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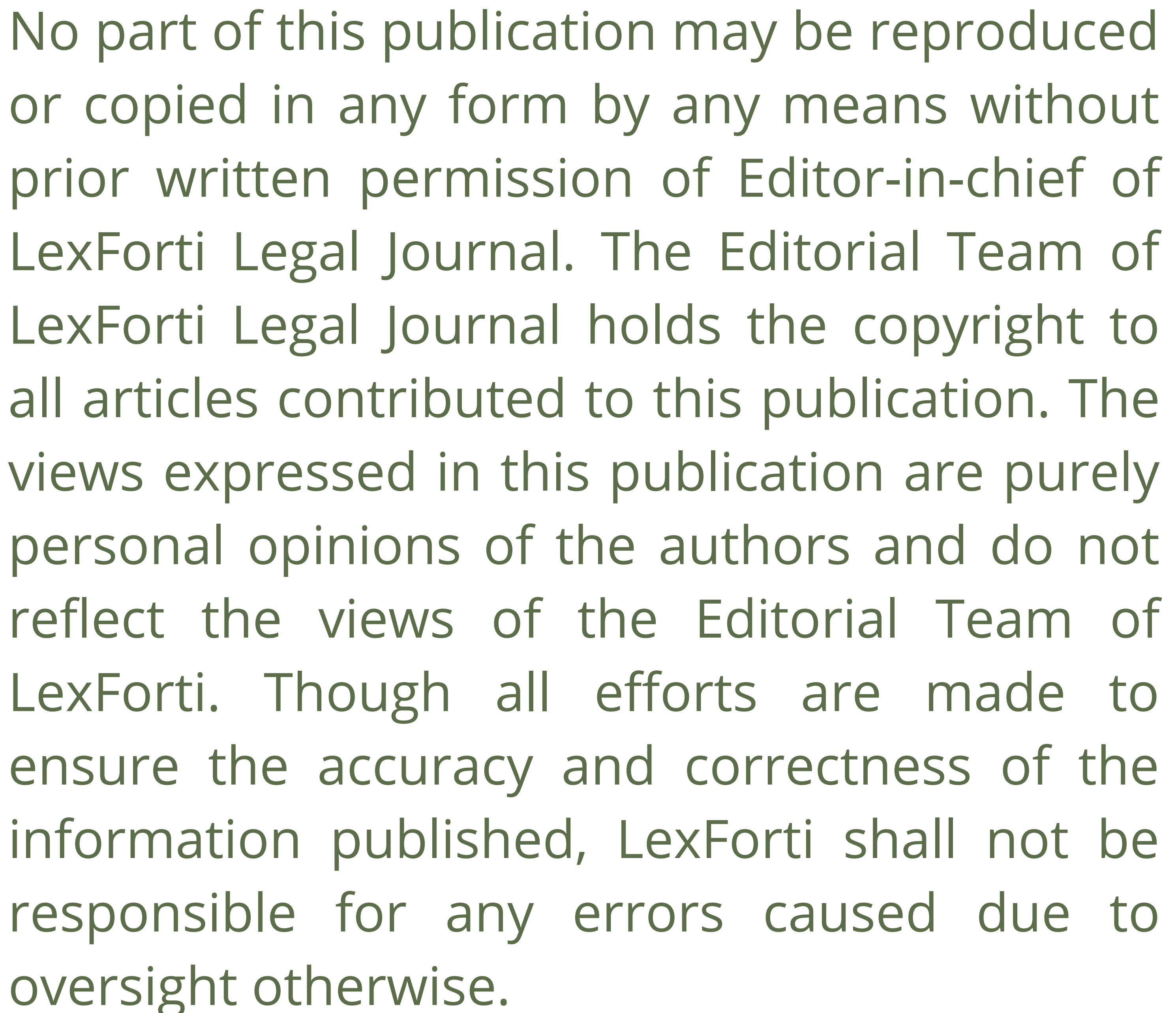

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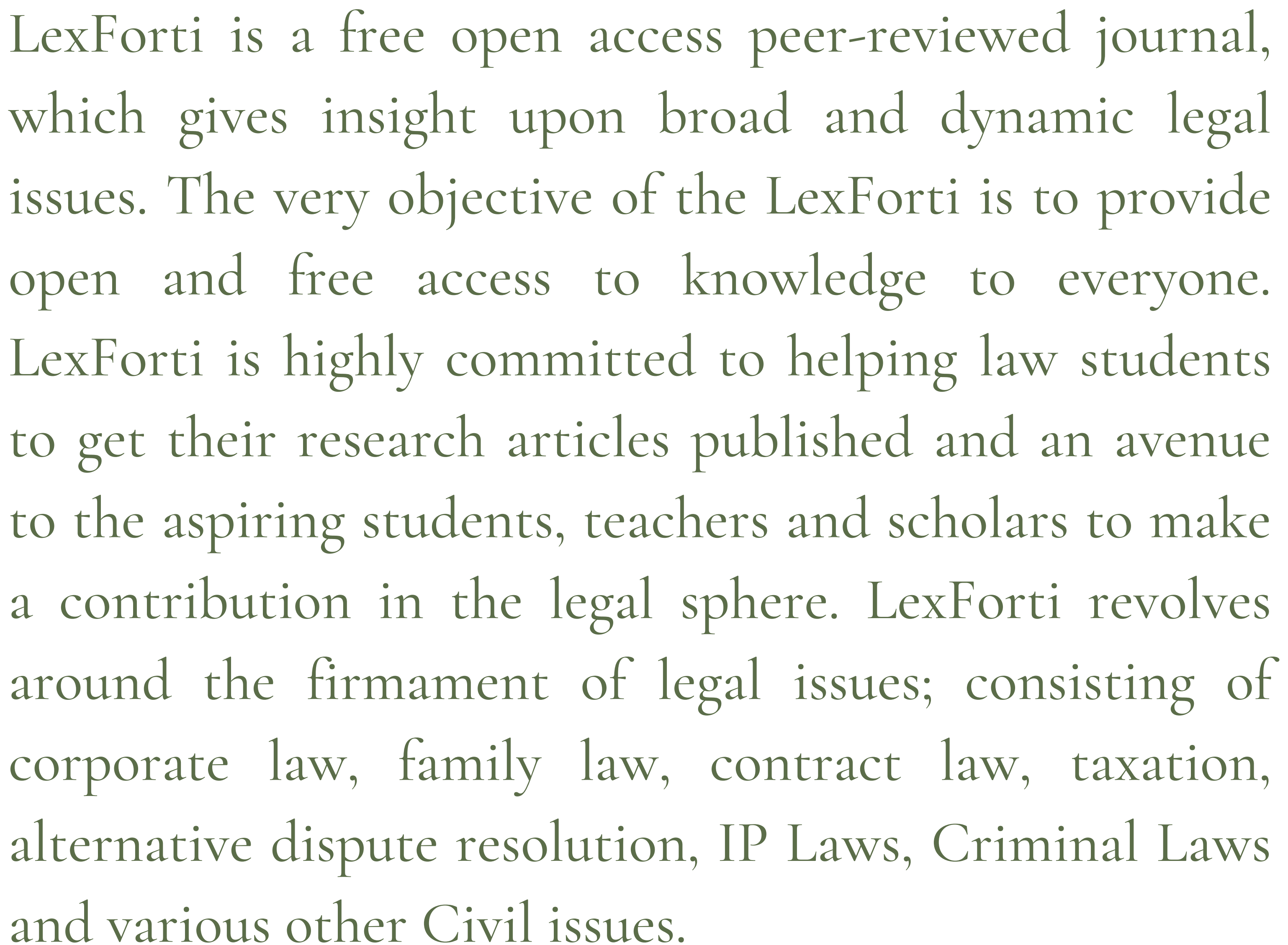

