"(*b*) The right of the Employer to execute the Works or any part thereof on, over, under, in or through any land.

"(*c*) Injuries or damage to persons or property which are the unavoidable result of the execution or maintenance of the Works in accordance with the Contract.

"(*d*) Injuries or damage to persons or property resulting from any act or neglect of the Employer, his agents, servants or other contractors, not being employed by the Contractor, or for or in respect of any claims, proceedings, damages, costs, charges and expenses in respect thereof or in relation thereto or where the injury or damage was contributed to by the Contractor, his servants or agents such part of the compensation as may be just and equitable having regard to the extent of the responsibility of the Employer, his servants or agents or other contractors for the damage or injury.

[A/CN.9/WG.V/WP.4/Add.5*]

XIII. Exoneration

A. *Introduction*

1. Most, if not all, legal systems make provision for unforeseen or unavoidable circumstances which prevent, impede or delay the performance of a contract. The nature and scope of such circumstances affecting a contract differ in varying degrees among different legal systems. The two main doctrines that have been evolved to deal with such circumstances are *force majeure* and frustration, though the former doctrine may mean different things in different legal systems.

2. Parties often insert "*force majeure*" or "frustration" clauses either to expand or narrow the scope of the two doctrines. In such clauses, parties may also allocate their risks in a more precise manner taking into consideration the nature of the performance of the particular contract.

3. In this study, the term "exoneration" is used to cover circumstances relieving parties from liability. Although the circumstances under discussion may straddle the doctrines of *force majeure* or frustration the term "exoneration" is used to avoid confusion, as there may be events under consideration which do not fall within the scope of either one or the other of the two doctrines as understood in the various legal systems. However, the terms "*force majeure*", "frustration" and other epithets will be used where clauses under discussion are taken from contexts which employ these terms.

4. An exoneration clause constitutes one of the most important clauses in a works contract; it deals essentially with the allocation of risks in the event of changed circumstances. Such a clause could save the contract from automatic termination which may be too drastic and may not be to the mutual interests of both parties. At a regional level, attempts at drafting "relief" clauses for use in contracts for the supply and erection of plant and machinery have been made, for example, by ECE. The ECE General Conditions are designed for application in different legal systems. At a global level, the "Exemptions" provision in the Sales Convention provides an example of success in the harmonization of this area of law in the context of sale of goods. Parties to works contracts have also attempted to modify the doctrines of *force majeure* and frustration in order to determine the kinds of contingency that would suspend or terminate their obligations and also the consequences of such suspension or termination.

B. *Exonerating circumstances*

1. Force majeure *clauses in contractual stipulations*

5. An examination of some works contracts indicates a number of approaches:

(*a*) Reference is made to the applicable law of the contract with no attempt to extend or narrow its scope. For example, in one clause reference was made to "Articles 513 and 514 of the Civil Code".

(*b*) *Force majeure* clauses are defined generally by the parties but no attempt is made in spelling out the exonerating events. For example, one such clause reads: "Neither party hereto shall be liable for any failure or delay in performing any obligation hereunder (except the payment of any amount due hereunder) due to *causes which are reasonably beyond its control.*" This clause is from one of the contracts to be performed in Trinidad and Tobago. The clause is to be read with the applicable law of the contract.

(*c*) Some *force majeure* clauses attempt to list, in varying details, the exonerating circumstances. But most are only illustrative of the scope and leave the question to be determined by the judge or arbitrator. Other clauses attempt a more comprehensive, though not exhaustive, list and end with a general clause, as for example, that it is ". . . without prejudice to the generality, any other circumstance or occurrence beyond the reasonable control of the sellers."

6. The following criteria were found in the definition of "*force majeure*" or other such-like clauses but with varying combinations:

* 17 March 1981.

Unexpected circumstances

Foreseen but unavoidable event

Unforeseen event

Cause beyond the control of the parties

Prevented from fulfilling obligations

Unable to prevent despite exercise of reasonable care and due diligence

Event occurring after conclusion of contract

Event not due to fault of party.

7. Subject to variations as to scope and precision, the following are some exonerating circumstances found in *force majeure* clauses:

Natural disasters (e.g. lightning, earthquakes, storms, floods)

Political obstacles (e.g. acts of enemy, revolutions, riots, sabotage, embargoes, withdrawal of licences)

Economic obstacles (e.g. withdrawal of licences, embargoes, industrial disputes, strikes, lock-outs, industrial disturbances, shortage of labour, concerted acts of workmen)

Legal obstacles (e.g. acts of government)

Transport obstacles (e.g. delay of vessel, shipwreck)

Other obstacles (e.g. explosions, breakdown of machinery, accidents, theft).

2. *ECE 188A and ECE 574A*

8. Clause 25.1 of ECE 188A reads:

"The following shall be considered as cases of relief if they intervene after the formation of the Contract and impede its performance: industrial disputes and any other circumstances (e.g. fire, mobilization, requisition, embargo, currency restrictions, insurrection, shortage of transport, general shortage of materials and restrictions in the use of power) when such other circumstances are beyond the control of the parties."

9. Clause 25.1 of ECE 574A reads:

"Any circumstances beyond the control of the parties intervening after the formation of the Contract and impeding its reasonable performance shall be considered as cases of relief. For the purposes of this Clause circumstances not due to the fault of the party invoking them shall be deemed to be beyond the control of the parties."

10. The difference between ECE 188A and ECE 574A is that the former contains some specific references to the kinds of relief which fall within its scope. The enumeration under 188A is not exhaustive but only illustrative of some of the "reliefs" contemplated.

11. Under both clauses the circumstances must occur after the formation of the contract and must be beyond the control of the parties. There must be a nexus between the supervening circumstances and the performance of the contract. ECE 188A speaks of circumstances which "impede its performance" while ECE 574A, "impeding its *reasonable* performance". The epithet "reasonable" qualifying "performance" was thought sufficient to exclude strikes and industrial disputes which may impede performance, but may not be "reasonable", depending of course on the nature of the strike and industrial dispute.

