



INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW
INSTITUT INTERNATIONAL POUR L'UNIFICATION DU DROIT PRIVE

**Principles of International Commercial Contracts
Working Group on Long-Term Contracts**

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Contracts with evolving terms ^(*)

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(*) Cf. Study L – Doc. 127, Issue (d).

ARTICLE 4.3*(Relevant circumstances)*

In applying Articles 4.1 and 4.2, regard shall be had to all the circumstances, including

- (a) preliminary negotiations between the parties;**
- (b) practices which the parties have established between themselves;**
- (c) the conduct of the parties subsequent to the conclusion of the contract;**
- (d) the nature and purpose of the contract;**
- (e) the meaning commonly given to terms and expressions in the trade concerned;**
- (f) usages.**

COMMENT**1. Circumstances relevant in the interpretation process**

[...]

2. “Particular” and “general” circumstances compared

[...]

~~3. “Merger” clauses~~**3. Practices established between parties and conduct subsequent to the conclusion of the contract relevant particularly in interpretation of long-term contracts**

Conduct subsequent to the conclusion of the contract can assist in determining what the parties intended their obligations to be. This may be the case particularly in the context of long-term contracts, which often involve complex performance and are “evolutionary” in nature, i.e. may require adaptations in the course of performance. Such contracts may involve repeated performance by one party with the opportunity for the other to assert that such performance does not conform to the contract.

As a rule the subsequent conduct of the parties can only be an interpretative tool, i.e. be used to explain or amplify, but not to contradict, the terms of the contract as originally agreed between the parties.

Illustrations

5. Supplier A enters into a five-year contract with Shopping Mall B to supply B’s need for “salt” to clear ice in its parking lot and on its sidewalks. For the first two winters, Supplier A provides an ice-melting substance which is not a “salt,” with no objection being raised by B. At the start of the next winter, B objects that the substance is not a “salt” as stated in the contract. The fact that for two winters both A and B performed as though the supplied substance satisfied the contract permits the inference that the parties intended the contract’s reference to “salt” to include such an ice-melting substance.

6. Contractor A agrees to provide Client B with concrete slabs of a particular thickness in a building at a unit price of X without specifying whether that price applies to a square metre of those slabs or cubic metres of concrete. The parties perform over several months without any objection as though the unit price applied to square metres of slabs. A dispute subsequently arises

regarding the proper unit of measure. The fact that for several months A and B had performed as though the proper unit of measure was square metres of slabs permits the inference that the parties intended that to be the proper unit of measure.

To avoid any uncertainty as to the effects of subsequent conduct on the content of the contract, the parties may wish to adopt particular mechanisms for possible variations and adjustments of the contract in the course of performance. They may, for instance, provide for the issuance of “variation orders” by one party for acceptance by the other party (e.g. in construction contracts the “Employer’s Representative” and the “Contractor’s Representative”, respectively), or establish special bodies composed of representatives of both parties or of independent experts (so-called “contract management committees”, “auditing bodies” or the like), with the task of monitoring both parties’ performance and possibly also of suggesting adjustments to the contract so as to bring it in line with developments. Obviously, the more precisely the parties regulate the procedure for adjustments to the contract, the less relevant any informal conduct of the parties would be to the interpretation of the contract.

Illustrations

7. A construction contract between Employer A and Contractor B provides that A’s “Representative” has the authority to give instructions regarding additions, omissions or other changes in work to be performed by B. So long as those additions, omissions or other changes fall within the overall scope of work under the contract, B will be bound to perform them and they will have the effect of changing the relevant work provided for in the original contract.

8. Contractor A enters into a Design, Build and Operate (DBO) contract with Company B to design and build a factory and operate it for twenty years. The contract provides for the parties to appoint jointly an independent and impartial Auditing Body whose purpose is to audit and monitor the compliance of each of the parties with the operation management requirements set out in the contract. The contract may also provide that, if the Auditing Body determines that a party has failed to comply, that party must take appropriate corrective action. Therefore, if in a given case the Auditing Body determines that A has not complied with its obligations under the contract, A is bound to take the appropriate action.

4. “Merger” and “No oral modification” clauses

Parties to international commercial transactions in general, and to complex long-term contracts in particular, frequently include a provision indicating that the contract document completely embodies the terms on which they have agreed. ~~For the effect of these so-called “merger” or “integration”~~ (so-called “merger” or “entire agreement” clauses) and that any modification to the contract or specific terms of it must be made in writing (so-called “no oral modification clauses”). For the effect of the former type of clauses, in particular whether and to what extent they exclude the relevance of preliminary negotiations between the parties, albeit only for the purpose of the interpretation of the contract, see Article 2.1.17. As to the latter type of clauses, see Article 2.1.18, and the limitation of the rule therein contained by virtue of the principle of prohibition of inconsistent behaviour laid down in Article 1.8.

Illustration

9. Manufacturer A enters into an agreement with Distributor B for the distribution of its products in country X. The agreement expressly states that the distributorship is non-exclusive and, in fact, in country X A's products are distributed also by Distributor C. The agreement between A and B also contains a "no-oral modification" clause according to which any modification of its terms has to be in writing and approved by A's parent company. Subsequently C ceases its activity and B acts, to A's knowledge, as though it has become the exclusive distributor of A's products in country X by, among others things, holding itself out as such to C's clients, without any reaction on the part of A. When A replaces C with a new distributor, B may not object that by their conduct A and B have modified their original agreement, turning it into an exclusive agreement.