-fulfilment. In case of a resolutive condition, the condition should not be deemed not to be fulfilled, but the party acting contrary to good faith etc. should not be able to rely on the fulfilment. This wording would strengthen the position of the other party because it would grant him an option: In case of a suspensive condition, for instance, it could still decide to walk away from the contract.

33. The consequences of the rephrased wording are tested with the help of illustrations 1 and 2 to Art. 16:102 PECL (*Lando/Clive/Priim/Zimmermann*, Principles of European Contract Law, Part III, 2003, p. 234). In illustration 1, the changed wording would not change the position of A; he would be bound by the contract and unable to rely on the non-approval. B on the other hand would have an option to either walk away from the contract (e.g., because he no longer wishes to co-operate with A) or treat the condition as fulfilled and exercise the remedies available to him under the PICC. In illustration 2, again, the changed wording would not affect D’s position who would not be entitled under the contract. E, again, would have an option: He would not be under any obligation to perform, but he may perform if he chooses.

34. The group agrees that rephrasing the article in accordance with Goode’s suggestion would be an improvement.

35. Bonell adds that the rephrased wording would also be in line with Art. 1.8 PICC on inconsistent behaviour.

*d) Heading of the new provision*

36. The group agrees on the heading “Interference with Conditions”.

**Article 7**

*„Article 7. Rights preserved*

*Before the condition is satisfied, the party for whose benefit a condition has been stipulated (creditor) may take all measures necessary to preserve her rights, and take action against any transaction effected by the debtor in fraud of her rights.*

*a) Policy of the provision*

37. Fauvarque-Cosson explains that the provision is a corollary of the general lack of retroactive effect. *Pendente conditione* a party’s actions may detrimentally affect the other party’s position. The underlying idea of the provision is that it is generally better to prevent such actions than to cure their results.

38. As an illustration, Fauvarque-Cosson gives the case of a sale of a house under the condition that the buyer obtains a loan to pay the purchase price. While trying to procure the loan, the buyer realises that the seller is going to lease the house to a third party. The buyer should be able to prevent the seller from concluding the lease by an injunction.

39. In order to underline that the provision is not only related to proprietary rights, Bonell adds the example of a conditional sale of a house in the mountains, and while the condition is pending in winter, the seller deliberately turns off the heating.

40. The group is divided as to whether a provision is needed to cover this type of situation. Furmston, Goode and Zimmermann are in favour of deleting the provision for the following reasons: (i) The idea expressed by the rule is already covered by the general duties of good faith and fair dealing or co-operation. The problem addressed by the provision is not particular to conditional obligations. (ii) It might look strange to have a special provision to prevent a threatened breach of contract in the context of conditions, while there is no rule on this question in general. (iii) A special rule might even invite an unwanted *e contrario*-argument to the effect that in other instances no such duty applies. (iv) It is unclear what measures are meant by the provision. Self-help should, of course, be excluded. Concerning interim relief, the question must necessarily be left to the national laws of procedure, which seem to differ on this point. (vii) In the illustration given, the lease of the house can be approached with the general rules on breach of contract.

41. Bonell, Fauvarque-Cosson and Fontaine are in favour of including a special provision in the draft for the following reasons: (i) There are similar provisions in some national codes. (ii) The question whether interim relief is granted can be left to the national courts. The provision is still important both in arbitration proceedings and as a reminder to the parties who enter into a contract under a condition to consider this issue. (iii) The situation *pendente conditione* is different from breach of contract in general and therefore deserves special treatment. (iv) Because of the peculiarities of a conditional obligation, one does not have to fear an unwanted *e contrario*-argument.

42. Since the group is divided, Bonell and Fauvarque-Cosson as the Reporter suggest that the issue be discussed by the entire Working Group.

*b) Drafting of the provision*

43. Some members of the group consider the draft provision as too vague. Zimmermann points out, first, that the phrase “all measures” is unclear and possibly too wide and, secondly, that it would be in line with the decision on Article 6 to delete the requirement that the condition be to the benefit of one party in this article as well.

44. The group agrees on a new drafting: “Pending fulfilment of the condition, a party shall act in such a way as not to prejudice the other party’s rights in case of fulfilment of the condition.”

45. This new drafting is supposed to make it sufficiently clear that it only refers to conditional obligations. It is strongly felt that the reference to the “other party’s *rights*” is required so that the provision is sufficiently precise.

*c) Application to both suspensive and resolutive conditions*

46. The group stresses that the provision applies to both suspensive and resolutive conditions. A possible example of a resolutive condition is given by Fontaine: A, who works in Paris, sells his house in Bordeaux to B under the resolutive condition that A gets a new job in Bordeaux.

47. However, Goode and Zimmermann express doubts: In their view, the envisaged provision could unduly restrict the buyer’s possibilities to refurbish the house and remodel it to his needs, for example if A is a professor and B an artist and therefore B wants to turn A’s study into a studio.

## **Article 8**

*“Article 8. Transmission and assignment*

*Conditional obligations are transmissible on death, unless the parties have provided otherwise, or the nature of the obligation prevents it. Subject to the same restriction, the benefit of condition obligation is assignable inter vivos.”*

48. The group agrees to delete Article 8.

## **Article 9**

*“Article 9. Time of transfer of risk*

*Unless the parties otherwise agree, where an obligation has been contracted under a suspensive condition, the thing (goods) which is the subject matter of the contract is delivered only when the condition is satisfied ; before delivery, the thing remains at the risk of the party who must deliver it (debtor).”*

49. The group agrees to delete Article 9.

## **Article 10**

*“Article 10. Deterioration and perishment*

*If, before the condition is fulfilled, the thing deteriorates, the beneficiary of the condition (creditor) has a choice between terminating the contract and requiring the thing as it is, with reduction of price, without prejudice to any award of damages which may also be due under the national rules of tort law.*

*If the thing perishes in its entirety, the obligation is extinguished and the contract terminated, without prejudice to any award of damages which may also be due under the national rules of tort law.”*

50. The group agrees to delete Article 10, since the situation addressed is arguably covered by the redrafted article 7 and, moreover, the PICC do not know a remedy of reduction of the price.