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# THE HARDSHIP DEFENCE UNDER THE UNITED NATIONS CONVENTION FOR INTERNATIONAL SALE OF GOODS

-KOPAL MITTAL & MEHEK DUA

# INTRODUCTION

The United Nations Convention for International Sale of Goods is the most widely accepted and used convention for governing international commercial transactions and contracts. It has been stated and accepted that the CISG *"can be regarded as one of the most successful attempts in international commercial law to harmonize divergent legal concepts and principles from various national laws and legal systems."* The CISG provides a default uniform law of sales for international commercial contracts and transactions to the seventy-eight ratifying countries, who collectively account for more than three-quarters of the world's international trade. [1]

As the CISG is an international treaty, the sources of its interpretation relied on by the arbitration tribunals and courts, including scholarly commentary, the *travaeux prepatoire,* arbitral awards, foreign courts' decisions are in general only of persuasive value and are not of a binding character. Despite the obvious lack of any precedential force, these sources still do hold a rather strong persuasive authority for courts and tribunals dealing with a situation of the interpretation of the CISG.[2] The lack of binding precedents for this ambiguity leads to several unique issues in the process of interpretation of this convention and application to different situations of hardship and non-performance.

The principle of hardship is commonly used in internal commercial contracts as a remedy where fulfilling the obligations agreed upon under the contract or performing the contract becomes ***excessively onerous*** to one party due to unforeseen circumstances. It shifts the balance of the economic equilibrium between the parties.[3] However, hardship and its remedy do not find an express inclusion in the CISG which has led to debate over applicability.

This debate arose due to the use of the vague term, *'impediment'* in the Article. The Convention uses this term in the Article of Force Majeure but fails to define what constitutes an impediment. Some scholars have used the terminology of hardship and economic impediment interchangeably.[4]

There have been some attempts to include the concept of hardship within the ambit of Article 79 of the CISG. This has been done in mainly two manners. First, the inclusion of hardship using a

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[1] Peter J. Mazzacano, 'Force Majeure, Impossibility, Frustration & the Like: Excuses for Non-Performance; the historical Origins and Development of an Autonomous Commercial Norm' CISG, NORDIC J. COM. L., issue 2011 50
http://ssrn.com/abstract=1982895.
[2] Ibid.
[3] CISG-AC Opinion No. 7, Exemption of Liability for Damages under Article 79 of the CISG, Rapporteur: Professor Alejandro M. Garro, Columbia University School of Law, New York, N.Y., USA. Adopted by the CISG-AC at its 11th meeting in Wuhan, People's Republic of China, on 12 October 2008.
[4] Ibid.

wide interpretation of the term 'impediment'; second, citing a gap in the Convention and filing it by resorting to Article 7.

## ARTICLE 79 CISG

Article 79 is an exemption from the liability clause under the Convention. As its title suggests, it is a Force Majeure Clause which allows a party to plead non-performance in case of an impediment as given under the Article. The text of the article is reproduced below:

*"(1) A party is not liable for a failure to perform any of its 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.*

*(2) 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.*

*(3) The exemption provided by this article has effect for the period during which the impediment exists.*

*(4) The party who fails to perform must give notice to the other party of the impediment and its effect on his ability to perform. If the notice is not received by the other party within a reasonable time after the party who fails to perform knew or ought to have known of the impediment, he is liable for damages resulting from such non-receipt.*

*(5) Nothing in this article prevents either party from exercising any right other then to claim damages under this Convention."*

Article 79 of the CISG exempts a party from liability to pay damages in case of non-performance of the contract caused by an *impediment beyond the party's control.* The essential ingredients for the exemption of liability are stated in Article 79(1) which establishes the impediment as a prerequisite for invoking the article. However, the term "impediment" has not been defined under the Convention. This leads to ambiguity in the Article and opens the debate into the scope of exemptions offered under it.

Clearly, the terms "hardship" or "economic difficulty" do not appear in this provision. The term actually used, i.e. "impediment" leaves significant room for interpretation. Therefore, several legal commentators have been extensively been attempting to interpret this "vague and imprecise"[5]

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[5] Joern Rimke, 'Force Majeure and Hardship: Application in International Trade Practice with Specific Regard to the CISG and the UNIDROIT Principles of International Commercial Contracts', REVIEW OF THE CONVENTION

provision with the intention to bring finality to the ongoing debate as to the inclusion of the principle of hardship or economic duress within the ambit of the aforementioned Article.

