Science of Law Journal (2023)
Clausius Scientific Press, Canada

DOI: 10.23977/law.2023.020202
ISSN 2616-2296 Vol. 2 Num. 2

Basic Legal Framework of Hardship Clause and Comparative Research

Jing Zhou

Università degli Studi di ROMA "La Sapienza", Rome, Italy

Keywords: Hardship clause, force majeure, change of situation, PICC

Abstract: The hardship clause is a specific application of the principles of fairness and good faith in contractual relations, and has always played an important role in international commercial trade. The hardship clause intends to exclude manifestly unfair outcomes in contracts resulting from significant changes in the political, economic or social situation, reflecting fairness and justice. This article outlines the legal framework and functions of hardship clause, briefly compares hardship and force majeure, and accordingly elaborates on the equivalent concept of "change of situation" in Chinese law.

1. Introduction

In the case C.07.0289.N decided by the Belgian Appeals Court on June 19, 2009, the price of steel unexpectedly increased by 70% after the buyer and seller entered into a contract for the sale of steel pipes.[1] The contract did not contain a price modification clause. The Belgian Appeals Court, citing the hardship clause in the UNIDROIT Principles for International Commercial Contracts (hereinafter referred to as PICC), held that the balance of interests in the contract had been fundamentally upset in this case and upheld the buyer's claim for renegotiation of the terms of the contract.

The hardship clause invoked by the Belgian Appeals Court in the above-mentioned case is systematically provided for in the PICC, which is a collection of international commercial contract legislation. The hardship clause is a specific application of the principles of fairness and good faith in contractual relations, and has always played an important role in international commercial trade.

2. Overview

2.1 Background and theory development

The Hardship clause was originally introduced by the German courts because of the severe inflation in Germany which made the performance of the contract on the original terms extremely unfair to one of the parties, and therefore the courts could provide relief for hardship based on the principle of good faith in the Civil Code.

It can be seen that the hardship clause is designed for the performance of long-term contracts such as construction or installation, periodic supply or cyclical services, etc. The parties may encounter difficulties in the performance of the contract due to significant changes in political,

economic or social circumstances, and they may be forced by their economic situation to continue the contractual relationship and perform the contract, but wish to modify the contract according to the changed circumstances They may wish to continue the contractual relationship and perform the contract, but wish to modify the contract in light of the changed circumstances.

The Hardship clause has been developed to date, and there is much legislation in both legal systems that has adopted this doctrine.

French Civil Code (Art.1148) and Commercial Code do not recognize the concept of hardship. However, the French Supreme Court has started to move towards the recognition of the hardship regime. Many other civil law countries have embraced the hardship doctrine, such as Germany (Art.157, Art.242 BGB), the Netherlands, Italy, Greece, Portugal, Austria, and the Scandinavian countries.

English law does not contain any concept of hardship, however, exceptions are allowed in the case of frustration of contract. The American Uniform Commercial Code (UCC) has developed the general doctrine of impracticability, which is similar in general terms to the hardship clause.

The introduction of the exemptions in Article 79 of CISG is similar to that of hardship (but I don't think CISG really contains hardship clause). [2]

2.2 Definition

According to Art.6.2.2 PICC, the hardship clause means that the parties may request a change or release from their contractual obligations if they encounter unforeseen and uncontrollable contingencies in the course of performing the contract that fundamentally change the balance of interests between the parties.

The constituent elements of hardship conclude:

Hardship occurs after the contract is concluded and before performance is completed. When the contract is only partially performed, a fundamental imbalance of contractual interests occurs, and the hardship clause applies only to the part of the contract that has not yet been performed.

The disadvantaged party could not reasonably have anticipated the occurrence of the hardship at the time of the conclusion of the contract, and the hardship was beyond the control of the parties.

The hardship is a risk that should not be borne by the disadvantaged party. (Risks that should be borne by the parties to the contract are known as commercial risks.)