3. *FIDIC-CEC*

12. A works contract would invariably involve some civil engineering works. The provision on "frustration" in FIDIC-CEC reads:

Clause 66: "If a war, or other circumstances outside the control of both parties, arises after the Contract is made so that either party is prevented from fulfilling his contractual obligations, or under the law governing the Contract, the parties are released from further performance, then the sum payable by the Employer to the Contractor in respect of the work executed shall be the same as that which would have been payable under Clause 65 hereof if the Contract had been terminated under the provisions of Clause 65 hereof."

13. Two categories of "frustration" are provided in the above clause: first, "circumstances outside the control of both parties" ("war" being an example) which prevent the fulfilling of contractual obligations; secondly, where the governing law releases the parties from further performance.

14. In addition, the FIDIC-CEC Conditions contain an enumeration of "special risks" in clause 65 (5). These risks may subsequently lead to the "frustration" of the contract within the meaning of clause 66:

"The special risks of war, hostilities (whether war be declared or not), invasion, act of foreign enemies, the nuclear and pressure waves risk described in Clause 20 (2) hereof, or insofar as it relates to the country in which the Works are being or are to be executed or maintained, rebellion, revolution, insurrection, military or usurped power, civil war, or unless solely restricted to the employees of the Contractor or of his Sub-Contractors and arising from the conduct of the Works, riot, commotion or disorder."

4. *FIDIC-EMW*

15. All works contracts would invariably involve some electrical and mechanical works. A clause on "frustration" is contained in FIDIC-EMW:

Clause 48: "If a war or other circumstance outside the control of both parties arises after the

Contract is made so that under the law governing the Contract the parties are released from further performance then the sum payable by the Employer to the Contractor in respect of the work executed shall be the same as that which would have been payable under Clause 46 if the Contract had been terminated under the provisions of Clause 46."

16. This clause is similar to the FIDIC-CEC clause (see *supra,* paragraph 12). However, it leaves the question of "frustration" to be determined by reference only to the law governing the contract.

17. The "special risks" defined in FIDIC-EMW are similar though not identical to FIDIC-CEC (see *supra,* paragraph 14). Clause 47.5 of the former reads:

"The special risks are the nuclear and pressure wave risks described in Clause 15.1 (*b*) iii and IV or insofar as it relates to the country in which the Works are to be erected, war, hostilities (whether war be declared or not), invasion, act of foreign enemies, rebellion, revolution, insurrection, military or usurped power, civil war or, unless solely restricted to the employees of the Contractor or of his Sub-Contractor and arising from the conduct of the Works, riot, commotion or disorder."

In FIDIC-EMW, except for nuclear and pressure wave risks, all other risks so enumerated in the above clause must relate to the country in which the works are carried out. These include war, hostilities (whether declared or not) and invasion. However, in FIDIC-CEC, risks of war, hostilities and invasion need not relate to the country in which the works are carried out.

5. *UNIDO model contracts (CRC, TKL and STC)*

18. All the three UNIDO model contracts adopt the same approach to the definition of *force majeure.* For convenience, reference is made to clause 34.1 of the UNIDO-CRC model contract:

"In this Contract, *Force Majeure* shall be deemed to be any cause beyond the reasonable control of the CONTRACTOR or the PURCHASER (as the case may be) which prevents, impedes or delays the due performance of the Contract by the obligated party and which, by due diligence, the affected party is unable to control, despite the making of all reasonable efforts to overcome the delay, impediment or cause."

Force Majeure is defined in article 34.1 to include the following:

"Any war or hostilities;

"Any riot or civil commotion;

"Any earthquake, flood, tempest, lightning, unusual weather or other natural physical disaster. Impossibility in the use of any railway, port, airport, shipping-service or other means of transportation (occurring concurrently . . .);

"Any accident, fire or explosion;

"Any strike, lock-out or concerted acts of workmen (except where it is within the power of the party involving the Force Majeure to prevent);

"Shortages or unavailability of materials (compounded by the same shortage or unavailability from alternate sources) if beyond the CONTRACTOR's control."

6. *Sales Convention*

19. Most contracts for the supply and construction of large industrial works would probably fall outside the scope of the Sales Convention. Be that as it may, the approach adopted in the "Exemptions" provision in the Convention may be relevant in examining an exoneration clause in a works contract. Article 79 (1) reads:

"A party is not liable for a failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control and that he 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."

20. The conditions under which a party is not liable for a failure to perform his obligations under article 79 (1) are similar to some *force majeure* clauses in works contracts.

21. The Convention also makes provision for exemption in the case of a failure by a third party whom the seller had engaged to perform the whole or a part of the contract. Article 79 (2) is intended *to be limited to the exemption of a sub-contractor and not a supplier.* It reads:

"If the party's failure is due to the failure by a third person whom he has engaged to perform the whole or a part of the contract, that party is exempt from liability only if:

"(*a*) He is exempt under the preceding paragraph; and

"(*b*) The person whom he has so engaged would be so exempt if the provisions of that paragraph were applied to him."

7. *ICC* force majeure *clause*

22. ICC has drafted a *force majeure* clause for insertion in "contracts to be performed by stages or with deferred performance especially in international practice". In its report on "*Force majeure* and hardship clauses in international contracts" it was stated that "it is necessary to adapt the clauses to the basic economic situation which they are to govern" (Documents Nos. 460/233, 460/247 and 460/262).

23. Among the types of contract which were examined in the preparation of the ICC *force majeure* clause were "contracts aimed at the construction of large industrial, mining, agricultural or building complexes, and particularly so-called 'turn-key contracts'".

24. The following *force majeure* clause was suggested (revised 1980):

"Clause of release from liability

"I. *Definition of circumstances releasing from liability*

"(1) *Event of force majeure*

"A circumstance releasing a party from liability may be defined as any event of force majeure, or any unforeseen event occurring outside the control of that party, in so far as he was unable to prevent its occurrence or anticipate its effects, which temporarily or permanently prevents him from fulfilling his contractual obligations in whole or in part, account being taken of the diligence which may reasonably be required of him.

