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**“CHANGED CIRCUMSTANCES IN OIL AND GAS CONTRACTS”**

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## TABLE OF CONTENTS

ABSTRACT.....	5
INTRODUCTION.....	6-7
<b>1. RENEGOTIATION CLAUSES AND CHANGED CIRCUMSTANCES: THEIR ROLE IN CONTRACTUAL PRACTICE</b>	
1.1. Renegotiation due to a change of circumstances in oil and gas contracts.....	8-10
1.2. Oil and gas contracts <i>with</i> a renegotiation clause.....	10-11
1.2.1 The Triggering event.....	11-12
1.2.2 Objective of renegotiation.....	13
1.2.3 Procedure for renegotiation.....	13-14
1.2.4 Consequences of renegotiation.....	14-15
1.2.5 Failure of the renegotiation process – The role of arbitration.....	15-17
1.2.6. Key issues when drafting a renegotiation clause.....	17-18
1.3 Oil and gas contracts <i>without</i> a renegotiation clause.....	18-21
<b>2. THE HARDSHIP DOCTRINE AND THE CONTRIBUTION OF HARDSHIP CLAUSES IN OIL AND GAS CONTRACTS</b>	
2.1.Introduction: The evolution of the doctrine and the contribution of the Unidroit principles.....	22-24

2.2. The definition of an onerous performance.....	24-26
2.3. Additional requirements for hardship.....	26
2.3.1. Events occur or become known after the conclusion of the contract. The “unforeseeability” of events.....	26-28
2.3.2. The concept of externality to the Party claiming hardship.....	28-29
2.3.3 The assumption of risk.....	29
2.4. Legal effects of Hardship	
2.4.1. Termination or renegotiation of the contract.....	29-30
2.4.2. Negotiations in good faith and the exercise of efforts to overcome the effect of changes in circumstances.....	30-31
2.5. The role of the court.....	32-33
2.6. Special considerations when drafting a hardship clause.....	34 -37
2.7. The ICC Hardship clauses.....	37

### 3. FORCE MAJEURE AND THE CONTRIBUTION OF FORCE MAJEURE CLAUSES IN OIL AND GAS CONTRACTS

3.1. Introduction.....	38-40
3.2. Events that constitute Force Majeure.....	40
3.2.1. Economic change as an event of Force Majeure .....	40-41
3.2.2. War as an event of Force Majeure .....	41-42
3.3.3. Revolution as an event of Force Majeure .....	42-43

3.3.4. Strikes as an event of Force Majeure .....	43-44
3.3.5. Supervening illegality as an event of Force Majeure .....	44
3.3.6. Sars-Cov-2 as an event of Force Majeure.....	44-45
3.4. Obligations of the party claiming Force Majeure.....	45-46
3.5. Legal consequences.....	46-47
3.6. Special considerations when drafting a force majeure clause.....	47-51
3.7. The ICC force majeure clause.....	51-52
4. COMPARATIVE APPROACH OF DOMESTIC LEGAL SYSTEMS ON CHANGED CIRCUMSTANCES	
4.1. The Civil law and Common law approach.....	53-54
4.1.1 The frustration doctrine.....	54-55
4.1.2. Commercial impracticability.....	56
4.1.3. Imprévision.....	57-58
4.1.4. The German legal doctrine of “Wegfall der Geschäftsgrundlage” .....	58
4.1.5. The Greek law on changed circumstances.....	59-61
Conclusion.....	62-64
List of literature.....	65-71
International Documents.....	71
Case law.....	71-72
Selected contracts.....	73

## **Abstract**

Oil and gas contracts, characterized by the longevity of their lifespan, are particularly vulnerable to unforeseeable economic, legislative and political changes, significantly affecting the parties' contractual relationship. In their effort to deal with the issues of changed circumstances, contracting parties often seek different mechanisms to ensure the continuation of their business agreements.