Hardship fundamentally alters the balance of contractual interests, either by substantially increasing the cost of contract performance, or by substantially reducing the value of contract performance or defeating the purpose of contract performance. Some scholars believe that the definition of "fundamental" may be based on a 50% standard.

2.3 Legal effects

Hardship relates only to the unfinished performance. If a fundamental change in the contractual equilibrium occurs only for part of the contractual obligations, then hardship is valid only for the part of the obligations that are still to be performed.

According to Article 6.2.3 of the PICC, the legal effects of hardship have procedural and substantive legal provisions. The procedural aspect includes renegotiation and access to the court, while the substantive aspect refers to the principles and obligations that the parties should follow in renegotiation and the court’ dealing with hardship situations.[3]

When there is already an automatic modification clause in the contract, a request for renegotiation cannot be made. However, the automatic modification clause in the contract must be set for a hardship situation, otherwise the parties' right to request renegotiation cannot be excluded.

The request for renegotiation should be made as soon as possible after the alleged hardship

occurs, together with a statement of the reasons on which it is based. An adverse party does not lose the right to request renegotiation because the request is delayed. A request that is not accompanied by a statement of reasons will be considered untimely unless the alleged hardship is obvious.

A request for renegotiation does not give the adverse party the right to cease performance of its contractual obligations. In Case 10021, arbitrated by the ICC Arbitration Tribunal, the Tribunal held that the adverse party due to hardship does not have the right to unilaterally declare the termination of the contract, and that he only has the right to submit to the court or the Arbitration Tribunal a modification of the contract or termination of the contract if the request for renegotiation to the other party is unsuccessful.

The process of renegotiation is subject to the general principle of good faith and the duty to cooperate. The parties must negotiate in a beneficial manner, in particular by excluding any obstructive forms and providing all necessary information.

The court may only modify the contract unless it is established that the hardship situation is justified. According to Clive M. Schmitthoff, the yardstick for a court to modify a contract is to adjust the initially designed contractual parity so that the interests of the parties are newly balanced, not simply averaged.

2.4 Function: an amendment to Pacta sunt servanda

As an exception to the principle of "Pacta sunt servanda" (which means the contract should be strictly observed) in contract law, the hardship system is an important safeguard to uphold the principle of fairness in contract law as an amendment to Pacta sunt servanda. [4]

Both the PICC and the Principles of European Contract Law (PECL) (Article 6.111) establish the principle of "Pacta sunt servanda", which states that a validly formed contract is binding on the parties. However, in some cases, sticking to the contract can cause extremely unfair consequences for the parties. In modern society, if the underlying situation at the time of contract formation is changed in a way that is unforeseen by the parties and cannot be attributed to them, and if the continuation of the contract will cause significant losses to one party while the other party gains unjustified benefits from it, it is obviously not in line with the law's desire to pursue In such cases, if the improperly positioned party is not allowed to modify or terminate the contract, it is obviously not in line with the fairness and justice that the law seeks.

In international commercial transactions, the hardship clause mainly solves difficulties in contract performance caused by abnormal changes in the economic environment, excludes manifestly unfair results caused by hardship, balances and coordinates the interests between the parties, and maintains social justice and economic flow order.

3. Relevant concepts

3.1 Comparison between hardship and force majeure

Hardship and force majeure are two types of performance hurdles that are clearly defined in the PICC (Art.7.1.7). In the real world of trading, hardship and force majeure are prevalent and to some extent intersect in the performance of contracts. However, there are differences in their historical origins, legal connotations, linkage distinctions and application of the law. Clarifying the differences in the legal effects of the two in their application is of great significance in facilitating the realisation of the purpose of the contract and the smooth conduct of the transaction.

There are significant differences between the two. [5]

Objective manifestations are different. Hardship generally manifests itself in the form of dramatic changes in the socio-economic situation affecting the performance of the contract. Force

majeure is generally manifested by catastrophic events that affect the contract, including those caused by natural forces, as well as abnormal actions of society.