"(2) *Other circumstances*

"A circumstance releasing a party from liability may be defined as any one of the following events, when they are of a nature to prevent one of the parties temporarily or permanently from fulfilling his obligations in whole or in part:

"(*a*) War and civil war, whether declared or not, riots and revolutions, acts of piratry, boycott;

"(*b*) Acts of sabotage, requisition, confiscation, nationalisation, embargoes and expropriation;

"(*c*) Violent storms, cyclones, earthquakes, tidal waves, destruction by lightning and other natural disasters;

"(*d*) Explosions, fires, destruction of machines, of factories, and of any kind of installations inasmuch as these occurrences are not imputable to the fault of the party relying on them;

"(*e*) Strikes and lock-outs of all kinds, including 'go-slows', occupation of factories and premises, strikes which do not involve any interruption of work, and work stoppages arising in the enterprises of one of the parties, whether or not any preliminary conciliation procedure laid down by law has been followed, and without having to examine the causes of these occurrences;

"(*f*) Acts of authority, whether or not they are legally justifiable, and whether or not arbitrary, apart from these for which one party assumes the risk by virtue of other provisions of this contract;

"(*g*) Discontinuance or interruption, for reasons not imputable to the fault of a Party, of normal supplies either of primary products, of materials, of energy or other items necessary for the performance of the obligations, or significant reduction of such supplies provided that in this latter case, the Party has carried out a reasonable allocation of his supplies between his different co-contracting Parties and provided that in all cases, the Party has shown that he has taken the measures reasonably required of him in these circumstances to provide substitutes;

"(*h*) Default of suppliers or sub-contractors by reason of events affecting them and constituting circumstances releasing from liability, so far as they are concerned, within the meaning of the present contract, provided that the Party has shown that he has taken all measures reasonably required of him to provide substitutes in respect of the defalcation;

"(*i*) Impossibility for the Party to resell the products manufactured—transported—supplied—by virtue of the contract, as a result of any circumstances for which he is not responsible;

"(*j*) Impossibility of securing adequate means of transport by reason of market conditions, any event constituting circumstances releasing from liability within the meaning of the present contract affecting the transport, port, maritime or air installations, or transport by land as well as transport enterprises whose assistance is required for the performance of the contract, provided that the Party has demonstrated that he has taken all measures reasonably required of him to provide substitute in respect of these defalcations;

"(*k*) (Other circumstances may, if desired, be included here in the light of the particular circumstances of the individual contract).

"The parties specify that the following events shall not, in any case, be considered as circumstances releasing from liability:

"(*a*) Refusal of authorisation of licences, of entry and residence permits, or of necessary approvals, to be issued by a public authority of any kind whatsoever so as to permit performance of this contract;

"(*b*) . . . (if desired, insert here other events of which the risk is to be assumed by one of the parties)."

25. The ICC clause is not integrated as part of a set of general conditions applicable to a specific type of contract. It was drafted on the understanding that "it would be necessary to adapt it according to the contract and the requirements of the applicable national law."

C. *Notification*

1. *Duty to notify*

26. The party who relies on an exonerating event is generally required to notify the other party of the event

which prevented the performance of any of his obligations under the contract. The method of notification does not seem to differ much between one type of contract and another, i.e. whether it is one relating to a works contract or a sales contract. The following main types of notification found in contractual stipulations, general conditions, the UNIDO model contracts and the Sales Convention are given below:

By notice in writing

By any means

By notice in writing to be sent by air mail

By cable or telex when such means of communication are available and to be confirmed by registered air mail

By giving notice.

27. In the notification the *force majeure* event may be verified by the following:

By a public authority in the country where the circumstances occurred and operated, e.g. notary public, local or federal government, as the case may be

By consulate

By chamber of commerce

Where *force majeure* occurs outside the supplier's country, the event to be endorsed by local chamber of commerce confirmed by the embassy of the supplier's country residing there.

28. The time within which the notification must be given varies. The following were found:

Immediately

Without delay

Within a time limit agreed.

29. Even in the absence of a specific provision on notification, a party should, nevertheless, inform or advise the other party of an exonerating event in case he may subsequently rely on it.

30. Clause 25.2 of both ECE 188A/574A provides:

"The party wishing to claim relief by reason of any of the said circumstances shall notify the other party in writing without delay on the intervention and on the cessation thereof."

31. The various draft UNIDO model contracts, viz. CRC, TKL and STC require the affected party to give written notice to the other party within ten (10) days of the occurrence of the *force majeure*. The notice must specify the details constituting *force majeure,* with necessary evidence that a contractual obligation is thereby prevented or delayed, and that anticipated period (estimated) during which such prevention, interruption or delay may continue (article 34.2 of each of the models).

32. Under the ICC *force majeure* clause:

"Any Party invoking an event releasing from liability is obliged to inform the other Party of it within a time limit of ( ) days from the moment when it learned of the event and to give a precise description of the event and to communicate all relevant information relating to it, as soon as available so as to permit an appraisal of this event and its effects on performance of the contractual obligations. Termination of the effect of the event releasing from liability will also be communicated within the same time-limit by the Party relying on it."

2. *Failure to notify*

33. In some legal systems, failure to give notification would disentitle the person affected from relying on *force majeure.* However, in other legal systems like many of the common law systems, the doctrine of frustration is not dependent on notice.

34. Where parties expressly make provision for notification in a *force majeure* clause, the consequences to be drawn from failure to give such notification are often spelt out.

35. Under ECE 188A/574A it is expressly stated that the party wishing to claim relief shall notify the other party.

36. Under all the UNIDO models, viz. CRC, TKL and STC reliance on *force majeure* is conditional upon notification being given to the other party (article 34.2 of each of the models).

37. Under article 79 (4) of Sales Convention, if notice of the impediment is not given to the other party within a reasonable time, the non-performing party is liable for the damages resulting from such non-receipt, together with other remedies under the Convention which the party may have against him.

38. Under the ICC clause:

"If the Party concerned fails to carry out the communications referred to above, he will automatically lose all right to rely on the event as a circumstance releasing from liability."