The most widely accepted view has been in favor of the wider interpretation of Article 79(1), which collides with the **CISG AC Opinion No.7**, that accepts and advocates the inclusion of *"changes in circumstances"* within the meaning of the term "impediment" and therefore, including the situations of non-performance due to economic circumstances resulting in the performance excessively onerous. A plethora of scholars, including Professor Bonell analyzing and understanding the wording of Article 79 of the CISG to reach a conclusion, stated that the terms *"impediment"* and the wording *"could not reasonably be expected . . . to have avoided or overcome it or its consequences"* conclusively show that change in circumstances that do not make the performance of the obligations under the contract strictly impossible, in other words, change in circumstances that fall short of impossibility can also be unforeseeable and unreasonable to enforce and therefore, it can reasonably be deduced that the concept hardship is well within the scope of Article 79.[6]

The competing and opposite argument states that there is an impending risk inherent in international commercial transactions, and for this reason, no situation or change in circumstance short of impossibility would satisfy the provisions of Article 79, and therefore, the concept of hardship cannot be read within the purview of Article 79. With the changing times, internationally accepted instruments like the CISG need to be analyzed in a dynamic manner as they are not likely to be redrafted and that is not even practical. There has been a growing judicial trend to read hardship within the purview of the provisions of Article 79.

However, due to a plethora of unsettled and inconsistent decisions supporting both the arguments, the goal of uniformity of interpretation and standardized application of the CISG becomes difficult and undermined. Therefore, to achieve international harmony while applying the CISG, adjudicators are required to consistently apply Article 79 without being swayed by or relying on any particular domestic legal systems. Meanwhile, the CISG advisory council and the various scholars should endeavour to promote the harmony and uniformity and standardisation in the interpretation of Article 79, instead of varied opinions and fragmented application.

## CLAIMING EXEMPTION UNDER ARTICLE 79

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ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS (CISG) (PACE INT'L L. REV. eds., 1999–2000) 197, 218.

[6] Michael J. Bonell, 'Force Majeure e Hardship Nel Diritto Uniforme Della Vendita Internazionale', DIRITTOD DEL COMMERCIO INTERNAZIONALE 570 (1990) (It.).

In international commercial contracts governed by the provisions of the CISG, the non-performing party, that is the party that fails to complete their part of the duties as they are contractually obligated to perform may be liable to pay certain damages to the other party. The CISG grants an exemption from damages in certain exceptional and extraordinary circumstances. To be granted such an exemption from the non-performance, the defaulting party is required to prove the following:

1. The existence of an impending impediment;
2. The impediment prevented the performance of the obligations of one party by making the performance excessively onerous;
3. The impediment was beyond the realm of control of the party;
4. The said impediment could not have been reasonably foreseen at the time of the conclusion of the contract; and,
5. The impediment could not have been in good faith and reasonably avoided or overcome.

## Impediment must be unforeseen

In practicality, it can be understood that impediments are somewhat foreseeable at some point, or to some extent all possible impediments are foreseeable at some level. It is pertinent to understand that the degree of foreseeability used in Article 79(1) does not denote an unimaginable or unthinkable or not even remotely possible situation or event. The foreseeability of an event has to be understood from the perspective of a rational third person. A situation would be determined and treated as an unforeseeable situation when even a rational and objective person would not have been able to foresee or even consider the possibility of the said situation arising at the time when the contract was being concluded.[7]

## Impediment beyond a party's control

Any event or change in circumstances that are caused due to overwhelming external obstacles are understood to be beyond the risks and obligations undertaken by the parties to the contract. It is, therefore, an essential requirement that is required to be fulfilled to be granted an exemption from damages. A mere denial or refusal to complete the contract cannot be treated as a relevant or acceptable ground for exemption. Thus, constituting a limit and assessing the extent of the risk undertaken by the parties is an intrinsic part of this essential.

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[7] Stephan Kroll, Loukas A Mistelis and Pilar Perales Viscasillas (eds), "Art 7', UN Convention on Contracts for the International Sale of Goods (CISG) Commentary' (Beck and Hart Publishing 2011),

The analysis of these limits is known as the sphere of risk. It specifies the risks that a contracting party has to undertake. These generally do not constitute impediments within the scope and ambit of Article 79.[8] Thus, these impediments that are directly within the "sphere of risk" would constitute an impediment only in some extraordinary and exceptional cases.

### Unavoidability

There is a general obligation to fulfill all the terms agreed upon under the contract if their performance is even remotely possible. This principle is called *pacta sunt servanda.* Thus, this obligation includes the duty to offer a commercially viable and objectively reasonable substitute if that is possible, further, to also bear the additional and overhead costs that might have been incurred to overcome such circumstances. In cases of economic impediments, this requirement (*i.e. unavoidability)* and the requirement of the impediment being beyond the party's control are interconnected. Thus, the sphere of risk or the limit of risk allocation determines the action that the party has to undertake to fulfill the contract. This is an essential requirement to assess economic impediments under Article 79.

## EXISTENCE OF AMBIGUITY

Article 79(1) CISG forms the basis for exemption from liability to pay damages in cases where performance becomes onerous for one party. However, the CISG scholars have been divided on the question of whether this article would cover situations of hardship. The term "hardship" has not been used in the article and thus the difficulty and ambiguity as categorizing hardship as an impediment occurs.

Professor Schwenzer has pointed out that those changes that are unforeseeable in circumstances that alter the economic equilibrium of a contract between the parties are one of the biggest problems that parties to an international commercial contract face and thus, there is a need to clarify this ambiguity.[9]

There have been a plethora of academics who have analyzed the provisions of this Article. In their distinct and various analyses, the differing opinions about the existence of a hardship defence under the provisions of Article 79 of the CISG have been expressed. The CISG Advisory Council

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[8] Ingeborg Schwenzer, 'Force Majeure and Hardship in International Sales Contracts', 39 VICT. U. WELLINGTON L. REV. 709 (2009).