\* \* \*



## Appendix 1: Synopsis

Draft WP.16

Draft as of 5 March 2008

Conditional Obligations	Conditional Obligations
<p><b>Article 1. Definition</b>  A contractual obligation is conditional where it is contractually made to depend upon the occurrence of a future and uncertain event.</p> <p><b>Article 2. Effect of a suspensive condition</b>  A suspensive condition is an event until which the creation of the obligation is suspended. Upon fulfillment of the condition, the obligation takes effect. It has no retroactive effect, unless the parties otherwise agree.</p> <p><b>Article 3. Effect of resolutive condition</b>  A resolutive condition is an event on which the obligation is terminated. Upon fulfillment of the condition, the obligation comes to an end. It has no retroactive effect, unless the parties otherwise agree.</p>	<p><b>Article 1. Types of Condition</b>  A contractual obligation may be made conditional upon the occurrence of an uncertain future event, so that the obligation takes effect only if the event occurs (suspensive condition) or comes to an end if the event occurs (resolutive condition).</p> <p><b>Article 2. No Retroactive Effect</b>  Neither a suspensive condition nor a resolutive condition has retroactive effect, unless the parties otherwise agree.</p>
<p><b>Article 4. Condition must be possible and lawful</b>  A condition must be possible and lawful. A condition which rests on a thing that is impossible or unlawful is null and nullifies the contract which depends upon it.  However, the condition can be struck out and contract can be maintained when the condition was not a decisive reason for the parties' having entered into the contract.</p>	<p><i>[deleted as far as possibility of fulfilment is concerned]</i>  <i>[to be discussed in the context of the draft chapter on illegality as far as unlawfulness of condition is concerned]</i></p>
<p><b>Article 5. Condition which depends on the sole will of a party</b>  A condition whose fulfillment depends upon the sole will of the party who owes the condition (debtor) is null.  However, such a nullity cannot be claimed when the obligation has been performed in full awareness of the situation.</p>	<p><i>[deleted]</i></p>

<p><b>Article 6. Undue interference with a condition</b>  The parties have an obligation of good faith, cooperation and consistent behavior in the fulfilment of the condition.  A condition is deemed to have been fulfilled if the party who is interested in its failure has obstructed its fulfilment.  A condition is deemed to have failed if its fulfilment has been caused by the party who had an interest in this occurring.</p>	<p><b>Article 3. Interference with Conditions</b>  (1) If fulfilment of a condition is prevented by a party, contrary to the duties of good faith and fair dealing or co-operation, that party may not rely on the non-fulfilment of the condition.  (2) If fulfilment of a condition is brought about by a party, contrary to the duties of good faith and fair dealing or co-operation, that party may not rely on the fulfilment of the condition.</p>
<p><b>Article 7. Rights preserved</b>  Before the condition is satisfied, the party for whose benefit a condition has been stipulated (creditor) may take all measures necessary to preserve her rights, and take action against any transaction effected by the debtor in fraud of her rights.</p>	<p><b>Article 4. Rights Preserved</b>  Pending fulfilment of the condition, a party shall act in such a way as not to prejudice the other party's rights in case of fulfilment of the condition.</p>
<p><b>Article 8. Transmission and assignment</b>  Conditional obligations are transmissible on death, unless the parties have provided otherwise, or the nature of the obligation prevents it. Subject to the same restriction, the benefit of condition obligation is assignable inter vivos.</p>	<p><i>[deleted]</i></p>
<p><b>Article 9. Time of transfer of risk</b>  Unless the parties otherwise agree, where an obligation has been contracted under a suspensive condition, the thing (goods) which is the subject matter of the contract is delivered only when the condition is satisfied ; before delivery, the thing remains at the risk of the party who must deliver it (debtor).</p>	<p><i>[deleted]</i></p>
<p><b>Article 10. Deterioration and perishment</b>  If, before the condition is fulfilled, the thing deteriorates, the beneficiary of the condition (creditor) has a choice between terminating the contract and requiring the thing as it is, with reduction of price, without prejudice to any award of damages which may also be due under the national rules of tort law.  If the thing perishes in its entirety, the obligation is extinguished and the contract terminated, without prejudice to any award of damages which may also be due under the national rules of tort law.</p>	<p><i>[deleted]</i></p>

Working Group for the preparation of  
Principles of International Commercial Contracts (3<sup>rd</sup>)  
Drafting Committee  
Hamburg, 3-6 March 2008

#### **Session 4:**

#### **Illegality**

(Unidroit 2008 Study L – WP.17)  
Reporter: Michael Furmston

#### Minutes

Present:

Prof. Joachim Bonell  
Prof. Bénédicte Fauvarque-Cosson (only part of the session)  
Prof. Marcel Fontaine  
Prof. Michael Furmston  
Prof. Roy Goode  
Prof. Reinhard Zimmermann

Keeper of the Minutes: Dr. Phillip Hellwege

1. Introducing his draft chapter Furmston pointed out that it takes account of what has been agreed on at the session in Rome. It is not based on any particular national legal system in the world because, in the view of Furmston, the rules on illegality of all legal systems are defective. As a consequence the draft rules are different from those to be found in any national legal system. They are also different from those to be found in the PECL. His aim was to draft rules that are sensible in an international context.

2. Bonell asked Furmston to give more background information about his draft articles, especially concerning international instruments like the PECL and the Restatements for the next meeting, and Zimmermann added that such background information would make it easier to see and to explain where and why the draft chapter deviated from other rules on illegality.