D. *Consequences of exoneration*

1. *Effects contemplated by parties in contractual stipulations*

39. Depending on variations and precise scope, the following consequences have been incorporated into *force majeure* clauses:

Obligations of defaulting party suspended for duration of event

Delay occasioned by *force majeure* shall automatically lead to an extension of the time for performance—commensurate with such delay

Defaulting party to take reasonable steps to correct the situation as soon as circumstances permit with a view to resuming full performance

Parties will renegotiate the contract

Parties are *entitled to repudiate* the contract after giving notice

After certain period, either party may terminate the contract with applicable law as to consequences upon termination.

2. *ECE 188A and ECE 574A*

40. Under ECE 188A/574A if by reason of the circumstances the performance of the contract within a reasonable time becomes impossible, either party shall be entitled to terminate the contract by notice in writing to the other party without requiring the consent of any court (clause 25.3 of both ECE 188A/574A. For details regarding the consequences of termination, see part two, XVII, *Termination*).*

3. *FIDIC-CEC*

41. The consequences of "special risks" are set out in detail in clause 65:

"Notwithstanding anything in the Contract contained:

"(1) The Contractor shall be under no liability whatsoever whether by way of indemnity or otherwise for or in respect of destruction of or damage to the Works, save to work condemned under the provisions of Clause 39 hereof prior to the occurrence of any special risk hereinafter mentioned, or to property whether of the Employer or third parties, or for or in respect of injury or loss of life which is the consequence of any special risk as hereinafter defined. The Employer shall indemnify and save harmless the Contractor against and from the same and against and from all claims, proceedings, damages, costs, charges and expenses whatsoever arising thereout or in connection therewith.

"(2) If the Works or any materials on or near or in transit to the Site, or any other property of the Contractor used or intended to be used for the purposes of the Works, shall sustain destruction or damage by reason of any of the said special risks the Contractor shall be entitled to payment for:

"(*a*) Any permanent work and for any materials so destroyed or damaged, and, so far as may be required by the Engineer, or as may be necessary for the completion of the Works, on the basis of cost plus such profit as the Engineer may certify to be reasonable;

"(*b*) Replacing or making good any such destruction or damage to the Works;

"(*c*) Replacing or making good such materials or other property of the Contractor used or intended to be used for the purposes of the Works.

". . .

"(4) The Employer shall repay to the Contractor any increased cost of or incidental to the execution of the Works, other than such as may be attributable to the cost of reconstructing work condemned under the provisions of Clause 39 hereof, prior to the occurrence of any special risk, which is howsoever attributable to or consequent on or the result of or in any way whatsoever connected with the said special risks, subject however to the provisions in this Clause hereinafter contained in regard to outbreak of war, but the Contractor shall as soon as any such increase of cost shall come to his knowledge forthwith notify the Engineer thereof in writing.

". . .

"(6) If, during the currency of the Contract, there shall be an outbreak of war, whether war is declared or not, in any part of the world which, whether financially or otherwise, materially affects the execution of the Works, the Contractor shall, unless and until the Contract is terminated under the provisions of this Clause, continue to use his best endeavours to complete the execution of the Works. Provided always that the Employer *shall be entitled at any time* after such outbreak of war *to terminate the Contract* . . ."

42. The consequences of "frustration" are described in clause 66:

"If a war, or other circumstances outside the control of both parties, arises after the Contract is made so that either party is prevented from fulfilling his contractual obligations, or under the law governing the Contract, *the parties are released from further performance,* then the sum payable by the Employer to the Contractor in respect of the work executed shall be the same as that which would have been payable under Clause 65 hereof if the Contract had been terminated under the provisions of Clause 65 hereof."

4. *FIDIC-EMW*

43. In clause 47 of FIDIC-EMW the consequences of "special risks" are similar to those in FIDIC-CEC:

"47.1: Notwithstanding anything in the Contract contained, the Contractor shall be under no liability whatsoever whether by way of indemnity or otherwise for or in respect of destruction of or damage to the

* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

Works, save to work rejected under the provisions of Clause 28 hereof prior to the occurrence of any special risk hereinafter mentioned, or to property whether of the Employer or third parties, or for or in respect of injury or loss of life which is the consequence of any special risk as hereinafter defined.

"47.2: If the Works or any Plant on or near or in transit to the Site, or any other property of the Contractor used or intended to be used for the purposes of the Works, shall sustain destruction or damage by reason of any of the said special risks the Contractor shall be entitled to payment for:

"(*a*) Any Portion of the Works or of Plant so destroyed or damaged,

"and so far as may be required by the Engineer, or as may be necessary for the completion of the Works, on the basis of cost plus such profit as the Engineer may certify to be reasonable for

"(*b*) Replacing or making good any such destruction or damage to the Works;

"(*c*) Replacing or making good such materials or other property of the Contractor used or intended to be used for the purposes of the Works.

"47.3: Destruction, damage, injury or loss of life caused by explosion or impact whenever and wherever occurring of any mine, bomb, shell, grenade, or other projectile, missile, munition or explosive or war, shall be deemed to be a consequence of the said special risks.

"47.4: The Employer shall repay to the Contractor any increased cost of or incidental to the execution of the Works, other than such as may be attributable to the cost of reconstructing work rejected under the provisions of Clause 28 hereof, prior to the occurrence of any special risk, which is howsoever attributable to or consequent on or the result of or in any way whatsoever connected with the said special risks, subject however to the provisions in these Conditions in regard to outbreak of war, but the Contractor shall as soon as any such increase of cost shall come to his knowledge forthwith notify the Engineer thereof in writing."

44. The following consequences of "frustration" are set out in detail in the FIDIC-EMW Conditions:

Clause 46: "If during the currency of the Contract there shall be an outbreak of war (whether war is declared or not) in any part of the world which, whether financially or otherwise, materially affects the execution of the Works the Contractor shall, unless and until the Contract is terminated under the provisions in this Clause contained, use his best endeavours to complete the execution of the Works, provided always that either the Employer or the contractor shall be entitled, at any time after such outbreak of war, *to terminate* this Contract . . ." (See also clause 46.2 in part two, XVII, *Termination*.)*

45. These Conditions also contemplate the possibility of the parties being released from further performance under the law governing the contract:

Clause 48: "If a war or other circumstance outside the control of both parties arises after the Contract is made so that under the law governing the Contract the parties are released from further performance then the sum payable by the Employer to the Contractor in respect of the work executed shall be the same as that which would have been payable under Clause 46 if the Contract had been terminated under the provisions of Clause 46."

