

Newsletter No. 119 (EN)

**Comparison of commonly used
Hardship and Force Majeure Clauses**

May 2017

Although Lorenz & Partners always pays great attention on updating information provided in newsletters and brochures we cannot take responsibility for the completeness, correctness or quality of the information provided. None of the information contained in this newsletter is meant to replace a personal consultation with a qualified lawyer. Liability claims regarding damage caused by the use or disuse of any information provided, including any kind of information which is incomplete or incorrect, will therefore be rejected, if not generated deliberately or grossly negligent.

1. Introduction

When drafting international contracts, a matter of particular concern should be to focus on unforeseen circumstances, which might lead to substantial problems. Questions may arise, such as:

- Who will be responsible, if e.g. a ship with urgent cargo for a construction site was damaged by a heavy storm and the cargo is lost?
- Who is responsible for the delays in completing the construction work and substantial penalties that might appear?

In legal terms, this refers to Force Majeure and Hardship. **Force Majeure**, on the one hand, applies to cases where performance has become (temporarily) impossible due to an event beyond one party's control even though all reasonable precaution measures had been taken. **Hardship**, on the other hand, deals with cases where the agreed performance is basically still possible. However, the underlying facts have substantially changed so that fulfilling the agreement would be economically detrimental.

It is important to be aware that Force Majeure and Hardship are two different principles, even if they sometimes are treated as the same. They are different in their preconditions, and in their legal consequences. To apply **Force Majeure** to a case, the legal obligations of a party must become impossible for anybody due to circumstances that nobody can avoid (*such as earthquakes or lightning*). Such circumstances are principally known to the public, but nobody is able to predict where and when they will arise. For this, the English translation for Force Majeure is an "**Act of God**", which makes it clear that nobody is able to influence these circumstances.

Hardship, in contrary, is based on the fact that the underlying circumstances of the contract change in a way which the parties did not foresee at the time when concluding the contract, and the change of the underlying circumstances is due to economic influences.

Furthermore, the legal consequences of both doctrines are very different. Consequence of **Force Majeure** is that one party cannot fulfil its contractual obligations anymore (*impossibility*). The legal consequence of **Hardship** is that the party, for which the underlying circumstances did change substantially, can basically still fulfil its contractual obligations and perform the contract, but the performance became economically worthless. Depending on the contractual agreement between the parties, the material law and/or the agreed legal consequences with regards to Force Majeure / Hardship, the contract might be adjusted to the changed circumstances automatically, or the parties will renegotiate the contractual details which are affected by the changed circumstances (*most likely be the purchase price*).

Under German law, the basic principle "*pacta sunt servanda*" states that once a contract has been entered, the contracting parties are obliged to fulfil their obligations, no matter if circumstances change later. The legal concepts called "*economic impossibility*" or "*frustration*" are, in general, no reason for not performing a contractual obligation.

Such principles, however, cannot be simply transferred to international law. E.g., the United Nations Convention on Contracts for the International Sale of Goods ("**CISG**") or the principles of the International Institute for the Unification of private law ("**UNIDROIT**") or the rules of the International Chamber of Commerce ("**ICC**"), all contain provisions

dealing particularly with Force Majeure and Hardship.

Apart from that, there are various other contract terms issued by renowned international associations, such as the Fédération Internationale Des Ingenieurs-Conseils (“**FIDIC**”), which include e.g. a particular Force Majeure Clause. It has to be noted that the FIDIC terms focus on contracts concerning construction and engineering projects.

The CISG contains a Force Majeure Clause; however, it does not contain any rules on Hardship. In a landmark decision, the Belgian Supreme Court (19 June 2009, case number: C.07.0289.N), therefore, applied the UNIDROIT principles to close this loophole in the CISG, although UNIDROIT principles were not agreed between the parties.

Since the consequence of this judgement could be extensive, this newsletter provides an overview on the different Force Majeure and Hardship Clauses that are available under international commercial law.