[9] Ingeborg Schwenzer, 'Force Majeure and Hardship in International Sales Contracts', 39 VICT. U. WELLINGTON L. REV. 709 (2009).

thus tried to clarify and reduce the ambiguity in this Article through its AC Opinion No. 7 of October 2007, stating that:

> *"A change of circumstance that could not reasonably be expected to have been taken into account, rendering performance excessively onerous, may qualify as an "impediment" under article 79(1). . . . Therefore, a party that finds itself in a situation of hardship may invoke hardship as an exemption from liability under article 79"*[10]

As one of the CISG's most challenging and important provisions, Article 79 attempts to explain and lay down laws for when a contracting party should be exempted from liability for damages resulting from failure to perform and/or fulfill a contractual obligation. With the intention, *"that Article 79 would establish its own autonomous definition of impediments beyond a party's control"*[11] the drafters of the CISG intentionally avoided the use of various familiar legal terms that are widely used and accepted in a plethora of domestic legal systems such as *force majeure*, *wegfall der geschäftsgrundlage*[12], *impossibility, eccessiva onerosità sopravvenuta*[13], and *impracticability* in favour of *"terminology neutrality"*.

In this way, Article 79 attempts to bridge and consolidate the various domestic legal doctrines of the different signatory states.[14] However, the vague language of the Article intended to bring uniformity to different domestic legal terms has caused ambiguity and ironically lack of uniformity in Article 79.

The terminology used in Article 79 often leads to the interchangeable use of the principle of force majeure and impediment. Both these concepts are separate and distinct as the situations of impediments vary in different domestic and international scenarios and in their analysis of the principle of force majeure. Force majeure is applied in a strict sense and refers to situations practical impossibility whereas impediment is often understood to be applied in a much more flexible manner. Thus, it can be concluded that the concept of Impediment lies somewhere in between the principles of force majeure and hardship.[15]

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[10] CISG AC Opinion No 7 Exemption of Liability for Damages Under Article 79 of the CISG (Rapporteur: Professor Alejandro Garro) 12 Oct 2007, Opinion 3.1 [CISG AC Opinion No 7]

[11] Camilla Baasch Andersen, 'UNIFORM APPLICATION OF THE INTERNATIONAL SALES LAW. UNDERSTANDING UNIFORMITY, THE GLOBAL JURISCONSULTORIUM AND EXAMINATION AND NOTIFICATION PROVISIONS' (2007) 94.

[12] Germany's domestic hardship principle. "Wegfall der geschäftsgrundlage" roughly translates to "elimination of the basis of the business transaction."

[13] The Italian adoption of Germany's wegfall concept, eccessiva onerosità sopravvenuta roughly translates to an excessively burdensome supervening event. Mazzacano, at 46.

[14] Professor John Honnold, one of the drafters of the CISG, opines: "Article 79 may be the least successful part of the half-century of work towards international uniformity." UNIFORM LAW FOR INTERNATIONAL SALES UNDER THE 1980 UNITED NATIONS CONVENTION, 425 (ed. H. M. Flechtner 2009).

[15] KP Berger, 'The Creeping Codification of the Lex Mercatoria', (The Hague: Kluwer Law International, 1999).

## WORDING OF ARTICLE 79 ALLOWS FOR HARDSHIP

The wording of the article was specifically chosen in place of the term *"impossibility"* by the working group so as render the article less restrictive. The wording talks about "failure to perform due to an impediment beyond his control", it thus, highlights that there is an element of an outside force that precludes the performance of the obligations.

The learned Professor John Honnold opined that there is a need or a requirement for *an element of causation*, this element must be of such a magnitude that it actually hinders the performance of the contract.[16] He further stated that the working group excluded the term that incorporated economic impossibility within its scope, i.e. "frustration" within the article since they were of the opinion that *"an extreme and unforeseeable change in economic circumstances"* that prevents performance would qualify the requirements of Article 79. Thus, the working group concluded and understood that the term "impediment" would in fact incorporate situations of economic hardship.[17]

To read the concept of hardship within the ambit of Article 79, the competing arguments have to be rebutted. The most prevalent argument that is advocated to remove hardship from the ambit of Article 79 is that the "drafting history of the convention indicates that the term and the concept of hardship were intentionally excluded and it was concluded that hardship does not fall within the "insurmountable obstacle" aspect of "impediment". However, the *travaeux prepatoire* indicates that there were no conclusive or in-depth discussions regarding the inclusion or exclusion of hardship from the Article. Thus, hardship cannot be refused to be incorporated within the ambit of the Article by merely relying on the drafting history of the article.

Moreover, the term "impediment" has not been conclusively defined in the CISG, thus, to relate this term to actual and absolute impossibility is not justified. "A situation or an event that renders the performance of the contract excessively difficult or onerous could also be treated to be an "impediment".

The Judicial trend and the general understanding of Article 79 used to denote that there is no room for the concept of hardship within the Article.[18] However, there has been a growing acceptance and inclination towards accepting hardship as a part of the terminology "impediment" within Article 79. There have been a number of cases as well as articles and publications by various

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[16] J. Honnold, 'UNIFORM LAW FOR INTERNATIONAL SALES UNDER THE 1980 UNITED NATIONS CONVENTION' 427.
[17] Ibid.
[18] Hans Stoll in Peter Schlechtriem (ed) 'Commentary on the UN Convention on the International Sale of Goods' (2ed, Clarendon Press, Oxford, 1998).

eminent scholars [19]stating that the wording of Article 79 does include situations of changed circumstances that make the performance of the contract excessively financially onerous for a party. Thus, it does include hardship within its ambit. This view is gaining even wider acceptance with an intention to achieve unity in its application.

Although hardship can be read into the wording of Article 79, not every change in circumstance would be exempted. The underlying intent that can be derived from other articles and clauses of the convention is the principle of *pacta sunt servanda*.[20] Therefore, merely because the performance of the contract has become onerous for one party due to events that could have been anticipated at the time of the conclusion of the contract, would not qualify as an exemption under Article 79.[21] A situation would warrant the application of "hardship" under the article if the performance is rendered excessively onerous[22] and the equilibrium is fundamentally altered.

The essentials for a situation to qualify as a hardship situation are similar to those for the application of the concept of force majeure. The *circumstance must not have been foreseeable and avoidable and should not be within the sphere of risk of the party* asking for the exemption. Therefore, it can be stated that hardship forms a subset of special cases under the general force majeure exemption. Thus, the term "impediment" can be clarified in light of the interrelation between these two concepts to denote the change in circumstances that render the performance excessively burdensome and onerous, although possible.