5. *UNIDO model contracts (CRC, TKL and STC)*

46. The consequences of *force majeure* adopted by the three models are identical in some respects. The non-performing party is excused from "the performance or punctual performance (as the case may be) as from the date of notification of the 'force majeure' for so long as may be justified" (article 34.2 of the respective models). All three models contain a renegotiation clause (see XIV, *Renegotiation, infra,* paragraph 60. For consequences of termination, see part two, XVII, *Termination*).*

6. *Sales Convention*

47. Paragraph (1) of article 79 provides exemption from liability for a failure to perform obligations due to *force majeure*. Paragraph (5) provides that exemption from liability under the article prevents the other party from exercising only his right to claim damages, but not in respect of other rights under the Convention.

7. *ICC* force majeure *clause*

48. The consequences of *force majeure* are spelt out in detail with provision for renegotiation:

"The effect of the event releasing from liability is to suspend performance of the obligations which has become impossible as well as of the corresponding obligations (without prejudice to the application of the clauses for adaptation contained in the present contract). No Party will be liable to pay an indemnity on this account. The contractual time limits are extended for a period corresponding to that of the effects of the event releasing from liability.

"During the period of suspension, the parties shall bear permanently half the burden of the costs required for continuation, under the best conditions, of the

* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

performance of the contractual obligations temporarily suspended.

"Clearance of the said costs shall be carried out either on cessation of the circumstances releasing from liability or on settlement of the accounts in the event of termination of the contract on expiry of the period of suspension."

[Renegotiation provision—see XIV, *Renegotiation, infra,* paragraph 64.]

"The parties will retain the fruits of their reciprocal performances carried out previously. They will account to one another. Each party must account to the other for advantages received and kept under the partially performed contract subject to the reservation that the sums due under this provision may not exceed the cost of services tendered, of deliveries carried out, and of goods or other items supplied by the other party. Account will be taken of payments already made by the parties in execution of the terminated contract."

XIV. Renegotiation

A. *General remarks*

49. The nature of a works contract necessitates performance over a period of time. Because of a number of factors—for example, economic, fiscal, commercial, legal, political and technological—it is not always possible to proceed with the contract as originally contemplated. Indeed, parties at the outset may not be aware of all factors that may subsequently bear upon the performance of the contract and upon their contractual equilibrium. Even though parties may not be able to carry on with the contract in strict adherence to its terms, it may still be to their mutual advantage not to terminate the contract but to adapt it to the new environment.

50. The mechanism of renegotiation is designed to serve a practical and functional purpose of enabling all parties concerned to review and adapt the contract to changed circumstances when even the more flexible doctrines of *rebus sic stantibus, imprévision* and *Wegfall der Geschäftsgrundlage* may not suffice as a conceptual framework for the revision of contracts.

51. Renegotiation of contracts, at least in certain types of contract including a works contract, is a recent phenomenon. But there appears to be a growing awareness that while renegotiation may not provide the panacea to all problems posed by changed circumstances, nevertheless, it enables parties to agree on finding a means of re-establishing their contractual equilibrium. Of course, even in the absence of such a clause, parties can still review their contract but the insertion of such a clause provides the assurance that parties would resort to some process in order to rescue the contract.

52. There is no renegotiation clause in ECE 188A and ECE 574A, FIDIC-CEC and FIDIC-EMW. In the UNIDO model contracts (CRC, TKL and STC), renegotiation is confined only to *force majeure* situations.

53. The wording of the clauses under study is varied, particularly in the hardship clauses. One reason is that the full implications of changed circumstances, short of rendering the contract incapable of performance under an exoneration clause (see XIII, *Exoneration, supra*), have not been fully worked out in most legal systems.

B. *Renegotiation in event of* force majeure

54. In the UNIDO model contracts (CRC, TKL and STC), it was noted that renegotiation was provided for in some *force majeure* clauses (see XIII, *Exoneration, supra,* paragraph 46).

1. *Contractual stipulations*

55. Very few *force majeure* clauses in the Secretariat's collection were found to make provision for renegotiation or adjustment. This is not to say that the renegotiation mechanism is seldom employed.

56. In a works contract between a West European and Middle East entity a renegotiation clause was inserted in a *force majeure* clause to enable parties to "consult with each other" regarding the "future implementation of the agreement." This is an example of a very general clause.

57. Another renegotiation clause found in a recent contract entered into between a West European and African entity reads:

"If 'force majeure' last continuously for ( ) months, then both parties shall without delay meet to consult each other and try to find an appropriate remedy to the situation and to reach agreement thereon. When considering the measure to be taken, the Owner and the Contractor shall give due and serious attention to the difficulties caused by the above-mentioned circumstances, and make serious attempts at finding a fair solution."

58. In contrast to the above clauses, an example may be given of a more specific clause—a time limit is given to the parties to agree to a solution, failure of which entitles either party to cancel the contract. The clause states:

"If any such delay . . . lasts for more than 90 days, the parties shall immediately consult with one another for the purpose of agreeing upon the basis on which

seller resumes production at the end of delay. If they do not agree upon a solution of the problem involved, including adjustment of the price, within 150 days from the beginning of such delay, then either party may, by written notice cancel the portion of the order which is delayed and in such event the Purchaser shall pay to seller reasonable and proper cancellation charges.

59. In some renegotiation clauses express provision is made for the consequences of a breakdown of renegotiation. In others, it is silent. In such a situation the original provisions of the contract will be applicable.

2. *UNIDO model contracts (CRC, TKL and STC)*

60. The wording of the renegotiation provision in the *force majeure* clause in the UNIDO-CRC model differs slightly from that in the UNIDO-TKL. The wording of the latter is identical with that of the UNIDO-STC. The UNIDO-CRC reads:

"*Article 34:* Force Majeure

"34.3: The PURCHASER or the CONTRACTOR (as the case may be) shall be diligent in endeavouring to prevent or remove the cause of Force Majeure. Either party upon receipt of the Notice of Force Majeure under Article 34.2 shall confer promtly with the other and agree upon a course of action to remove or alleviate such cause(s), or shall seek alternative methods of achieving the performance objectives under the Contract.

