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Celebrating the 40th Anniversary of the CISG:

CISG as a Tool for Global Trade

- Theory and Practice



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Optimizing the CISG: *Favor Contractus* and COVID-19

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CISG provides default rules for international sale of goods

Article 6 CISG [Party Autonomy]

- The parties may
 - exclude the application (i.e., opt out) of the CISG; **OR**
 - derogate from or vary the effect of any of its provisions (except for art. 12)

CISG provides default rules for international sale of goods

- The provisions of the CISG are default rules for international sale of goods, that apply by default, unless the parties agree otherwise. It can be optimized to meet the needs of the parties (even by opting out).
 - Example: increase certainty by defining “a reasonable time” for the buyer’s duty to give notice of non-conformity (Arts 39, 43 CISG)

Spectrum of Contracts: relational contracts, discrete contracts

- Relational contracts (e.g., long term contracts, supply chains) v. discrete contracts/arm's length contracts (e.g., one-shot contracts)
- CISG basically addresses contract types in the middle.
 - Emphasis on predictability (“foreseeability” at the time of contract: fundamental breach (Art 25), scope of damages” (Art 74), exemption (Art 79)).
 - Principle of “*favor contractus*”.
 - No provision addressing the distinct needs of long-term contracts.

Principle of “Favor Contractus” (or “Pro-Contract”)

- What is *favor contractus*?
 - “... the aim of preserving the contract whenever possible, thus limiting the number of cases in which its existence or validity may be questioned or in which it may be terminated before time.” (Bonell, 1994 [on the Unidroit Principles])
 - Giving full effect to the “contract” to govern their relationship
- Some examples of *favor contractus* in the CISG
 - Facilitation of contract formation (Art 19(2))
 - Denial of invalidation due to “initial impossibility”
 - **Limitation of avoidance of contracts** (fundamental breach (Arts 25, 49, 64); seller’s right to cure (Art 48))

Two Topics for Optimization of the CISG

- TOPIC 1: Is there a need to optimize the CISG for super-discrete contracts (e.g., commodity sales)?
- TOPIC 2: How should the CISG be optimized for “relational contracts” (e.g., long-term supply contracts)?

TOPIC 1: Optimization for Super-Discrete Contracts?

- Should the parties opt-out of the CISG?
 - Is a stricter contract law rule allowing easy termination (e.g., English law) more suitable?
- Not necessarily so:
 1. CISG allows easy termination for such contracts.
 - “fundamental breach” (Art 25 CISG) focuses on “what [the party] is entitled to expect under **the contract**”.
 2. CISG does not limit damages (Arts 45(1)(b), 61(1)(b)).
 3. Advantages of “uniformity” lost.

TOPIC 2: Optimization for Supply-Chains

- Global Supply Chains can be relational transactions, especially in the upstream (where the supplier will make relation-specific investment)
- A major issue facing global supply-chain in the COVID-19 pandemic is the question of “**hardship**” (economic difficulty)
 - Supplier’s infection or increased health risks to continue business
 - Government measures: lock-down, closing of border, etc

TOPIC 2: Optimization for Supply-Chains

- “Hardship” is not a traditional legal concept. It arises out of business practice of incorporating “hardship clauses” especially in long term supply contracts (e.g., energy contracts) in the 1970s.
 - Duty to Renegotiate, Adaptation of the Contract by Court/Arbitral Tribunal
- Taken up by ICC hardship clause (1985); UNCITRAL Legal Guide on Drawing Up Int’l Contracts for the Construction of Industrial Works (1987) ... **post-CISG development**
- Unidroit Principles (1994, 2004, 2010, 2016)

ARTICLE 6.2.2

(Definition of hardship)

There is hardship where the occurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party receives has diminished, and

- (a) the events occur or become known to the disadvantaged party after the conclusion of the contract;
- (b) the events could not reasonably have been taken into account by the disadvantaged party at the time of the conclusion of the contract;
- (c) the events are beyond the control of the disadvantaged party; and
- (d) the risk of the events was not assumed by the disadvantaged party.

ARTICLE 6.2.3

(Effects of hardship)

(1) In case of hardship the disadvantaged party is entitled to request renegotiations. The request shall be made without undue delay and shall indicate the grounds on which it is based.

(2) The request for renegotiation does not in itself entitle the disadvantaged party to withhold performance.

(3) Upon failure to reach agreement within a reasonable time either party may resort to the court.

- (4) If the court finds hardship it may, if reasonable,
 - (a) terminate the contract at a date and on terms to be fixed, or
 - (b) adapt the contract with a view to restoring its equilibrium.

TOPIC 2: Optimization for Supply-Chains

- CISG does not specifically address “hardship”.
- However, hardship (economic difficulty) can be an “impediment” under Art 79 CISG. (CISG-AC Opinions No. 7 and No. 20)
 - However, the effect of Art 79 is exemption from damages liability. Avoidance is still allowed.
 - The essence of “hardship clauses” were in renegotiation (and contract adaptation.
 - Incorporation of “hardship clause” should be considered for global supply chain contracts.

1. A party to a contract is bound to perform its contractual duties even if events have rendered performance more onerous than could reasonably have been anticipated at the time of the conclusion of the contract.
2. Notwithstanding paragraph 1 of this Clause, where a party to a contract proves that:
 - a) the continued performance of its contractual duties has become excessively onerous due to an event beyond its reasonable control which it could not reasonably have been expected to have taken into account at the time of the conclusion of the contract; and that
 - b) it could not reasonably have avoided or overcome the event or its consequences, the parties are bound, within a reasonable time of the invocation of this Clause, to negotiate alternative contractual terms which reasonably allow to overcome the consequences of the event.

3A Party to terminate	3B Judge adapt or terminate	3C Judge to terminate
Where paragraph 2 of this Clause applies, but where the parties have been unable to agree alternative contractual terms as provided in that paragraph, the party invoking this Clause is entitled to terminate the contract, but cannot request adaptation by the judge or arbitrator without the agreement of the other party.	Where paragraph 2 of this Clause applies, but where the parties have been unable to agree alternative contractual terms as provided for in that paragraph, either party is entitled to request the judge or arbitrator to adapt the contract with a view to restoring its equilibrium, or to terminate the contract, as appropriate.	Where paragraph 2 of this Clause applies, but where the parties have been unable to agree alternative contractual terms as provided in that paragraph, either party is entitled to request the judge or arbitrator to declare the termination of the contract.