Purposes are different. The purpose of a party invoking force majeure is to pursue an exemption from liability for its failure to perform the contract after the occurrence of the event, with the legal consequence of delayed performance or termination of the contract. The primary purpose of invoking hardship is to renegotiate the contract in order to restore the balance of interests between the parties, so that the modified terms of the contract will remain in force, with the ultimate goal of continuing to perform the contract.

Legislative intents are different. Hardship is designed to avoid manifest unfairness in the performance of a contract, and force majeure is designed to relieve the non-performing party from liability for damages in the event of a catastrophic failure to perform.

Hardship is often associated with long-term contracts and is not usually explicitly invoked in contracts. Force majeure is usually explicitly invoked in contracts and is more common in both short-term and long-term contracts.

Settlement procedures are different. The procedure for force majeure is relatively simple, as the party asserting force majeure only needs to give unilateral notice. A hardship claim, on the other hand, requires negotiation between the parties to the contract and even court intervention, which is much more complex.

Despite all the differences, there are objective situations where it is difficult to distinguish between hardship and force majeure, and in such cases the PICC allows the party affected by the incident the flexibility to choose a different claim, i.e. the parties can choose either one at will, depending on their purpose. This provision is very humane, because the choice to apply force majeure can avoid complicated procedures, saving time and money, but generally speaking the parties to the contract is to be able to successfully perform the contract, then you can choose hardship to achieve the desire.

3.2 “Change of Situation” in China

As a member of the UNIDROIT, China participated in the drafting of the PICC and has been approved to join the PICC.

Hardship has a legal equivalent in China, namely "change of situation" which is codified in Article 533 of the Chinese Civil Code.[6] Article.533 specifies that where the basic conditions of a contract undergoes a material change unforeseeable by the parties at the time of contracting which is not a commercial risk after the formation of the contract, rendering the continuation of the performance of the contract unconscionable for either party, the adversely affected party may renegotiate with the other party; and if the renegotiation fails within a reasonable time limit, the party may request the people’s court or an arbitration institution to modify or rescind the contract. The people’s court or arbitration institution shall change or rescind the contract based on the actual circumstances of the case, in accordance with the principle of fairness.

This article includes “force majeure” in the scope of the change of situation, and also specifies the way for the parties to exercise their rights, i.e., by requesting the People's Court or the arbitration body to change or cancel the contract in case of failure to renegotiate. In the special period of the new crown epidemic, the provisions of the Civil Code on the principle of change of situation can be more in line with the principle of fairness while considering the performance of the contract.[7]

4. Conclusion

This paper outlines the legal framework and functions of the hardship clause, briefly compares

hardship and force majeure, and correspondingly elaborates on the change of situation in China.

Hardship clause is a specific application of the principle of equity in contractual relationships, aiming to exclude manifestly unfair results in contracts caused by significant changes in political, economic or social situations, and to reflect fairness and justice.

References

[1] Harry M. Flechtner, CISG's exclusion clause and comments on the hardship clause and the Belgian High Court decision of 19 June 2009, Shandong Justice, No. 4, 2016

[2] Yang Baoyi, Hardship and Consequential Relief under Article 79 of CISG, Law & Society, Vol. 6, 2019

[3] Guo Hongjun, The difference between hardship and force majeure and their different legal effects, Modern Jurisprudence, 1998, No. 5

[4] Zhao Li, The amendment of the principle of equity to Pacta sunt servanda - Situational change in international model legislation, Law Review, No. 5, 2007

[5] Bi Xiuli, Comparative Analysis of Hardship and Force Majeure, Political Law Series, June 10, 1999, No. 3

[6] Wang Yongxin, The current situation of the hardship clause in China, Law and Economics, No. 9, 2009

[7] Gong Bohua, Legal Analysis of the Application of Force Majeure Clauses in International Commercial Contracts to the Covid-19 epidemic, Journal of SUIBE, March 2020, Vol. 27, No. 2