2. Force Majeure Clauses

2.1 Definition

Force Majeure is French and stands for higher force. Force Majeure means unavoidable events such as natural disasters of all kinds, especially storms, earthquakes, flood, volcanic eruption, but also fire, traffic accidents, kidnappings, wars, riots, revolution, terrorism, sabotage and strike. Force Majeure regularly requires an unexpected occurrence of those events. However, a Force Majeure event has to be denied if the parties must consider such incident to happen, e.g. floods that occur repeatedly in the same region or fires in dry countries, and one party neglected to take the respective precautions. A Force Majeure event, therefore, could be generally described as an event that affects the contractual relationship unpredictably from the outside and that, despite the parties taking extreme care, was not avoidable.

2.2 Spirit and Purpose

The question remains who is responsible for the non-performance of the contract due to the Force Majeure event. In order to avoid disputes and risks of interpretation, Force Majeure Clauses have been included in a great number of international commercial sources of law to essentially dispense both parties from liability or their obligations when an extraordinary event or circumstance beyond the control of the parties occurs. The occurrence of a Force Majeure event leads to the – *at least temporary* – suspension of the primary obligations of both contracting parties. Either party has to bear the adverse consequences of non-performance or the delay in performance. As a consequence, the liability dispenses and the other party is unable to claim compensation for damages or the like.

3. Hardship

3.1 Definition

In case of Hardship, the performance of the contract is not impossible, but merely hindered. Hardship is defined as any event of legal, technical, political or financial nature occurring after the conclusion of the contract, which was unforeseeable at the time the contract had been formed, despite using the utmost care. In general, Hardship does not cause the impossibility of performance, but allows for renegotiation of the contract.

3.2 Spirit and Purpose

Hardship clauses typically recognise that parties must perform their contractual obligations even if events will render performance more difficult than one would reasonably have anticipated at the time of the conclusion of the contract. However, where continued performance has become excessively burdensome due to an event beyond a party’s reasonable control, a Hardship clause can oblige the parties to negotiate alternative contractual terms. The purpose of a Hardship clause is to provide a higher level

of flexibility and to balance the risk between the parties.

The principle of Hardship is particularly influenced by the Common Law and the Equitable Rights of the Anglo-American legal system, to find a balance under the principle of equity and good faith.

4. The Different Bodies of Rules and Regulations

4.1 CISG

CISG is a treaty offering a uniform international sales law that, as of May 2016, has been ratified by 85 countries. This makes the CISG one of the most successful international uniform laws.

CISG is directly applicable to contracts for the sale of goods between parties whose places of business are in different member states (Art. 1(1)(a) CISG). CISG is also applicable in case only one of the parties is a resident in a CISG member state but the contract between the parties refers to the material law of this state (Art. 1(1)(b) CISG). Even if neither party is resident of a member state, CISG can be applicable when the parties expressly agree on its application for their legal relationship. CISG defines its own territorial criteria of application without the need to resort the rules of private international law. For sales contracts concluded prior to the ratification of the CISG, Article 100(2) CISG applies:

“This Convention applies only to contracts concluded on or after the date when the Convention enters into force in respect of the Contracting States referred to in subparagraph (1)(a) or the Contracting State referred to in subparagraph (1)(b) of article 1.”

4.2 ICC Force Majeure Clause 2003 (ICC Publication No. 650)

The ICC is the largest, most representative business organisation in the world. Objective of the ICC is to promote international trade and to support international businesses to face

challenges and opportunities of globalisation. By issuing contract rules, an efficient settlement of international transactions is promoted.

4.3 The UNIDROIT Principles

UNIDROIT is an independent intergovernmental organisation. Its purpose is to study needs and develop methods for modernising, harmonising, and coordinating private international law and in particular commercial law between states, and to draft international regulations to address the needs of the members. Membership of UNIDROIT is restricted to states adhering to the UNIDROIT Statute. UNIDROIT’s currently 63 member states represent a variety of different legal, economic, and political systems as well as different cultural backgrounds.

4.4 The FIDIC Rules

FIDIC, the International Federation of Consulting Engineers, represents members of the engineering industry. As such, FIDIC promotes the interests of the construction and engineering industry. Founded in 1913, FIDIC today numbers 75 Member Associations representing approx. 1 million professionals. FIDIC also publishes international contract samples and business practice documents.