3. Furmston then introduced Art. 1 of the draft chapter. He pointed out that the definition in Art. 1 draws on the definition of Art. 15:101 PECL the difference being that for the PICC the number of widely accepted principles is smaller than for the PECL. One principle that is, however, generally accepted even on a broader level is that corruption is not allowed.

4. Furmston turned to the different possibilities of how to define illegality. It could be defined by a broad statement as found in the PECL, by a broad statement accompanied by examples, or by a list of prohibited heads. Art. 1 contains a broad definition but paragraph

three of the comment gives a number of examples of the definition. Furmston went on to explain these examples. After that he turned to the fourth paragraph of the comments. He summarised that many systems have a category of contracts prohibited by statute. Since Unidroit has no legislature it has not created such rules. They are left to Art. 1.4.

5. Bonell commented that the PECL in Art. 15:101 and 15:102 prefer a two tier system. The draft chapter follows, however, only a one tier approach, and Zimmermann added that Art. 1 of the draft chapter only contains the first tier of the PECL to be found in Art. 15:101 and leaves the second tier of Art. 15:102 PECL to Art. 1.4 PICC. He asked whether or not the PICC should also have a second tier in the chapter on illegality. Fauvarque-Cosson reminded of the fact that Art. 1.4 addresses a question of private international law, especially the question whether one should accept a choice of law that is designed to escape mandatory rules. Bonell agreed that Art. 1.4 deals with a different problem than the present draft chapter on illegality does, and he asked, just like Zimmermann, whether or not the present chapter should approach the problem of the effects of illegality themselves. Fontaine agreed and pointed to the fact that many mandatory rules leave the question as to their effects open. Bonell suggested that this is the point where the PICC could come into place: by giving autonomous rules as to the effects of the infringement of a mandatory rule; the rules of the PICC could be more flexible than those of the national laws; the PICC could even offer in those cases rules as to the effects of the infringement of a mandatory rule if the infringed mandatory rule is from a national law. Zimmermann supported this view and argued that this is actually the position of the PECL as becomes obvious from illustration 1 in the comment to Art. 15:102 PECL: The example falls under the second tier although the mandatory rule which has been infringed in that example is clearly one that falls under Art. 1:103 PECL.

6. Furmston replied that he thought he had to leave such cases out. A discussion followed as to the correct interpretation of Art. 1.4 PICC. Furmston put forward the case that a national mandatory rule explicitly states that a contract made in contravention of it is invalid. He asked whether Art. 1.4 PICC means that the national mandatory rule only declares the contract to be illegal whereas the PICC can now opt for a different effect of the illegality than provided in the national mandatory rule. Bonell answered the question in the negative; however, in many if not most cases the domestic mandatory rules do not explicitly state what the effects of an infringement are. In these cases it is open to the PICC to provide a rule for the effects of the illegality. Furmston affirms that he has read Art. 1.4 PICC in a different way: the national mandatory rules do not only state that the contract is illegal but also what the effect of the illegality in the specific law is. However, Furmston agrees that Art. 1.4 PICC can also be interpreted in the way proposed by Bonell. Zimmermann expressed his agreement with Bonell's interpretation: if the national law provides for a specific consequence that consequence has to follow; however, if the effect of the infringement is open, then the PICC can, just like the PECL, make an autonomous rule. On this basis the different examples provided in Furmston's draft chapter were discussed. Bonell pointed to example e in the Comment to Art. 2 of the draft chapter. The mandatory rule which states that the lorry is not allowed to be used for this purpose is of national origin, but the effect of the infringement is open to the PICC.

7. Goode drew the attention to judge made law: how is the case to be solved if the domestic mandatory law leaves the consequences of an infringement open but if they have

been settled by judge made law? Zimmermann argued that in this case, too, it is open to the PICC to state a different effect of illegality.

8. It had been pointed out in the discussion that the mandatory law must be applicable to fall within 1.4.

9. Finally, an agreement was reached that the second tier should be dealt with in a separate article, a new Art. 2, which needs to be drafted.

10. The discussion then turned to Art. 1 and to Example 1 in which the “principle widely accepted throughout the international community of states” has been drawn from an international convention. Zimmermann asked what is meant by “principles”, where these “principles” can be gathered from, from which convention such “principles” can be drawn from, whether they can only be gathered from international conventions or also from national law if they are widely accepted. Furmston favours both: conventions can be a source for such principles mentioned in Art. 1. However, one can gather such principles also from national laws if it is widely accepted that certain dealings are illegal. Furmston also drew attention to the fact that views on what counts as a fundamental principle can change over the development of time and can be different in different parts of the world. Bonell proposed that this relativity of principles and their historical evolution should be stressed in the comment to Art. 1. He also argued that one should distinguish for the application of Art. 1: If the parties to the contract are from two states which share certain principles these principles should be recognised under Art. 1 even though they might not yet be accepted throughout the international community of states. The higher standard of the two countries should prevail. In addition Bonell questioned whether the phrase “international community of states” is not misleading. It could be interpreted as only referring to public international law. Furmston stressed that Art. 1 is not limited to principles of public international law and that principles do not lose their force because some countries do not (any longer) adhere to them.

11. In the light of Bonell’s last objection Goode proposed to change: “principles widely accepted throughout the international community” into: “principles widely accepted internationally”. Zimmermann argued that this would also include international commercial practices. Everybody agreed that commercial practices should not fall under Art. 1 of the draft chapter: a normative criteria needs to be found. Fontaine added that such normative criteria is not needed to exclude bad principles from the application of Art. 1 because bad principles will perhaps be used but they will not be “accepted”.

12. The discussion reached an agreement to change “principles widely accepted throughout the international community” into: “principles widely accepted as fundamental in legal systems throughout the world”. Thus, it was agreed that Art. 1 should read:

“Art. 1: Definition. A contract is illegal if the contract, or a substantial part of the contract, is contrary to principles widely accepted as fundamental in legal systems throughout the world.”