However, Article 79 does not directly or conclusively deal with the concept and defence of hardship. Therefore, even though there is scope in article 79 to cover the situations of hardship,

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[19] CISG AC Opinion No 7, 'Exemption of Liability for Damages Under Article 79 of the CISG (Rapporteur: Professor Alejandro Garro)' 12 Oct 2007, Opinion 3.1 [CISG AC Opinion No 7]; Schwenzer in Schlechtriem and Schwenzer (eds), Article 79 para 4; Niklas Lindström "Changed Circumstances and Hardship in the International Sale of Goods" (2006) (Issue 1) Nordic Journal of Commercial Law 23-24.

[20] Principles of International Commercial Contracts, Article 6.2.1; Principles of European Contract Law, Article 6:111(1); Draft Common Frame of Reference Article III – 1:110 [Draft Common Frame of Reference]; ICC Hardship Clause 2003 para 1 ; Joern Rimke "Force Majeure and Hardship: Application in International Trade Practice with Specific Regard to the CISG and the UNIDROIT Principles of International Commercial Contracts" Pace International Law Review (ed) Review of the Convention on Contracts for the International Sale of Goods (CISG) 1999-2000 (Kluwer, The Hague, 2001) 237.

[21] Ingeborg Schwenzer in Peter Schlechtriem and Ingeborg Schwenzer (eds) Kommentar zum einheitlichen UN Kaufrecht CISG (5 ed, CH Beck, Munich, 2008) Article 79, Para. 4

[22] Peter Schlechtriem, 'Uniform Sales Law: The UN-Convention on the International Sale of Goods' (Manz, Vienna, 1986) 102; Ulrich Magnus, 'J von Staudingers Kommentar zum Bürgerlichen Gesetzbuch mit Einführungsgesetzen und Nebengesetzen, Wiener UN-Kaufrecht (CISG)' (15 ed, Sellier, Berlin, 2006) Article 79 para 4; Dietrich Maskow, 'Fritz Enderlein, Dietrich Maskow and Heinz Strohbach (eds) Internationales Kaufrecht' (Haufe, Berlin, 1991) Article 79 para 6.3; Joseph Perillo 'Force Majeure and Hardship Under the UNIDROIT Principles of International Commercial Contracts' (1996) 5 Tul J Int'l & Comp L 1, 9; Jennifer Bund 'Force Majeure Clauses: Drafting Advice for the CISG Practicioner' (1998) 17 J L & Com 381, 389.

the consequences of hardship, and how to overcome these situations have not been conclusively dealt with.

## THRESHOLD FOR HARDSHIP

The foremost question while dealing with situations of hardship is whether the change in circumstance is beyond the *threshold of hardship*. It is pertinent to analyse whether the performance of the contract has become excessively onerous or whether there has been a fundamental alteration of equilibrium.[23] The threshold of hardship is also referred to as the "limit of sacrifice".[24] The limit of sacrifice is an acceptable international standard. The CISG advisory council while relying on it has stated:

*"economic impossibility which, while short of an absolute bar to perform, imposes what in some legal systems is conceptualized as a "limit of sacrifice" beyond which the obligor cannot be reasonably expected to perform."*

Thus, for a situation to qualify as hardship under the CISG, the alteration of the equilibrium has to go beyond the limit of sacrifice. For this, from the point of view of the seller, the decrease in the value of the performance of the obligations is relevant, and from the point of view of the buyer, the increase in the cost of performance of the obligations is relevant.

The next relevant consideration, while determining if the change in circumstance that led to the alteration of the equilibrium, actually amounts to a situation of hardship or not is to be ascertained by analysing the facts and circumstances of each individual case. Therefore, the *duration of the international commercial contract*, that is, short term or long term, would be an essential consideration.[25] Another important consideration to determine a case of hardship is the profit margin of the contract. Further, it is pertinent to note, that this threshold for hardship can be lowered in situations where it is imminent that the defaulting party would go into financial ruin.[26]

However, to remove any ambiguity in the application and interpretation of this threshold, and foster a sense of legal clarity, there has to be a clear benchmark for hardship. A few CISG scholars

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[23] Christoph Brunner, 'Force Majeure and Hardship Under General Contract Principles: Exemption of Non-Performance in International Arbitration' (Kluwer Law International, The Hague, 2009) 221-223.
[24] Schwenzer, Ingeborg (Ed.), 'Commentary on the UN Convention on the International Sale of Goods (CISG)', 3rd ed., Oxford University Press, Oxford 2010, p. 1076.
[25] Christoph Brunner, 'Force Majeure and Hardship Under General Contract Principles: Exemption of Non-Performance in International Arbitration' (Kluwer Law International, The Hague, 2009).
[26] Christoph Brunner, 'Force Majeure and Hardship Under General Contract Principles: Exemption of Non-Performance in International Arbitration' (Kluwer Law International, The Hague, 2009) 438-439.

relying upon domestic trends and their application opined that this benchmark or *threshold should be a **100 percent alteration** of the equilibrium.* [27]

However, it is pertinent to note, in situations of price fluctuations, arbitral tribunals while dealing with cases where the interpretation of Article 79 is needed have not been in favour of allowing for hardship.[28] Although, this determination seems to be an extremely endeavour to achieve as the benchmark would depend upon a number of fluctuating and individual circumstances including, dispute resolution methodology opted for, the contract entered between the parties, as well as the arbitrator's legal background and understanding. Even so, the 100 percent benchmark has become a general rule of thumb with the evolving international commercial contracts.[29]

However, a number scholars are also of the view that in considering the international market conditions, the increased risk in such situations and the possibility of parties to generally ask for an adjustment of the price of the contract, it would be more appropriate and relevant to set a higher point of the threshold. The judicial approach in international commercial arbitrations while dealing with cases of alteration of the equilibrium due to increase in price by a meager 10 percent to 50 percent, has been to reject the hardship exemption in such situations. An increase up to around 50 percent is considered to be insufficient to grant exemption from performance in an international commercial market.[30]

The intention of the tribunals and courts while dealing with international commercial cases, to grant this exemption is quite hesitant. The general opinion and approach are, that the parties to international contracts of sale undertake a greater threshold of risk than the parties to a domestic sales contract.