4.5 The BGB

The German Civil Code (*Bürgerliches Gesetzbuch* “BGB”) came into force on 01 January 1900, and was considered a massive and groundbreaking project after having been developed since 1874. The BGB is based on Roman law. Like other Roman-influenced codes, it regulates the law of persons, obligations, property, family and inheritance, and, unlike e.g. the French Code Civil or the Austrian Civil Code, a chapter containing generally applicable regulations is placed first.

5. Force Majeure in Law

5.1 Force Majeure in German Law

The term “Force Majeure” (“*höhere Gewalt*”) occurs in the BGB in §§ 651a et seq., which regulate the Travel Law. But nevertheless the idea of Force Majeure is also accepted in the law of obligations in § 275(1)-(3), § 326(1), (5) and §§ 323 et seq. BGB.

Example:

A vendor and a purchaser conclude a contract on the delivery of 5 tons of rice. The vendor sorts out those 5 tons and stores them in another warehouse ready for delivery. Due to a storm the warehouse and the rice are destroyed during the night.

Solution:

The rice is destroyed because of the storm. This is an unavoidable event of superior power which the parties could not have foreseen at the time of the conclusion of the contract. As the vendor already finished the ascertainment of goods by sorting out the rice and storing it in another warehouse, the performance of the delivery of exactly these 5 tons of rice is now impossible for the vendor and everyone else, § 275(1) BGB. On the one hand, the right of the purchaser to demand delivery is barred by this, § 275(1) BGB. On the other hand, the vendor cannot claim consideration, § 326(1) BGB. The purchaser has the opportunity to withdraw from the contract, § 326(5) BGB, without having to set a time limit. Thus, the performances exchanged have to be returned, e.g. the deposit the purchaser had to pay.

5.2 Force Majeure in the CISG

The CISG contains a written Force Majeure clause in Art. 79 CISG. According to the first paragraph, a party is not liable for failure to perform any of its obligations if it proves that the failure was due to an impediment beyond the party’s control and that such party could not reasonably be expected to have taken the

impediment into account at the time of the conclusion of the contract or to have avoided or overcome it or its consequences. If a party is able to prove these requirements, it is relieved from its liability of performance and the other party cannot claim any further rights.

5.3 ICC Force Majeure Clause 2003

§ 1 of the ICC Force Majeure clause states that in order to be considered Force Majeure, there must be an impediment due to failure, which is similar to Art. 79 CISG. § 2 is designed specifically on the basis of CISG article 79(2) and is intended to make it clear that a contracting party can invoke the clause where a party fails to perform its duties towards its contracting party because of non-performance of a third party. § 3 of the ICC Force Majeure clause provides a list of force majeure events, which includes e.g. war, explosions, natural disaster, strikes, etc. As a legal consequence, the party who fails to perform and claims Force Majeure will be relieved from liability without having to face any claims of the forfeiting party and the other party is released from their obligations as well.

5.4 Force Majeure in the UNIDROIT Principles

The UNIDROIT Principles of International Commercial Contracts 2010 contain a Force Majeure Clause in Art. 7.1.7. This rule excuses non-performance by a party if that party proves that the failure was due to an impediment beyond its control and that it could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract or to have avoided or overcome it or its consequences. The article does not restrict the rights of the party who has not received performance to terminate if the non-performance is fundamental. Where applicable, it states to exclude the non-performing party from liability in damages. In some cases, the impediment will prevent any performance at all but in many others it will simply postpone performance.

5.5 Force Majeure in the FIDIC Contract Samples

The “Red Book” (concerning construction contracts), the “Yellow Book” (concerning contracts on plants and their design) and the “Silver Book” (concerning EPC (*Engineering, Procurement and Construction*) contracts) all contain a Force Majeure Clause in their Art. 19. The Clause is a combination of a new provision for defined events of force majeure, and a new wording of a provision covering impossibility (or illegality) of performance. Clause 19.1. defines Force Majeure as an event beyond the control of the Employer and the Contractor, which makes it impossible or illegal for a party to perform, including but not limited to e.g. war, hostilities, rebellion, contamination by radio-activity from any nuclear fuel or riot.