13. There was then a discussion on the introductory phrase of Art. 1: Bonell pointed to the fact that Art. 1 starts out with: „A contract is illegal ...“, whereas Art. 2 begins: “A contract may be illegal ...”. He asked whether this different wordings made some difference. Bonell also questioned whether the term “illegal” should be avoided altogether. Furmston

added that he thought to use the phrase “not accepted” instead of the word “illegal”, and Goode observed that also the PECL avoid using the word “illegal”. However, an agreement was reached that the term “illegal” should be kept in Art. 1 and that it should also be used for the second tier.

14. The discussion then focused on the phrase “or a substantial part of the contract”. Zimmermann was of the opinion that this phrase addresses the problem of partial illegality / partial invalidity and that the problem of partial illegality should be devoted to a separate article. It should not be dealt with incidentally in this Art. 1. He also pointed out, that Art. 1 seems to suggest that it is of no consequences if only an insubstantial part of the contract is illegal. Zimmermann stressed that the opposite may be true. Even the illegality of an insubstantial part of the contract can affect the contract as a whole. If one only were to strike out the word “substantial” then Art. 1 would be too wide, since, in the view of Zimmermann, partial illegality does not turn the whole contract into an illegal one. The problem is about the effects of illegality, not about the definition of illegality. Zimmermann favoured a separate rule on partial illegality.

15. A tentative agreement was reached that in Art. 1 the word “substantial” probably should be deleted. In the following discussion Bonell pointed to Art. 3(3) which also deals with partial illegality. Goode and Furmston argued that Art. 3(3) says that even if the contract is illegal according to Art. 1 rights can arise under it. Read this way, both articles make, as they stand, perfect sense. Zimmermann again made the point that the whole phrase: “or a substantial part of the contract” should be deleted. Bonell, Fontaine, and Fauvarque-Cosson favoured this approach, and Bonell pointed to Art. 15.103 PECL where the question of partial illegality is also dealt with in a separate article. However, Goode insisted that there needs to be a definition to the end that a partial illegality might turn the contract into a fully illegal contract. Goode did not think that it is possible to leave the problem as to the definition unsettled and only deal with the problem from the end of the effect. Bonell responded that Art. 3.16 PICC deals with the problem of partial avoidance also only from the end of effect. Goode then made the point that there is in fact some discrepancy between Art. 1 and Art. 3(3): Art. 1 says that the illegality of an insubstantial part of the contract will not turn the whole contract into an illegal contract. However, Art. 3(3) also deals with the effects of a contract if only an insubstantial part of it is contrary to principles widely accepted as fundamental. Thus, Art. 3(3) may apply although one has decided under Art. 1 that the contract is not illegal. After some more discussion it was concluded to leave the word “substantial” for the time being in Art. 1.

16. Goode then turned to Example 1 in the Comment to Art. 1. Goode thought it to be misleading. Firstly, it should not be the signature of the convention that counts but the ratification. Secondly, the reader of the example focuses too much on the convention and the numbers of countries that have ratified the convention. Many if not most conventions have not been ratified by most of the states in the world. However, it is not necessary for a principle to count as widely accepted that most countries have ratified the convention from which the principle is gathered: There is no necessary correlation between the number of ratification and the question of whether or not a principle is widely accepted. It was agreed that the phrase “which is widely accepted” should be included in the end of the sentence: “This is contrary to an international convention”, and that the last three lines of the example can be deleted.

17. The discussion then turned to Art. 2. Furmston explained that he tried to describe when a contract may be illegal. Fontaine thought that, although Art. 2 is not meant to be a closed enumeration – this becomes obvious from the word “may” –, such enumeration should not appear in the article itself but rather in the comment. Goode replied that Art. 2 makes sense: Art. 1 only states that the contract itself may be illegal and Art. 2 adds that it can become illegal because its performance violates a relevant principle. However, after some discussion an agreement was reached that Art. 2 should be deleted. What is now the blackletter rule should go into the comment to Art. 1. What is now comment to Art. 2 should become illustrations to the comment. The examples (a) to (e) in what is now the comment to Art. 2 should follow immediately after the corresponding comment (a) to (e) in what is now the blackletter rule. It has also been agreed upon that as a consequence Art. 1 needs to be drafted broader.

“Art. 1. Definition: A contract is illegal if, whether by its terms, performance or otherwise, it is contrary to principles widely accepted as fundamental in legal system throughout the world.”

18. The discussion then went on to the different examples which are now contained in the Comment to Art. 2 and which should appear as illustrations in the comment to the revised Art. 1. Zimmermann critically observed that the examples in the comment, especially example b, are taken from domestic law and do not relate to international commercial contracts. The discussion reached an agreement that the examples should rather involve international contracts. Zimmermann also questioned the result of example e: He argued that this is not an illegal contract: it would have been an illegal contract if the parties had agreed that the contract should be performed with the lorry which is not licensed for this purpose. Goode and Furmston disagreed: the illegal performance may turn the contract into an illegal contract with the consequence that only one party might be able to enforce it. Goode proposed that letter a: “whose performance violates a relevant principle” should be changed into “whose performance will violate a relevant principle”, and it was generally approved that letter a should appear in the comment to Art. 1 only in this changed form. After some discussion Furmston agreed that he will think of a new example to illustrate letter c.

19. Furmston went on to introduce Art. 3 and Art. 4: Art. 3(1) contains as a general rule that the contract is unenforceable if both parties knew, or ought to have known, of facts which make the contract illegal and (3) relativises this general rule in case of partial illegality.