In ***ICC Award No. 8486***, where due to severe fluctuations in the exchange rate, the price of the goods dropped to a large extent. Consequently, the buyer stated that the exemption of hardship

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[27] Ibid, 428-435; Christoph Brunner, 'UN-Kaufrecht – CISG, Kommentar zum Übereinkommen der Vereinten Nationen über Verträge über den internationalen Warenkauf von 1980, unter Berücksichtigung der Schnittstellen zum internen Schweizer Recht' (Stämpfli, Bern, 2004) Article 79 CISG para 26.

[28] *ICC Award,* 26 Aug 1989, No 6281, CISG-online 8; *Tribunale di Monza*, 14 Jan 1993, CISG-online 540; Joseph Lookovsky, 'Impediments and Hardship in International Sales: A Commentary on Catherine Kessedjian's 'Competing Approaches to Force Majeure and Hardship''(2005) 25 Int'l Rev L & Econ 434, 438.

[29] *CIETAC*, 10 May 1996, No 21, CISG-online 1067; *Bulgarian Chamber of Commerce and Industry*, 12 Feb 1998, No 11, CISG-online 436; *Rechtbank van Koophandel, Hasselt*, 23 Feb 1994, No 1849, CISG-online 371; *Cour d'Appel de Colmar*, 12 Jun 2001, CISG-online 694; *Cour de Cassation*, 30 Jun 2004, No 964, CISG-online 870.

[30] Zaccaria, E. C., 'The Effects of Changed Circumstances in International Commercial Trade' International Trade & Business Law Review. 2005, 9: 169; Brunner C., 'Force Majeure and Hardship under General Contract Principles. Exemption for Non-Performance in International Arbitration' Kluwer Law International, 2009, p. 428−431; Houtte van, H., 'The UNIDROIT Principles of International Commercial Contracts and International Commercial Arbitration: Their Reciprocal Relevance' ICC Publication No. 490/1. Paris: International Chamber of Commerce, 1995, p. 190.

should be granted to him. The tribunal held that *"in international commerce one must rather assume in principle that the parties take the risk of performing and carrying out the contract upon themselves, unless a different allocation of risk is expressly provided for in the contract."*[31]

Moreover, the judicial approach states that changes in an international commercial scenario are not entirely unforeseeable and thus, parties should not be exempted from the performance or the consequences of non-performance. In international arbitration[32], the International Chamber of Commerce opined that the application of hardship to exempt a party from the consequences of non-performance. It was stated that *"caution is especially called for in international transactions where it is generally much less likely that the parties have been unaware of the risk of a remote contingency or unable to formulate it precisely."* Another CISG scholar has opined that in international commercial markets *"the risk of hardship is virtually inevitable in the field of international trade, as the economic and political context is subject to continual flux and rapid change."*[33] The suggested higher benchmark for hardship is ***150-200 percent***.[34]

## Alternative Criteria for Threshold

In international trade, there arise certain situations where the general benchmark set in numeric terms is not enough to analyse the applicability of the hardship exemption. There are situations where the circumstances warrant analysis of determinants other than the numeric benchmark. These situations might be:

i. The change in equilibrium cannot be measured numerically;
ii. The alteration of the equilibrium is numerically measurable, but the threshold has to be significantly lowered;
iii. The change in the value of the contract is indirect.

However, this list is not exhaustive. Hardship is a fairly flexible concept and thus, there can be numerous situations where alternative determinants have to be relied upon.

[31] ICC Award No. 8486 of 1996, 1999 Y.B. Comm. Arb. 162 (ICC Int'l Ct. Arb.).
[32] ICC Award No. 1512 of 1971, SIGVARD JARVIN & YVES DERAINS, COLLECTION OF ICC ARBITAL AWARDS 3 (1990)
[33] Elena C. Zaccaria, 'The Effects of Changed Circumstances in International Commercial Trade', 9 INT'L TRADE & BUS. L. REV. 135, 136 (2004).
[34] Hans Stoll and Georg Gruber in Peter Schlechtriem and Ingeborg Schwenzer (eds), '*Commentary on the UN Convention on the International Sale of Goods* (2 English ed, Oxford University Press, Oxford, 2005) Article 79' paras 10-24.

# THE GAP IN THE CISG ARTICLE 79

## Hardship as an Internal Gap in the CISG

The scope of the convention, as aforementioned has been outlined by Article 4 of the CISG. It provides that the scope of the convention covers only the rights and obligations of the parties to the international commercial contract and the formation of the contract. It is pertinent to note that the term *"rights and obligations of the parties to the contract"* has not been exhaustively defined.[35] This ambiguity leaves ample space in the convention to govern situations of hardship, which is a right of the party to get the exemption in a situation when the performance of the contract becomes excessively onerous.[36]

The evolution of Article 79 of the CISG is a pertinent aspect that had to be analysed to see whether hardship constitutes a gap within its ambit[37]. Professor Honnold, a renowned CISG scholar has opined, that the word "impediment" was categorically used in place of the term "circumstances" so as to not include situations that make the performance of the contract within the scope of the said article. However, the growing opinion has been that the circumstances that constitute or should be eligible for exemption from liability in situations of non-performance cannot be seen from a strict force majeure point of view while maintaining that the article has to still be interpreted somewhat narrowly.[38]

CISG scholars have agreed that even within this narrow understanding of the article and the term impediment, the changes in circumstances that are completely unexpected and create an unreasonable burden on a party would constitute an impediment. This growing acknowledgment has created a view that certain situations that are not completely dealt with in the article, might constitute a part of it. All these situations would thus constitute internal gaps.

Another reason to include hardship within Article 79 of the CISG is to avoid the varied interpretation and usages of several domestic legal systems to deal with such situations.

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[35] Peter Schlechtriem and Ingeborg Schwenzer (eds), "Art. 7', *Commentary on the UN Convention on the International Sale of Goods (CISG)'* (Second edition, Oxford University Press 2005)., p. 103.