6. Hardship in Law

6.1 Hardship in German Law

The BGB contains a hardship clause in § 313(1) BGB. Since the reform of the law of obligations in 2002, the doctrine of frustration has been included in § 313 BGB. This provision states that a contract has to be renegotiated if an event occurs which fundamentally alters the present contract and places an excessive burden on one of the party’s performance making the adherence to the contract unreasonable. In case renegotiation is impossible, the disadvantaged party can withdraw from the contract. The hardship clause in § 313(1) BGB results from the ideas of good faith in § 242 BGB and restricts the basic principle “*pacta sunt servanda*”.

6.2 Hardship in CISG

The CISG does not contain a Hardship clause, and the prevailing opinion is that Art. 79 CISG does not cover Hardship. Renegotiation is therefore not an option.

6.3 ICC Hardship Clause 2003

Paragraph 1 of the ICC Hardship clause recognises that parties must perform their contractual obligations even if “*events have rendered performance more onerous than would reasonably have been anticipated at the time of the conclusion of the contract.*” However, according to paragraph 2, where continued performance has “*become excessively onerous due to an event beyond a party’s reasonable control which it could not reasonably have been expected to have taken into account,*” the clause requires the parties to “*negotiate alternative contractual terms which reasonably allow for the consequences of the event.*” According to paragraph 3, the party invoking the Hardship clause is entitled to terminate the contract in case alternative contract terms cannot be agreed upon.

6.4 Hardship in the UNIDROIT Principles

Art. 6.2.2 of the UNIDROIT Principles of International Commercial Contracts 2010 defines hardship as a situation where the occurrence of events fundamentally alters the contract, provided that those events meet the requirements which are laid down in subparagraphs. This also shows that Art. 6.2.2 is not exhaustive but has to be adjusted by the parties to fit their needs. Under the UNIDROIT Principles of International Commercial Contracts 2010, Hardship has effects both in procedural and material law (Art. 6.2.3). The disadvantaged party can request renegotiation. If this party fails to do so, it does not lose this right. However, this failure may affect the finding as to whether Hardship actually existed. If the parties fail to reach agreement on how to amend the contract according to the changed circumstances within a reasonable time, Art. 6.2.3(3) authorises either party to resort to the court. Paragraph 4 provides legal consequences (termination/contract adaptation) for the court to deliver judgement in these cases.

6.5 Hardship in the FIDIC Contract Samples

The major FIDIC contract samples do not contain Hardship Clauses. In large projects, where the performance of the parties' contractual obligations is spread over several years, the parties might thus consider to add a Hardship clause to the contract to stipulate when and how the parties will rearrange the contractual terms in the event the contract loses its economic balance.

7. Similarities and Differences of the Different Clauses

7.1 Force Majeure

7.1.1 Similarities

All of the above rules and regulations have in common that the binding character of a contract is not an absolute one; hence, an exemption might be possible. Nevertheless, all regulations point out strictly that such exemption can only be granted in exceptional cases. All clauses require an impediment which is due to the failure and the party who cannot perform has to prove that the impediment was beyond its control and not foreseeable.

7.1.2 Differences

The ICC does not point out the consequences of a third person's failure. Art. 19.1 FIDIC defines Force Majeure rather broad compared to the other regulations, as it states that the event or circumstances must be "exceptional". The event must be beyond the parties' control and the parties could not have reasonably been provided for such event before the contract was made. The event cannot be attributed to one of the parties. Art. 79(2) CISG contains a regulation in case a party's inability to perform is due to the failure of a third party, whom it has engaged for parts of the performance. Thus, the possibility of exculpation exists.

Furthermore, Art. 79 CISG does not contain an enumeration of possible impediments, so this article's field of application is not as narrow as the one of paragraph 1 of the ICC Hardship Clause.

Neither the FIDIC contract samples, nor the UNIDROIT Principles in Art. 7.1.7, envisage the possibility of exculpation by a third person's failure. The UNIDROIT article does also not contain an enumeration of possible impediments; therefore, it has to be understood wider than the definition of impediments in the ICC. Unlike the other regulations, Art. 19 FIDIC contains a more specified variety in its legal consequences, and their application has to be proved carefully.