20. Zimmermann asked whether Art. 3 could also be applied to the case of an infringement of a mandatory rule. Furmston answered in the positive. Zimmermann then questioned whether knowledge is also the decisive factor when a mandatory rule is infringed. Zimmermann proposed that also other factors have to be taken into account: the intention of the parties, the seriousness of the infringement, and policy considerations. An agreement was reached that Art. 3 has to be discussed separately for the two tiers. It has also been agreed upon that the phrase “if it had behaved reasonably” can be deleted both in Art. 3(1) and (2) since this is already contained in the word “ought”.

“Art. 3. Effects: (1) Where each party knows, or ought to have known, of facts which make the contract illegal, neither party has the right to enforce the contract.

(2) Where one party neither knew nor ought to have known of facts which make the contract illegal, it shall have such rights to enforcement or to damages as in all the circumstances are reasonable, paying due regards to the policies underlying the relevant principle.”

21. The discussion then centred around the term “enforce”. Zimmermann asked whether the contract should not be declared “void” or “invalid”. Furmston disagreed: all that needs to be said is that neither party can sue for specific performance and that neither party can sue for damages. Zimmermann und Goode went on to discuss what difference it could make to declare the contract “void” or “invalid”, especially with regards to restitution and the transfer of property. Goode and also Furmston believed that it would follow from declaring a contract void that there is prima facie restitution: if A gives money to B for killing C, under Art. 3 the contract cannot be enforced; if the contract was void it should follow that A has a right against B for the repayment of the money; Goode and Furmston argued that this result cannot be correct. Zimmermann responded that this was a case for the *pari turpitudine* rule. Goode and Furmston insisted that there are no practical differences between “enforce” and “void” and that “enforce” should therefore be kept. This was supported by the group.

22. Bonell, however, reminded that the term “enforce” has not yet been used in the PICC to mean what Furmston just has explained; people will rather understand it to refer only to specific performance. He proposed to change “enforce” into “is of no effect”. An agreement was reached that the phrase “exercise remedies under the contract” is better.

“Art. 3. Effects: (1) Where each party knows, or ought to have known, of facts which make the contract illegal, neither party has the right to exercise remedies under the contract.

23. It was then agreed that a similar change should be made to Art. 3(2). The phrase: „it shall have such rights to enforcement or to damages“ should be replaced by „it shall have such remedies“.

“(2) Where one party neither knew nor ought to have known of facts which make the contract illegal, it shall have such remedies if this in all circumstance is reasonable, paying due regards to the policies underlying the relevant principle.”

24. Bonell turned to the phrase “paying due regards to the policies underlying the relevant principle” in the end of Art. 3(2) and asked whether that is all that needs to be taken into consideration. Zimmermann also wondered whether there are other considerations, such as the seriousness of the infringement. Bonell suggest that this phrase can only apply to the first tier, not, however, to the second and that it needs to be deleted insofar.

25. Bonell then asked whether the innocent party in Art. 3(2) should not always have a remedy under the contract. Goode disagreed and stated that this would depend on the circumstances of the individual case. It was also discussed whether it is possible that the innocent party can claim damages, but not specific performance. Fontaine came up with the example that somebody purchases goods the trading of which is illegal; however, the buyer did not know about this illegality; the buyer might be able to claim damages, but he will not be able to ask for specific performance. Everybody agreed that this example should appear in the comment.



26. The discussion went on to Art. 3(3). Zimmermann reminded of the point, which had been made earlier by Goode, that it could happen that a contract is not illegal under Art. 1 because only an insubstantial part of the contract contravenes principles in the sense of Art. 1 but that Art. 3(3) nevertheless needs to be applied. Zimmermann and Bonell wondered whether Art. 3(3) perhaps even only covers the case in which only an insubstantial part of the contract contravenes fundamental principles; if a substantial part of the contract contravenes fundamental principles then Art. 1 tells us that the whole contract is illegal; however, Art. 3(3) requires only a partial illegality to be applicable; thus, only Art. 3(1) and (2) are applicable. Furmston and Goode expressed the view that the opposite conclusion is also possible but should not be taken: if Art. 1 says that the contract is not illegal if only an insubstantial part of it contravenes fundamental principles, Art. 3(3) is not applicable because Art. 1 said that it is not at all illegal; however, Art. 3(3) clearly needs to be applied to this case, too. Furmston agreed that he will redraft Art. 3(3) to remedy these problems.

27. Zimmerman and Bonell drew attention to the fact that in Art. 3(3) the knowledge-test is the only test whereas in Art. 3(2) there was further discretion to the judge. And Goode wondered why Art. 3(3) only mentions damages whereas Art. 3(1) and (2) also speak of specific performance. Furmston agreed to redraft Art. 3(3) in order to align it with Art. 3(2).

28. A further point of consideration was raised again by Zimmermann: Is it possible that only an insubstantial part of the contract is illegal but that one nevertheless wants the whole contract to be unenforceable? Under the present Art. 3(3) such a solution would not be possible. Zimmermann suggested a more differentiated regime.

29. The discussion then turned again to the point whether or not the partial illegality needs to be dealt with already in Art. 1.

30. In conclusion it was agreed that Art. 3(3) needs to be revised. Furmston was asked to draft a new rule that deals with partial illegality taking into consideration that different rules may be needed for the first and for the second tier.

31. Finally, the examples to Art. 3 were the centre of attention. It was agreed that example 1 needs to be split up into two examples. With regards to example 2 it was agreed that the sentence „The injured girls can sue X.“ needs to be deleted or it needs to be indicated that they are not party to the contract and that they may only have a claim in tort; as it stands the example could lead to confusion. An example for Art. 3(3) is still missing and Furmston agreed to think of one.