[36] UN Convention on Contracts for the International Sale of Goods (CISG),Commentary, Kröll, Mistelis, Perales Viscasillas (eds), Published by C.H. Beck Verlag, Co-published by Hart Publishing, 2010.

[37] K. Boele-Woelki, 'Principles and Private International Law—The UNIDROIT Principles of International Commercial Contracts and the Principles of European Contract Law: How to Apply Them to International Contracts' 4 UNIFORM L. REV. 651 (1996) (general overview of PICC and PECL), p. 483.

[38] Peter Schlechtriem, '100 Uniform Sales Law - The UN-Convention on Contracts for the International Sale of Goods 100 (1986)'
http://cisgw3.law.pace.edu/cisg/biblio/schlechtriem-79.html (analysis of Article 79) (Schlechtriem, Uniform Sales Law).

Therefore, it can be clearly concluded that situations of hardship are covered and a part and parcel of Article 79 of the CISG.[39] However, since these situations are not conclusively settled and the remedies of it are also vague and unsettled. It creates a gap in the convention, and such a gap is an ***internal gap***. This internal gap in the CISG has been recognised by a plethora of articles and scholarly writings.[40][41]

## FILLING THE HARDSHIP GAP

To fill the gap in Article 79 of the CISG, first, the principles underlying the Convention on which the CISG is based has to be resorted to, then by turning to applicable international rules or domestic legal systems. To find the underlying principles of the convention, ***Article 7(1)*** has to be applied and the ***principle of good faith*** is to be applied. Another possibility is to analyse ***Article 79(5)*** to understand how courts and tribunals interpret these articles to provide remedies for situations of hardship. The main determination in regard to fining the remedies would be to determine what the parties respectively owe each other and then accordingly ***adapt the contract.*** However, this has to be with extreme caution so as to maintain the uniformity in the international application of the CISG.

A number of CISG scholars and arbitral awards and decisions have recognised[42] and follow the ***principle of good faith and the principle of fair dealing*** as an underlying principle which forms the basis of CISG. There are a few principles that can be regarded as fundamental principles. It is pertinent to note, that these principles also in themselves, contain the principle of good faith. Thus, the principle of good faith is one of the most important principles underlying the convention and it has been relied upon in the process of interpretation of Article 79 to fill the hardship gap.

The internal gaps of the convention that cannot be substantially and conclusively be filled by the application of Article 7(1) and the general principles underlying the convention, the principles of

[39] Ingeborg Schwenzer, 'Force Majeure and Hardship in International Sales Contracts' 39 VICTORIA UNIV. WELLINGTON L. REV. 709 (2009).
[40] Stefan Kröll, Loukas A Mistelis and Pilar Perales Viscasillas.
[41] Joseph Lookofsky, 'Walking the Article 7(2) Tightrope between CISG and Domestic Law' [2005] Journal of Law and Commerce 87, p. 101.
[42] Ferrari, 'Schlechtriem/Schwenzer (eds.), Kommentar zum Einheitlichen UN-Kaufrecht – CISG –, 5th ed., Munich 2008, Art. 7' no. 43; Schlechtriem, in: Schlechtriem/Schwenzer (eds.), Commentary on the UN Convention on the International Sale of Goods (CISG), 2nd English ed., Munich 2005, Art. 7, no. 8 and 27 et seq., Art. 7, no. 30; Magnus, Die allgemeinen Grundsätze im UN-Kaufrecht, (1995) 59 Rabels Zeitschrift für ausländisches und internationales Zivilrecht (RabelsZ), 485; Rosenberg, The Vienna Convention: Uniformity in Interpretation for Gapfilling – An Analysis and Application, (1992) 20 Australian Business Law Review (Aust Bus Law Rev), 443. Cf. also Gebauer, Uniform Law, General Principles and Autonomous Interpretation, Uniform Law Review (ULR) 2000, 696; Honnold, Uniform Words and Uniform Application. The 1980 Sales Convention and International Juridical Practice, in: Schlechtriem (ed.), Einheitliches Kaufrecht und nationales Obligationenrecht, Baden-Baden 1987, 138 et seq.

private international law have to be resorted to as has been denoted in ***Article 7(2)*** of the CISG. There are numerous sets of rules and principles that could be relied upon to fill the gap in Article 79 of the convention. The most universally used and applied to be the UNIDROIT Principles of International Commercial Contracts (*UNIDROIT Principles*).[43] The Preamble of the UNDRIOT PICC states that *"they may be used to interpret or supplement international uniform law instruments".*[44]

The lacuna in Article 79 of the CISG can be best filled by the ***UNIDRIOT PICC*** according to the provisions of Article 7(2) of the CISG. Thus, the basic relationship between the UNIDROIT PICC and the CISG is to provide the most appropriate and solution for the *"questions concerning matters governed by CISG which are not expressly settled in it"* and provide the mechanism for the remedy that could be utilized for the situations that are not completely covered by the CISG.[45]

***Article 6.2.2*** of the UNIDROIT Principles deals with situations of hardship and states:

*"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."*

The concept of hardship, as it appears in the aforementioned article, is a complex one. This is because the said article besides defining the concept of hardship, further states all other factors that have to be taken into account to make a situation come within the legal threshold of hardship. The legally relevant hardship thus, requires that there must have been *"the occurrence of events*

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[43] *Principles of International Commercial Contracts*. Rome: International Institute for the Unification of Private Law (UNIDROIT), 2010.
[44] CM Schmitthoff, The Export Trade – The Law and Practice of International Trade (4th edn, London: Stevens & Son Limited, 1962).
[45] Joern Rimke 'Force Majeure and Hardship: Application in International Trade Practice with Specific Regard to the CISG and the UNIDROIT Principles of International Commercial Contracts' Pace International Law Review (ed) Review of the Convention on Contracts for the International Sale of Goods (CISG) 1999-2000 (Kluwer, The Hague, 2001) 197, 219.