7.2 Hardship

7.2.1 Similarities

There are no similarities between the existing Hardship clauses in § 313 BGB, ICC and UNIDROIT Principles.

7.2.2 Differences

The UNIDROIT principles contain a written Hardship clause in Art. 6.2.2, and the ICC contains a definition in paragraph 1 of its Hardship Clause. The CISG and the FIDIC contract terms do not contain similar clauses. The ICC does not set out the provisions of hardship in a standard clause so that a hardship clause has to be inserted by the parties if necessary. Instead, the ICC provides four alternatives relating to the effects of hardship the parties can adopt. The UNIDROIT Principles define Hardship as a situation where the occurrence of events fundamentally alters the equilibrium of the contract, provided that those events meet the requirements which are laid down in subparagraphs. This also shows that Hardship under UNIDROIT is not exhaustive but has to be adjusted by the parties to fit their needs.

8. Reviewing the Decision of the Belgian Supreme Court of 19 June 2009

8.1 Facts of the Case

A French vendor and a Dutch purchaser entered into successive contracts for the sale and the delivery of steel tubes to Belgium. In early 2004, after facing a 70% increase in the market price of steel, the vendor asked for the contract to be renegotiated due to the increased raw material price. As they could not reach a satisfying agreement, the case went to court.

8.2 Facts of the Decision

The Supreme Court ruled that circumstances which were not reasonably foreseeable at the time of the conclusion of an agreement and which increase the burden of the agreement disproportionately can, under certain circumstances, be considered an “impediment” within the meaning of Art. 79 CISG. The Belgian Supreme Court further held that Art. 79 CISG can govern Hardship. As this article contains no indication how to resolve Hardship, it relied on Art. 7(1), (2) CISG to bridge the gap. Since Art. 7 CISG is a good faith clause, interpretation is accessible and the resolving of Hardship issues can be adapted on the individual needs. To interpret the definition of Hardship, the Supreme Court used the UNIDROIT regulations to apply Hardship to that case, despite the fact

that the parties never agreed to apply UNIDROIT to their contract.

8.3 Causes of this Ruling

As the CISG does not give any indication how to solve Hardship, the court had to access the UNIDROIT Principles to come to a just decision. However, it has to be noted that the Court applied the UNIDROIT Principles without them being agreed between the parties.

9. Conclusion

The aforementioned rules and regulations are just examples for the variety of regulations available to deal with Force Majeure and Hardship events. Due to this, the parties have to take a closer look at what they believe is necessary to be regulated in the contract itself. Different contracts need different clauses on diverse grounds. There needs to be an evaluation what exact purpose the clause shall serve in the individual case.

It has to be mentioned that all the existing Hardship clauses are quite soft, so that there might be a right of renegotiation even if the change in the circumstances is less than 70%. Hence, concerning Hardship, it might be recommendable to apply the UNIDROIT Principles with the provision that a fundamental change of circumstances is only given if the diversification reaches 100%.

*We hope that the information provided in this newsletter was helpful for you.
If you have any further questions please do not hesitate to contact us.*

LORENZ & PARTNERS Co., Ltd.

27th Floor Bangkok City Tower
179 South Sathorn Road, Bangkok 10120, Thailand
Tel.: +66 (0) 2-287 1882
E-Mail: info@lorenz-partners.com