"34.4: If by virtue of Article 34.2, either of the parties is excused from the performance or punctual performance of any obligation for a continuous period of six (6) months then the parties shall consult together to seek agreement as to the required action that should be taken in the circumstances and as to the necessary amendments that should be made to the terms of the Contract.

"34.5: If by virtue of Article 34.2, either of the parties is excused from the performance or punctual performance of any obligation for a continuous period of nine (9) months for one or more causes and if the consultations referred to in the preceding Subarticle 34.4 have not resulted in mutual agreement (or have not taken place because the parties have been unable to communicate with one another), the parties shall thereupon agree to amend the terms of this Contract by virtue of the prevailing Force Majeure circumstances and shall determine the course of further action. If the parties are unable to reach an agreement to amend the terms of this Contract by virtue of the prevailing Force Majeure then the Contract *shall be deemed to be terminated* pursuant to Article 33 above . . ." (see part two, XVII, *Termination*).*

* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

61. The UNIDO-CRC counter-proposal seeks to amend the UNIDO-CRC by shortening the period to six months within which the parties must examine the possibility of continuing with the contract in the context of the *force majeure*. Otherwise the parties will have the right to terminate the contract:

"*Article 34:* Force Majeure

"34.3: Either party upon receipt of the Notice of Force Majeure under Article 34.2 shall confer as soon as possible with the other and agree upon a course of action to remove or alleviate such cause(s), or shall seek alternative methods of achieving the performance objectives under the Contract, and on the other party upon the relevant consequences on the Contract Price and on the Contract execution time.

"34.4: If the duration of the circumstance of Force Majeure exceeds six (6) months, the Parties shall meet together again to examine the possibility of continuing to carry out the contract. If an agreement cannot be reached upon, the Parties shall have the right to terminate all or part of the contract; in that case the CONTRACTOR shall be indemnified for the consequences of such termination as set forth in Article 33.3."

62. As stated earlier, there is a slight difference in the wording of the UNIDO-CRC model on the one hand and the UNIDO-TKL and UNIDO-STC models on the other. However, the real difference seems to be that while article 33 of the UNIDO-CRC model (dealing with ordinary termination of contract) applies to the termination of a contract in the context of *force majeure* upon failure of an agreement in renegotiation, the counterparts of article 33 in the other models do not apply to the latter models in a similar situation (see part two, XVII, *Termination*).

63. Although the renegotiation provisions in the *force majeure* clauses under study do not expressly state what the position of the contract is during renegotiation, there are other provisions in the *force majeure* clauses which excuse the party affected by *force majeure* from punctual performance or performance.

3. *ICC* force majeure *clause*

64. The ICC *force majeure* clause makes provision for renegotiation of the contract:

"If the circumstances releasing from liability continues to produce its effects for more than ( ) months, the contract shall be automatically abrogated at the expiry of this period, *unless before such expiry the parties, after consulting one another, agree to modify the contract so as to adapt it to the circumstances arising from the occurrence of the event resulting in a release from liability.*"

In the ICC clause, unlike those in the UNIDO model contracts, renegotiation is not mandatory. No provision is made for third party intervention—only the parties to the contract are involved in the readaptation.

C. *Renegotiation in hardship situations*

1. *Contractual stipulations*

65. Renegotiation of contracts to meet fundamental changes particularly in economic or financial events is commonly found in hardship clauses. The scope of such clauses under study varies from a very specific (e.g. limiting the clause to only price-revision) to a general situation.

66. A number of studies on hardship clauses demonstrate that while each type of contract may require certain characteristics not found in other types of hardship clause, the combined totality of the characteristics could well be employed, *mutatis mutandis,* in other types of contract, including, of course, a works contract.

67. In a study of such clauses undertaken by the "International Contracts" study group (under Marcel Fontaine, Director, Centre de Droit des Obligations, Catholic University of Louvain)[1] it was noted that among the types of contract in which hardship clauses were inserted are "large works projects" and "mechanical engineering." It was also noted that "long-term contracts are clearly those where hardship clauses are most frequently stipulated . . ."

68. It should be emphasized that this section of the study is based mainly on the hardship clauses made available to the above-mentioned "International Contracts" study group. Although some of these hardship clauses were taken from "large works projects" and "mechanical engineering" contracts, there was no attempt at isolating them for the purpose of that study.[2] Be that as it may, these hardship clauses examined may well apply to a works contract.

69. An analysis of a number of hardship clauses reveals the following criteria. Some of these criteria are conceived in wider scope while others in narrower scope.

(a) *Criteria*

(i) Change in circumstances

This factor has been expressed in the following ways:

(*a*) ". . . If at any time during the term hereof either party shall by notice in writing to the other claim upon reasonable grounds . . . that owing to changed circumstances including, but not limited to changes in monetary values or discriminatory Governmental action or regulations . . ."

(*b*) "In the event of a fundamental change in the conditions which were material to the making of this Agreement, and if from such fact, in order to respect certain provisions, either of the Parties is required to bear unfair hardship, they will meet with a view to modifying the terms and conditions of the present Agreement."

(*c*) "If either party considers, that owing to changed circumstances, the above price should be revised . . ."

(*d*) ". . . if there is the occurrence of an intervening event or change of circumstances . . ."

(*e*) ". . . should there be very important changes in circumstances or very significant changes in economic conditions . . ."

Although in some of the above clauses there is the requirement that the change must be "fundamental" and "important" while no such epithets are used in others, nevertheless, it would appear from the consequences that the change of circumstances would have no effect unless it seriously affects the obligations in the contract.

(ii) Unforeseeability

The following clauses emphasize the element of unforeseeability:

(*a*) ". . . it is impracticable to make provision for every contingency which may arise . . ."

(*b*) ". . . circumstances . . . beyond the normal expectations of the parties . . ."