*fundamentally altering 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".*[46]

The intent and the purpose, as it has been established, of Art. 79 CISG and Art. 6.2.3 of the UNIDROIT PICC is identical. This was also seen in the landmark case of ***Scafom International v. Lorraine Tubes SA.*** The Belgian Supreme Court reiterated the approach of hardship within art. 79. It, however, identified a gap in the article pertaining to the remedies of hardship. In order to fill this gap, the court looked towards Art. 6.2.3 of the UNIDROIT to provide the remedy of renegotiation.

In ***Scafom International v. Lorraine Tubes SA***, the parties concluded a contract for the purchase of steel tubes. After the contract was finalized, and before the goods were delivered, the market price of steel suddenly rose 70%. This meant a significant loss for the seller, which is why the seller tried to renegotiate the contract terms under hardship, but the buyer nevertheless insisted on the delivery of steel tubes according to the agreed conditions.[47]

In its reasoning, the Belgian Supreme Court stated:

> *"changed circumstances that were not reasonably foreseeable at the time of the conclusion of the contract and that are unequivocally of a nature to increase the burden of performance of the contract in a disproportionate manner, can, under circumstances, form an impediment in the sense of this provision of the Convention."*

By referring to the remedies of the UNIDROIT Principles, the Court of Cassation became the first court to signify the existence of hardship through market fluctuations in the CISG.[48]

Under the UNIDROIT Principles, hardship is defined to provide relief even if the party's performance remains possible. This is when post-contract developments fundamentally affect the equilibrium of the balance of the power between the contracting parties. In particular, economic impediments constitute hardship if the cost of performance has increased under article 6.2.2 of the UNIDROIT Principles. The relief that a party can claim from hardship is the requirement that the parties renegotiate the terms of the agreement to restore the original contractual equilibrium. If this fails, the court may adopt or terminate the contract without the explicit consent of the

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[46] Franco Ferrari, '*Uniform Interpretation of the 1980 Uniform Sales Law*' 24 GA. J. INT'L&COMP. L. 225 (1994-1995); Franco Ferrari, '*General Principles and International Uniform Commercial Law Conventions: A Study of the 1980 Vienna Sales Convention and the 1988 UNIDROIT Conventions on International Factoring and Leasing*' 10 Pace Int'l L. Rev. 157, 162 (Summer, 1998).
[47] *Scafom International v. Lorraine Tubes S.A.*
[48] Amalina Tajudin, 'Scafom International BV v Lorrain tubes S.A.S: A Case Review of Changing Circumstances under the United Nations Convention on International Sale of Goods (CISG) of 1980' (2014) 4(2) Juridical Tribune 211, 215.

parties. Referring back to Scafom International BV, the Supreme Court had applied the relief provided in the UNIDROIT Principles, as article 79 does not allow for explicit relief under 79(5).

The criteria of hardship defined in article 6.2.2 partly reflect the criteria that are given under Art. 79 CISG with reference to article 6.2.2(b) *'the events could not reasonably have been taken into account by the disadvantaged party at the time of the conclusion of the contract'* and (c) *'the events are beyond the control of the disadvantaged party.'*

Therefore, UNIDROIT PICC can be conclusively be used to fill the gap that is prevalent in Article 79 of the CISG with respect to the remedies of hardship.

## CONCLUSION

In international commercial contracts and general international transactions, the parties are oftentimes governed and regulated by one of the international instruments governing trans-boundary trade. In the fulfilment of these transactions and obligations under the contract, sometimes impediments arise that make the performance of the obligations agreed under the contract impossible or commercially impracticable. These change in circumstances lead to two situations: force majeure or hardship.

Hardship is a development of the concept of Force Majeure. With the growth of trade, globalisation and increasing importance of trans-boundary contracts, force majeure emerged as inadequate with led to the emergence of hardship. Hardship refers to situation which makes the performance of the legal obligations of a party under a contract excessively onerous due to unforeseen circumstances which cannot be overcome. The principle of hardship depends on the *equilibrium of power*. The parties of a contract are assumed to be at an equal footing so as to make the contract valid. Whenever a situation that fulfils the criteria alters this equilibrium to a disadvantage of a party, hardship is said to arise.

Article 79 of the CISG covers situations of impossibility of performance and the defence from non-performance. This Article covers the situations of hardship. The essentials of hardship are evident as, foreseeability at the time of conclusion of the contract, makes performance excessively onerous; and, cannot be reasonably avoided. The key point of distinction between hardship and force majeure is that while force majeure makes the performance impossible, hardship simply makes it *excessively onerous.*

These different and varied impediments do not always result in the performance of the contract or the remaining obligations under it becoming completely and actually physically impossible. These impediments result in imposing an excessive burden upon the promisor in the performance

of the obligations that are contracted for. Thus, in these situations the parties in good faith are not required to perform the contract simply because the performance of the contract is still possible. Therefore, because of the similarity of these defences and the changes in international trade, the concept of hardship is understood to be incorporated within the ambit of the CISG.

Article 79 is an exemption from liability clause under the Convention. As its title suggests, it is a Force Majeure Clause which allows a party to plead non-performance in case of an impediment as given under the Article. Clearly, the terms *"hardship"* or "*economic difficulty"* do not appear in this provision. With the changing times, internationally accepted instruments like the CISG need to be interpreted in a dynamic manner as they are not likely to be redrafted and that is not even practical. There has been a growing judicial trend to read hardship within the provisions of Article 79.

There is an internal gap in this article regarding the remedies of hardship. This gap is to be filled by using the UNIDROIT PICC. The provisions and the mechanism of remedies are thus, best incorporated in the CISG by resorting to the hardship provisions under the UNIDROIT PICC. The UNIDROIT Principles provide a uniform scheme for the solutions that are to be adopted to deal with situations of hardship.

According to Article 6.2.2 of the UNIDROIT PICC, the remedy for hardship is a renegotiation and the adaptation of the contract. Therefore, it can be categorically concluded that Article 79 of the CISG does cover situations of hardship within the meaning of the term impediment. However, there is a gap in the provision regarding the remedies available for them. This gap has to be filled by applying the provisions of Article 6.2.2 of the UNIDROIT PICC. The UNIDROIT PICC provides that the parties ought to renegotiate the contract to provide for the changed circumstances and equalise the equilibrium of the contract that had been altered.