	BGB	ICC Rules Publication No. 650, 2003	CISG Rules	UNIDROITS Prin- ciples	FIDIC Rules of the Major Works
1. Force Majeure:	§§ 326(1), (5), 275(1)-(3) BGB	§ 1 ICC Force Majeure Clause 2003	Art. 79 CISG	Art. 7.1.7	Art. 19 FIDIC
Basic Principle:	Pacta sunt servanda as an influence of the Roman Law	Rather be fair as an in- fluence of the Common Law System	Influenced by Com- mon Law, based on precedents rather than statute law	Affected by Common Law aiming to be fair and equitable	Drafted with a Com- mon Law background following laws based on previous rulings
Requirements:	<ul style="list-style-type: none"> ○ Impossibility of per- formance § 275(1) BGB for liable party or everyone or ○ Refuse of perform- ance because of mal- adjustment to equiva- lent, § 275(2) BGB, or ○ Refuse of perform- ance in case of duty to perform in person if performance is unac- ceptable 	<ul style="list-style-type: none"> ○ Impediment, beyond party’s control ○ Enumeration of events not being ex- haustive in para. 2 ○ Not reasonably fore- seeable at the time of the conclusion ○ Impediment was not reasonably avoidable ○ Duty of notification 	<ul style="list-style-type: none"> ○ Failure due to an impediment be- yond a party’s control ○ Not reasonably foreseeable at the time of the con- clusion ○ Impediment or consequences were unavoidable ○ Party who fails must give notice 	<ul style="list-style-type: none"> ○ Non-performance due to an impedi- ment beyond a party’s control ○ Not reasonably foreseeable at the time of the conclu- sion ○ Impediment or consequences were unavoidable ○ Party must give notice 	<ul style="list-style-type: none"> ○ Event beyond con- trol of Employer or Contractor ○ Which makes it im- possible or illegal for a party to per- form ○ Enumeration in Art. 19.1 not being ex- haustive

	BGB	ICC Rules	CISG Rules	UNIDROITS Prin-	FIDIC Rules of the
--	------------	------------------	-------------------	------------------------	---------------------------

		Publication No. 650, 2003		principles	major works
Legal Consequences:	<ul style="list-style-type: none"> ○ Claim of equivalent is dispensed. Relief from liability ○ § 326(1) BGB: Option for disappointed party: Rescission of the contract § 326(5), 323(1) BGB, but benefits have to be returned, § 346(1) BGB 	<ul style="list-style-type: none"> ○ Relief from liability, no further rights for disappointed party 	<ul style="list-style-type: none"> ○ Relief from liability, no further rights for disappointed party 	<ul style="list-style-type: none"> ○ Relief from liability, no further rights for disappointed party 	<ul style="list-style-type: none"> ○ Payment to Contractor if work suffers loss or damage, Art. 19.5 FIDIC ○ Optional Termination if the effects of force majeure continue for a period of 182 days, Art. 19.6 FIDIC ○ In case of termination, payment has to be carried out according to the value of the work done, Art. 19.6 FIDIC ○ Same Payment has to be made, if performance is released due to law of the contract

	BGB	ICC Rules, Publications No. 650, 2003	CISG Rules	UNIDROITS Principles	FIDIC Rules of the major works
2. Hardship:	§ 313(1), (3) BGB	Hardship Clause of 2003	No written Clause	Art. 6.2.2	No written Clause
Basic Principle:	Pacta sunt servanda as an influence of the Roman Law	Rather be fair as an influence of the Common Law System	Influenced by Common Law, based on precedents rather than statute law	Affected by Common Law aiming to be fair and equitable	Drafted with a Common Law background following laws based on previous rulings
Requirements:	<ul style="list-style-type: none"> ○ Circumstances that concern the contractual basis ○ Changed onerously after the conclusion of the contract ○ Parties would not have contracted if they had foreseen these changes 	<ul style="list-style-type: none"> ○ Continued performance of contractual duties has become excessively onerous due to an event beyond parties' control ○ Not reasonably foreseeable at the time of the conclusion ○ Could not reasonably have avoided the event or its consequences 	None	<ul style="list-style-type: none"> ○ Occurrence of events fundamentally altering the equilibrium of the contract ○ Either because the costs of the performance have increased ○ Or because the value of the performance a party receives has diminished ○ Events occur after conclusion ○ Not foreseeable ○ Events are beyond parties control 	None

				○ The risk of event was not assumed by disadvantaged party	
Legal Consequences:	§ 313(1) BGB: Adjustment of the Contract; if adjustment is not possible, disadvantaged party can resign from contract, § 313(3) BGB	Disadvantaged party can demand renegotiation	Non existent	Disadvantaged party can demand renegotiation	Non existent