(*c*) ". . . in the event of the occurrence of unforeseeable economic developments . . ."

(*d*) ". . . extraordinary or unforeseen circumstances . . ."

(iii) Event beyond control

The above criterion was contained in the following clauses:

(*a*) ". . . an intervening event or change of circumstances beyond said party's control when acting as a reasonable and prudent operator . . ."

(*b*) ". . . any circumstances beyond the control of the parties . . ."

The criteria of "unforeseeability" and "event beyond control" of the parties are separate. Failure to appreciate the difference, as seen in some clauses, and a substitute of one for the other would circumscribe the scope of such

[1] See (1976) 2 *Droit et pratique du commerce international,* p. 51.

[2] It is hoped that the Commission would provide the Secretariat with works contracts containing renegotiation provisions. There is a dearth of such documentation at the disposal of the Secretariat. It is also important to examine these clauses in the context of other provisions in the contract itself. In some instances, the Secretariat managed to obtain only specific clauses taken out of their context.

a clause. Other clauses do not mention the two criteria, which of course widens the scope considerably.

(iv) Substantial economic hardship

(*a*) ". . . substantial economic hardship . . ."

(*b*) ". . . which place said party in the situation that . . . all annual costs . . . associated with or related to (. . .) which is the subject of this Agreement exceed the annual proceeds derived from the sale of said (. . .) . . ."

(*c*) ". . . it, owing to circumstances . . ., the economy of the contractual relationships should become modified to the extent of rendering prejudicial, for one of the parties, the discharge of his obligations . . ."

(v) Seriousness of events

(*a*) ". . . substantial and disproportionate prejudice to either party . . ."

(*b*) ". . . undue hardship to either party . . ."

(*c*) ". . . unfairness or substantial and disproportionate prejudice to the interests of either . . ."

(b) *Procedure of renegotiation*

70. As noted, hardship clauses invariably provide for renegotiation of the contract. However, problems can arise if the conditions for renegotiation are not precise. A number of clauses under study contain procedures to determine the basis for renegotiation:

(*a*) ". . . the (prejudiced) party . . . may by notice request the other for a meeting to determine if said occurrence has happened . . . If the seller and the buyer have not agreed . . . within sixty days . . . either party may require the matter to be submitted for arbitration . . . The arbitrators shall determine whether the aforesaid occurrence has happened . . ."

(*b*) "In the absence of consensus, it is agreed that each of the parties shall designate an economic expert, assisted if appropriate by a financial expert, and that they shall meet together to determine whether the advantages of the present agreement have been fundamentally disrupted as a result of an unforeseeable event."

71. ICC has also made provision for third party intervention (see *infra*, paragraph 77). Such a procedure may obviate the practical problem which may arise, when the clause is not efficacious due to imprecise drafting and when the party who is not disadvantaged by the "hardship" seeks to prevent the renegotiation.

(c) *Time limit*

72. In some hardship clauses the time between the conclusion of the contract and the point of time when the clause can be invoked is given. For example, the renegotiation clause in the On-Shore (Voltaian Basin) Petroleum Production Agreement of 1974 between the Government of Ghana and Shell Exploration and Production Company of Ghana Ltd., a subsidiary of Shell International Ltd., reads:

"It is hereby agreed that if during the term of this Agreement there should occur such changes in the financial and economic circumstances relating to the petroleum industry, operating conditions in Ghana and marketing conditions generally as to materially affect the fundamental, economic and financial basis of this Agreement, then the provisions of this Agreement may be reviewed or renegotiated with a view to making such adjustments and modifications as may be reasonable having regard to the operator's capital employed and the risks incurred by him, always provided that *no such adjustments or modifications shall be made within 5 years after the commencement of production area and that shall have no retroactive effect.*"[3]

In a sales contract, a further restriction on the frequency of reliance of the hardship clause was found:

"This section may not be invoked by seller or buyer prior to the first day of October 19. . ., and no more often than once every two years."

(d) *Approach to renegotiation*

73. The hardship clauses under study demonstrate three approaches to renegotiation:

(i) Objective approach

". . . in order to restore the parties to a balanced situation comparable to that which obtained at the time that the present contract was concluded."

(ii) Subjective approach

a. ". . . in fairness to parties . . ."

b. ". . . appropriate and equitable in the circumstances."

c. ". . . such action as may be appropriate to abate such unfairness or undue hardship . . ."

(iii) Hybrid approach

". . . with fairness and without substantial and disproportionate prejudice to the interest of the other . . ."

(e) *Contract during renegotiation*

74. In the hardship clauses under study, there does not appear to be any express provisions as to the position of the contract during renegotiation. In the context of an

[3] Cited in Asante, "Stability of contractual relations in the transnational investment process" (1979) 28 *International and Comparative Law Quarterly*, pp. 401, 417.

exoneration clause the contract is suspended and may be suspended even if negotiations fail. Whether in events other than exonerating events, the contract will be suspended would depend on express stipulations.

(f) *Decrease or termination of hardship*

75. One such clause which made provision for the situation when the hardship has decreased or terminated reads:

> ". . . To the extent that any occurrence of hardship as determined under this Section 13.9 shall have decreased or ended then any revision of price or other conditions pursuant to an arbitration award shall likewise be changed or ended and the terms and conditions of the Agreement (if not already determined pursuant to paragraph *b* hereof) shall be restored to take account of the said decrease or ending of the occurrence of hardship."

2. *UNIDO model contracts (CRC, TKL and STC)*

76. Article 33.1 of each of the UNIDO-models appears to deal with a situation which could result in hardship. The article provides that "in the event that the PURCHASER is subject to any circumstances which are wholly unavoidable and/or beyond his control but not including occurrences which are covered by Article 34 . . .",[4] the purchaser is entitled to terminate the contract. It is noted that the clause is couched in very wide language and could cover a situation where no substantial hardship is involved. It may also be noted that no renegotiation is provided unlike in the *force majeure* clause (see *supra,* paragraph 60).