32. Furmston then introduced Art. 4. He suggested that there needs to be broad discretion as to whether or not restitution should be granted. Zimmermann suggested that one should draft a rule that is a little bit more specific: could one perhaps say that restitution is excluded where the party claiming restitution has contravened the principle which renders the contract illegal? Furmston replied that then in the example to Art. 4 restitution should not be granted; he, however, suggests that it should. Goode agreed with Furmston: B should be able to recover in the example because B repents. In the following discussion the application of the *pari turpitudine*-rule and of the *locus poenitentiae*-rule were discussed.

33. Bonell suggested that the example to Art. 4 should again be an example involving a commercial contract. He then stressed that the importance of Art. 4 is that against the

traditional rule restitution may be granted. He also expressed his wish to see some more examples where restitution is granted. Zimmermann without questioning that the traditional rule might be against restitution asked whether in the PICC the general rule should be against restitution or in favour of restitution. Furmston thought that this question can be left open. Goode expressed his view that the normal rule needs to be against restitution: the loss lies where it falls. Zimmermann mentioned that in Germany the trend goes to granting restitution in case of infringement of mandatory rules. Goode replied that that may be a valid rule in Germany; however, those mandatory rules that will be applied under the second tier will be of such great importance that an infringement of them is so grave that the rule necessarily needs to be against restitution. The group agreed on this approach.

34. Bonell then turned to the formulation of Art. 4. He thought that the phrase “the loss lies where it falls” should not appear in the text of the rule, but that it belongs rather as an explanation into the comment. Everybody agreed. The first sentence of Art. 4 was accordingly reformulated:

“Article 4: Restitution. Where money has been paid or property transferred in performance of a contract which is illegal, the normal rule shall be that there is no restitution. ...”

35. Zimmermann stressed that Art. 4 as it stands only addresses the problem of whether or not restitution should be granted. It does not say anything how restitution should take place. He went on to ask whether Art. 4 should then make up a new restitutionary regime or whether one could just refer to the general restitutionary regime under the PICC (Unwinding Failed Contracts: Unidroit 2008 Study L – WP 15). Furmston and Goode argued very strongly against applying the general restitutionary regime: there has to be discretion first as to whether restitution will take place and second as to how and how much restitution there should be and which remedy is available; they argued that there is the possibility that only partial restitution will seem fair and reasonable. Fontaine suggested that one should examine the general rules on restitution in order to see whether or not they fit to illegal contracts; only then one can answer the question put forward by Zimmermann. Furmston was asked by the group to find examples in which the normal restitutionary rules do not fit and were there is only partial restitution.

36. Finally, Bonell observed that the second sentence of Art. 4 might be hard to understand for somebody not coming from England. Furmston agreed to redraft the second sentence of Art. 4 and to possibly split it up into two sentences.

37. The group closed the session for the day. The group kindly asked Furmston to have finished the redrafting as discussed and to think especially of the restitutionary examples until the next morning.

38. The next morning Furmston presented the following text:

“Art. 1 bis: A contract may contain a provision which is ineffective under a relevant and applicable local law but which does not contravene fundamental principles. The remainder of the contract less the ineffective provision may be enforced.

A contract may be ineffective because it conflicts with an international or national mandatory rule. In considering such a case particular attention should be given to the purpose of the mandatory rule and any express statement in the rule as to its effects.

#### Examples

No. 3: A engages X as a chauffeur at three times the normal rate for chauffeurs. There is a written contract of employment of a normal kind but it is understood that if called on X will kill any of A's business rivals. The contract of employment is ineffective.

No. 4: X, a Utopian company, enters into a contract with Y to erect a building in Ruritania. The contract contains a provision for dispute-settlement by arbitration which can only be initiated after the work has been completed. Ruritanian law has a mandatory provision that either party is entitled to have any dispute settled by neutral adjudication at any time during the contract. This provision prevails but does not effect the validity of the remainder of the contract.

No. 5: A, a Ruritanian merchant, contracts to sell 100 tons of coffee beans to B, a Utopian merchant, on 28 days credit. He delivers the coffee beans but B now refuses to pay on the ground that he does not have, as Utopian law requires, a license to buy coffee. Enquiry shows that the Utopian rule is in effect a tax on importers. A can recover the price.

No. 6: The facts are as in 5 but enquiry shows that the Utopian government has adopted a fair trade policy designed to make sure that Utopian only drink coffee imported from approved countries and that the licensing scheme is an essential part of this policy. A can not sue for the price though he may have a restitutionary remedy.

39. The group then went on to recall what had been agreed upon the day before. For Art. 1 the following agreement had been reached:

“Art. 1. Definition: A contract is illegal if, whether by its terms, performance or otherwise, it is contrary to principles widely accepted as fundamental in legal system throughout the world.”

40. Bonell then recalled that it had been agreed upon that Art. 2 of the present draft is to be turned into the comment to Art. 1 and that the examples in the comment to the present Art. 2 need to be built into the different paragraphs of what is now the blackletter-rule of Art. 2 and what is to become the comment to Art. 1. Bonell also reminded the group of the changes to example 1 agreed upon.

41. Furmston explained that his new examples 3 and 4 deal with partial illegality and that his new examples 5 and 6 relate to mandatory rules. The group first discussed example 3. Zimmermann wondered whether this is really an example of partial illegality; X is paid three times the normal rate because he also has to kill; it is, however, not the case that X gets some money as chauffeur and extra money for killing; only this would be an example of partial illegality; as the example stands it is an example of total illegality. Zimmermann agreed that the result of the example is correct. Fontaine agreed that it would not make any difference whether X gets a normal salary and for the killing an extra “bonus”. Furmston replied that all

of this is a problem of construction. Goode, finally, suggested that the example should again involve a commercial contract.

42. Bonell then turned to example 4. Fontaine asked that there should be two examples one on the breach of a fundamental principle and one on the breach of a mandatory rule. Bonell replied that he cannot think of an example in which the infringement of a fundamental principle does not lead to total ineffectiveness. Then, the correct interpretation of Art. 1.4 PICC was again discussed, and the conclusion was reached that the comment to the first rule of the second tier has to refer the reader to the comment of Art. 1.4 PICC in order to explain the different possible applications of mandatory law.