Although there has been much debate over the issue of contract adaptation, this thesis stands for the introduction of contractual clauses to deal with the issue of changed circumstances. The thesis also elaborates on the two aspects of the changed circumstances, namely hardship and force majeure, through an international and national perspective, with emphasis on the revision of the international petroleum and gas contracts and relevant case law. Finally, it illustrates the leading role of the Unidroit Principles of International Commercial Contracts (PICC) in oil and gas contracts for drafters, judges or arbitrators and their effective contribution in the enhancement of contract adaptation.

## Introduction

During the last century, we witness a tremendous increase in economic activity. This growth is not only quantitative but also qualitative. Transactions have gained transnational and international character and have become more complex and difficult to manage, as they do not only include the import and export of goods, but also the exchange of services, technology and investment.

Due to the lack of expertise and resources, many governments seek foreign investments and sign long-term contracts with their counterparties, namely foreign investors. One of the most important feature of these agreements is their longevity, which requires a stability in the parties' behaviour. Parties are entitled to respect their agreements and act according to their provisions. This commitment has its origins in the *pacta sunt servanda* doctrine that pervades all contractual arrangements. The "sanctity of contract" is a general principle of international law, present in all legal systems<sup>1</sup>. Its value is indisputable if one stops to consider what would happen if it did not exist. Parties would cease to respect their commitments anytime, on the first twist of change.

However, the principle may lead to harmful situations regarding the life of the agreement, if applied in a rigid manner. This is particularly the case with long-term agreements where a sudden and unforeseeable change of circumstances may render the performance of one of the parties more burdensome or even impossible. The change may appear due to a modification in the legal, political or economic context in which the parties activate and perform. A sudden change in the currency of a country, an unexpected increase in the price of raw materials, an unforeseen change in the market for a product, political turbulence, terrorist attacks, hostilities, war and the on-going pandemic of Sars-CoV-2 are a few examples of its manifestations in today's world.

Therefore, in extreme situations, when a change occurs due to unpredicted and unpredictable circumstances, the contracting parties are likely to modify their agreement in order to safeguard their interests and ascertain that their commercial arrangement will remain fruitful, following the principle of *rebus sic stantibus*. Derived from canon law the *rebus sic stantibus clausula* indicates that contracts remain binding when circumstances under which they had been resumed are not *significantly* altered. In other words, as the *impossibilium nulla est obligatio* principle advocates<sup>2</sup>, when unforeseeable and extraordinary changes of circumstances come into the scene,

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<sup>1</sup> "The parties are bound by their contracts under Roman Law"; Zimmerman R., (1990), The Law of Obligations – Roman Foundations of the Civilian Tradition, Juta & Co Ltd, 1990, 577.

<sup>2</sup> According to this principle, there is no obligation to perform impossible things

which alter significantly the contractual equilibrium of the contract and render the parties' performance exceedingly burdensome or even impossible<sup>3</sup>, parties may choose to adapt their contracts accordingly, in order to mitigate the discontinuation and damage from the occurrence of changed circumstances. In this context, parties have a choice between contractual practices or statutory legal provisions. The parties' choice of contractual provisions, namely renegotiation, hardship or force majeure clauses<sup>4</sup> reflect the international trade practice and may lead to contract adaptation. Another solution derives from the rules provided by the law of the contract itself, which appoints a certain legal system to govern the contract.<sup>5</sup> Whatever the choice of the parties, all the above are aspects of the same *rebus sic stantibus* rule.

The thesis' scope is to examine the various existing options in order to deal with cases of changed circumstances. First, the thesis highlights the significance of renegotiation as a means of flexibility and protection of the contract, with particular emphasis on the role of renegotiation clauses, long-used in international contractual practice. Furthermore, the thesis examines the hardship and force majeure doctrines as the two major concepts of changed circumstances in international trade, with particular reference to the contribution of the Unidroit Principles of International Commercial contracts and emphasis on international gas and oil case law. The thesis also aims to highlight the role of hardship clauses as a means of adaptation of the contractual arrangement, while the role of force majeure clauses is to promote either adaptation or termination of the contract. Finally, the thesis compares the existing domestic legal systems provisions on the subject of changed circumstances, through a comparative approach. In this aspect, the thesis studies the English, American, German, French and Greek legal systems on changed circumstances, highlighting the inadequacy of domestic solutions with regard to an international environment.