3. *ICC "suggested hardship clause"*

77. The ICC "suggested hardship clause" (Document No. 460/233) is aimed at bringing about renegotiation, on new bases, of a contract which is in the process of being performed when the envisaged change in circumstance occurs. The clause reads:

"Suggested hardship clause

"(a) *Conditions for application*

"Should there occur after conclusion of the contract circumstances of the following nature: economic, political (including modifications of legislation or administrative measures) or technical, which were unforeseeable for the Parties at the moment the contract was concluded and are outside any control on their part and which destroy the equilibrium of the relations between the Parties making performance of the contract so onerous (though not impossible) for one of them that the burden would exceed all the anticipatory provisions made by the Parties at the time the agreement was concluded, such Party may request the revision of the present contract.

"This Party must inform the other Party within a time limit of (. . .) from the moment when it became aware of the event at the same time precisely describing the event relied on and explaining in what way it falls under the provisions of the present article; it will communicate to the other Party without delay every element required for an assessment in the matter in its possession. Unless it carries out this communication, the Party concerned will be automatically excluded from relying on the present article.

"The happening of the event justifying the request for adaptation of the contract does not in any case relieve the Party relying on it from his duty to continue performance of his obligations, nor does it involve a suspension of them.

"(If desired: The Parties agree that the following events in particular fall within the scope of this provision: . . .)."

"(b) *Effects*

"If continuation of the contract by means of a contractual adaptation does not appear economically possible for all the Parties, the Party invoking the benefit of the present clause may terminate the contract without prejudice to the right of the other party to bring any proceedings before the Courts (or: the arbitrator designated in accordance with Article . . .) if the conditions for application of the present clause are not fulfilled.

"If continuation of the contract appears economically possible for all the Parties by means of an adaptation, the Parties will immediately consult together with a view to incorporating in the present contract, in good faith and in equity, the adaptations which are necessary, account being taken of the new circumstances and of the risks and burdens that the Parties ought, in any case, to assume. Subject to contrary agreement of the Parties, these negotiations will be carried out during a maximum time limit of (. . .) months, running from the request to undertake them addressed by one Party to the other.

"The performance of the contract will be continued during these negotiations.

"Alternative 1

"If the negotiations do not succeed within this time limit, the Party invoking the benefit of the present clause may terminate the other contract without prejudice for the right of the other Party to bring any proceedings before the Courts (or: the arbitrator designated in accordance with Article . . .) if the conditions for application of the present clause are not fulfilled.

[4] Article 34 deals with *force majeure*. See XIII, *Exoneration, supra,* paras. 18 and 60.

"Alternative 2

"If the negotiations do not succeed within this time limit the contract will be readapted by a third Party, designated in accordance with the Rules on Adaptation of Contracts of the International Chamber of Commerce. This third Party will carry out his task on the conditions and in accordance with the procedure provided by the said Rules."

78. In regard to Alternative 2, ICC has drafted Rules for the regulation of contractual relations and related Standard Clauses (1978) which are designed to make third party intervention possible.

79. Although the ICC "suggested hardship clause" is not specifically drafted for use in a specific type of contract, nevertheless, it is designed for general application in international contracts, particularly in contracts involving a series of closely interrelated operations which, in the normal course of events, take place over a number of years.

[A/CN.9/WG.V/WP.4/Add.6*]

XV. Guaranties

A. *General remarks*

1. This study deals with two types of guaranties (*a*) a guaranty[1] for material, design and workmanship (mechanical guaranty); and (*b*) a guaranty for the proper performance of the works (performance guaranty).

2. In some contexts "warranty"[2] is used synonymously with "guaranty".

3. There are also various types of "bank" guaranty found in a works contract which are, however, outside the scope of this study.

B. *Mechanical guaranty*

4. The mechanical guaranty is called differently in the various forms under study. The ECE General Conditions speak of "guarantee" (clause 23). UNIDO-TKL speaks of "guarantee of workmanship and materials" (article 25) as well as of "warranties" (article 28). UNIDO-CRC uses "mechanical guarantees and warranties" (article 28.3). The FIDIC-EMW Conditions do not use the expression "guaranty" but speak of "defects liability" (clause 33).

5. The function of a mechanical guaranty is generally to limit the extent of the contractor's liability on the one hand and to give assurances and safeguards to the purchaser in regard to quality on the other hand. Clause 33.13 of FIDIC-EMW for instance provides:

"the Contractor shall be under no liability in respect of defects in or damage to the Works or any Section thereof developing or arising after the Works or any Section thereof has been taken over"

save as provided in the Conditions themselves, especially in clause 33.

1. *Extent of guaranty*

6. Under clause 23.1 of both ECE 188A/574A:

"the Contractor undertakes to remedy any defect resulting from faulty design, materials or workmanship."

7. Under clause 33.2 of FIDIC-EMW the contractor is responsible for any defect in or damage to any portion of the works which arises either (*a*) from any defective materials, workmanship or design, or (*b*) from any act or omission of the contractor done or omitted during the guaranty period.

8. The UNIDO model contracts, as criticized by an international group of contractors, deal with many questions repetitiously. Thus, for instance, the extent of the mechanical guaranty is covered in articles 25.1, 25.2, 28.1, 28.2, 28.3, 28.4, 28.8 and 28.9 of UNIDO-TKL.

9. Article 28.1 of UNIDO-TKL provides:

"The CONTRACTOR warrants that the Plant, equipment, materials, tools and supplies incorporated in the Works pursuant to this Contract conform with the specifications, plans and all of the contractual criteria, and that the work in every particular is free from defects in design, engineering, processes, materials, workmanship and construction."

10. Article 28.2 of UNIDO-TKL add further elements:

"The CONTRACTOR also warrants as to the correctness and completeness of the plans, all technical data and documents supplied by him as well as to the technical criteria of the equipment fabricated in accordance with his plans and instructions under the present Contract."

11. Article 28.4 of UNIDO-TKL refers to:

"faulty or improper design, workmanship, material, manufacture, fabrication, shipment or delivery."

12. Article 28.8 of UNIDO-TKL includes the warranty of all civil engineering structures,

"and in particular for the foundations for all buildings, plant and equipment."

* 21 April 1981.
[1] Also spelt as "guarantee".
[2] Also spelt as "warrantee".