43. Furmston went on to explain the new examples 5 and 6: the policy considerations underlying the mandatory rules are different and therefore the outcome of the cases needs to be different, too.

44. Furmston then explained the new Art. 1 bis: the first paragraph is aimed at partial illegality, but the illegality does not make the rest of the contract unenforceable.

45. The discussion then went onto the structure of the chapter. Different solutions were discussed: Fontaine declared his preference for two separate provisions: one on partial illegality in which both cases are covered, one on fundamental principles and one on mandatory law. Zimmermann suggested to have Art. 1 on fundamental principles, Art. 2 on mandatory law, and Art. 3 on partial illegality. Zimmermann stressed that it is still open to question whether this Art. 3 can be drafted to cover both Art. 1-illegality and Art. 2-illegality equally.

46. The question was raised how to formulate the new Art. 2 for the second tier. Furmston suggested to build in a reference to Art. 1.4. After lengthy discussion the following formulation had been agreed upon:

“Article 2: A contract, whether by its terms, performance or otherwise, is also illegal if it infringes a mandatory rule applicable under Art. 1.4 under these Principles.”

47. Zimmermann made the point that this definitional rule parallels, as it should do, Art. 1. The second sentence of Art. 1 bis, as presented to the group by Furmston, does not belong to the definition but deals with the effects.

48. The group discussed whether a rule on partial illegality should follow in the definitional rule or whether partial illegality should be dealt with after having dealt with the effects of illegality. Zimmermann favoured the second, the rest of the group the first possibility.

49. Bonell suggested to use Art. 15:103 PECL as a model, and Zimmermann added that one needs to exchange the word “ineffective” in Art. 15:103 PECL by the word “illegal” because the group has decided to deal with partial illegality by way of a definition and not only with respect to the effects of illegality. Furmston suggested that the presumption has to differ in the two rules. With fundamental principles the presumption is in favour of the whole illegality and with mandatory law the presumption is for partial illegality only. On this basis the rules were formulated as follows:

Art. 1(2): “If only part of the contract is illegal under Art. 1 the entire contract is illegal unless giving due consideration to all the circumstances of the case it is reasonable to hold otherwise.”

Art. 2(2): „If only part of the contract is illegal under Art. 2 the remaining part is not illegal unless giving due consideration to all the circumstances of the case it is reasonable to hold otherwise.”

50. The group then turned to redrafting the rules on effects. Zimmermann asked for conceptual clarity and raised again the question whether illegality invalidates the contract or not. If one talks about “to exercise remedies” what about arbitration clauses? Are they valid? What about transfer of ownership? Goode replied that arbitration clauses are kept separately under arbitration law; they can be left out. Zimmermann disagreed because the PICC also talk elsewhere about the effects on arbitration clauses. Furmston stressed that illegality will not affect arbitration clauses, the arbitrator has jurisdiction to decide on the illegality. Bonell then asked about an election of forum clause, about confidentiality clauses, and he drew a parallel to the case of termination. Goode stressed that he feels that invalidity is the wrong response: one party may be able to enforce the contract; the other party may not be able to do so; in terms of validity this would not be explainable. Finally, an agreement was reached that there is no practical relevance whether the contract is valid or invalid and that yesterday’s formulation should be kept.

“Art. 3(1): Where each party knows, or ought to have know, of facts which make the contract illegal under Art. 1, neither party has the right to exercise remedies under the contract.

Art. 3 (2): Where one party neither knew nor ought to have known of facts which make the contracts illegal under Art. 1 it has the right to exercise such remedies as in all the circumstances are reasonable.”

51. Fontaine reminded the group that with respects to illegality the case still needs to be dealt with where only part of the contract is illegal: if the whole contract is illegal the rule is that no remedies are available; if only part is illegal under Art. 1(2) then with regards to the rest remedies are allowed. It was agreed that the old Art. 3(3) is not to be included and that the comments should make clear that the normal remedies apply to the rest of the contract.

52. The discussion was then opened whether or not Art. 3 should be formulated in such a way that it covers both Art. 1 and Art. 2. This approach was favoured by Zimmermann. However, there was agreement that for the time being Art. 3 should first only be formulated with respect to Art. 1 and that the effects with respect to Art. 2 needed to be discussed separately. Zimmermann wondered whether one should perhaps then make two subsection, the fist being only devoted to the infringement of fundamental principles and the second to the infringement of mandatory rules. Bonell objected that in many cases it might not be clear what is infringed. Goode argued that anybody applying the rules anyway has to decide what has been infringed: principles or mandatory law.

53. Then again the structure of the chapter was discussed. Anybody who applies the rules needs to now that the first tier is split up into Art. 1 and Art. 3 and that the second tier is split up in Art. 2 and Art. 4, Art. 1 and Art. 2 being the definitions and Art. 3 and Art. 4 dealing

with the effects. Goode suggested as title for Art. 3: “Effects of Article Illegality under Article 1”. However, Goode and Bonell both thought that the reference to Art. 1 should not be restricted to the title. It has to be made clear in the text of the article, too. Goode was in favour of making a first paragraph to this effect. Bonell favoured a clarification only in the first sentence of Art. 3. Zimmermann suggested that Art. 3 could be paragraphs 3 and 4 off Art. 1. Another idea was to make it clearer through new titles. The title of Art. 1 should be: “Contracts contrary to fundamental principles” and the title of Art. 2: “Contracts infringing mandatory rules”. Finally, the agreement was reached to keep these titles but to restructure the chapter. The effects should be dealt with immediately following the definition. Thus following structure follows:

Art. 1: “Contracts contrary to fundamental principles“,  
Art. 2: “Effects of Illegality under Article 1”,  
Art. 3: “Contracts infringing mandatory rules”, and  
Art. 4: “Effects of contracts infringing mandatory rules”.

54. An agreement was reached that both in Art. 2 and in Art. 4 there should be further clarification that the article only applies to the exactly preceding article. Following formulations were agreed upon:

Art. 2(1): “This Article applies to illegality under Article 1.”  
Art. 4 (1): “This Article applies to contracts illegal under Article 3.”

55. It was then discussed whether one could use Art. 2 as a model for Art. 4. Furmston objected that it cannot be a model because the presumption is differently in Art. 4. The following text was finally agreed upon. Art. 4(4) is based on Art. 15:102(3) PECL:

“Art. 4: Effects of contracts infringing mandatory rules.  
(1) This Article applies to contracts illegal under Article 3.  
(2) The effects of any infringement of a mandatory rule upon a contract are those expressly prescribed by that rule.  
(3) Where the mandatory rule does not expressly prescribe the effects of an infringement upon a contract, the parties have the right to exercise such remedies as in all the circumstances are reasonable.  
(4) In determining what is reasonable regard is to be had in particular to:  
(a) the purpose of the rule which has been infringed;  
(b) the category of persons for whose protection the rule exists;  
(c) any sanction that may be imposed under the rule infringed;  
(d) the seriousness of the infringement;  
(e) whether the infringement was intentional; and  
(f) the closeness of the relationship between the infringement and the contract.”

56. The discussion finally turned to the question of restitution. The question was again put forward whether the general restitutionary rules are fit to be also applied in the present case. Furmston clarified that two questions need to be separated: firstly, when should restitution be granted? Furmston favoured a flexible approach. The second question is whether an extra set of rules is needed. Bonell suggested to concentrate for the time being on the first question. Art. 5(1) should state a general rule. Zimmermann reminded that yesterday

it had only been briefly discussed what the general rule should be and whether the general rule should be against restitution. He thought that with regards to mandatory rules the general rule could be in favour of restitution. But he recalled that an agreement was reached with Goode that due to the nature of the mandatory rules that apply under Art. 1.4 PICC the general rule should be against restitution.

57. The group discussed the problem of the interrelation between the remedies: If remedies are given although the contract is illegal, no restitution is necessary. But what about the case if only damages is available as remedy under the contract? Is restitution available? Goode expressed the view that it is not inconsistent to grant damages under the contract and restitution. The group agreed on the following general rule:

Art. 5(1): “Where there has been performance under an illegal contract restitution is excluded unless that would lead to unreasonable results.”

58. As regards to how restitution should be rendered it was discussed whether restitution is always concurrent. Zimmermann pointed out that this would be the case under the general restitutionary rules. The group agreed on the following paragraph:

Art. 5(2): “Where restitution is granted it may take the form of return of property, the repayment of money, or payment of an allowances for property transferred or services supplied, whichever is appropriate.”

# Appendix

## Present state of the Draft Chapter

### Article 1

#### *Contracts contrary to fundamental principles*

- (1) A contract is illegal if, whether by its terms, performance or otherwise, it is contrary to principles widely accepted as fundamental in legal system throughout the world.**
- (2) If only part of the contract is illegal under Article 1 the entire contract is illegal unless giving due consideration to all the circumstances of the case it is reasonable to hold otherwise.**

For agreed changes in the text, the comments and the examples, see No. 2, 10-12, 16-18, 39-40, 42, 49, 53 of the minutes.

### Article 2

#### *Effects of Illegality under Article 1*

- (1) This Article applies to illegality under Article 1.**
- (2) Where each party knows, or ought to have known, of facts which make the contract illegal under Article 1, neither party has the right to exercise remedies under the contract.**
- (3) Where one party neither knew nor ought to have known of facts which make the contracts illegal under Article 1 it has the right to exercise such remedies as in all the circumstances are reasonable.**

For agreed changes in the text, the comments and the examples, see No. 20-31, 50-54 of the minutes.

### Article 3

#### *Contracts infringing mandatory rules*

- (1) A contract, whether by its terms, performance or otherwise, is also illegal if it infringes a mandatory rule applicable under Art. 1.4 under these Principles.”**
- (2) If only part of the contract is illegal under Article 2 the remaining part is not illegal unless giving due consideration to all the circumstances of the case it is reasonable to hold otherwise.**

For discussion as to the purpose and application of this rule, its relation to Art. 1.4, see No. 5-8, 38, 41-44, 46-49, 53 of the minutes.



## **Article 4**

### *Effects of contracts infringing mandatory rules*

- (1) This Article applies to contracts illegal under Article 3.**
- (2) The effects of any infringement of a mandatory rule upon a contract are those expressly prescribed by that rule.**
- (3) Where the mandatory rule does not expressly prescribe the effects of an infringement upon a contract, the parties have the right to exercise such remedies as in all the circumstances are reasonable.**
- (4) In determining what is reasonable regard is to be had in particular to:**
  - (a) the purpose of the rule which has been infringed;**
  - (b) the category of persons for whose protection the rule exists;**
  - (c) any sanction that may be imposed under the rule infringed;**
  - (d) the seriousness of the infringement;**
  - (e) whether the infringement was intentional; and**
  - (f) the closeness of the relationship between the infringement and the contract.**

For agreed changes in the text, the comments and the examples, see No. 20, 24-31, 50-55 of the minutes.

## **Article 5**

### *Restitution*

- (1) Where there has been performance under an illegal contract restitution is excluded unless that would lead to unreasonable results.**
- (2) Where restitution is granted it may take the form of return of property, the repayment of money, or payment of an allowances for property transferred or services supplied, whichever is appropriate.**

For agreed changes in the text, the comments and the examples, see No. 32-36, 56-58 of the minutes.