In order to achieve the goals of the research, the methodology used is linguistic, systematic, historical, comparative and inductive. The linguistic method is used to comprehend legal acts and court cases. The systematic method analyzes the contractual and domestic law provisions, the case law and their interrelation. The historical method highlights the evolution of the hardship and force majeure doctrines. The comparative analysis emphasizes on the various differences of legal systems across countries and the inductive method is used to draw conclusions and determine the role of clauses in contractual practice in oil and gas contracts.

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<sup>3</sup> The hardship or the force majeure doctrines, respectively.

<sup>4</sup> Al Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*. Legal Research Paper Series. SSRN Electronic Journal, 1-16.

<sup>5</sup> A domestic legal system, which the parties appoint as their choice of law to govern their contract.

# 1. RENEGOTIATION CLAUSES AND CHANGED CIRCUMSTANCES: THEIR ROLE IN CONTRACTUAL PRACTICE

## 1.1. Renegotiation due to a change of circumstances in oil and gas contracts

Oil and gas contracts are concluded between either a host state and an investor or a state entity and a private party, their main characteristic being the longevity of their lifespan. Because of their capital intensity, their duration, their complexity and uncertainty, these long-term contracts are often subject to unexpected changes of circumstances, leading to significant imbalance of the of the parties' contractual relationship<sup>6</sup>. Since it is not possible for all events to be foreseeable beforehand,<sup>7</sup> it is probable that the occurrence of a change of circumstances may render the performance of one of the parties exceedingly "onerous<sup>8</sup> or even impossible<sup>9</sup>". Consequently, it is 'fair' for the parties to be able to confront these unpredicted changes by renegotiating their contracts in order to reconstitute the original equilibrium of their agreement<sup>10</sup> or adapt their contractual agreement in the changed circumstances. In this context, parties usually choose between two alternatives. Either they choose to renegotiate their contractual provisions after an event changes their arrangement, or, they terminate the agreement, if the cost of respecting a contract outweighs the cost of dismissing it. This choice does not only reflect the economic parameters of a contract, but also involves socio-cultural costs and benefits<sup>11</sup>.

If parties choose to introduce specific clauses in their contracts, they use them as mechanisms of adaptation to the changed circumstances. The clauses actually grant the parties more flexibility, restoring their contractual equilibrium.<sup>12</sup> Such clauses, which allocate an obligation for the parties to renegotiate in good faith in order to conclude a new arrangement on a contract's modified terms, are indeed encountered in several oil and gas agreements<sup>13</sup>.

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<sup>6</sup> Zaccaria, E.C., (2005). *The effects of changed circumstances in International Commercial Trade*. International trade and Business Law review, 2005, 137-138.

<sup>7</sup> Bernardini P., (2008). *Stabilization and adaptation in oil and gas investments*. Journal of World Energy Law and Business, 1 (1), 115

<sup>8</sup> The Unidroit principles of International Commercial Contracts (PICC) refers to the term, id.

<sup>9</sup> Force majeure in Roman Law is under the term "vis major" or "vis divina", in Katsivela, M. (2007). *Contracts: Force Majeure concept or Force Majeure Clauses?* Uniform Law Review 2007, 101.

<sup>10</sup> Oyewunmi, T., (2011). *Stabilisation and Renegotiation Clauses in Production Sharing Contracts: Examining the Problems and Key Issues*, Oil Gas and Energy Law Intelligence, 9 (6), 11.

<sup>11</sup> Salacuse, J., (2000). *Renegotiating International Project Agreements*. Fordham International Law Journal, 24 (4), 1341.

<sup>12</sup> Salih, M.S., Yamulki A., (2020). *Stabilisation and Renegotiation in Iraqi Kurdistan Oil and Gas Contracts: A comparative study*, Journal of Law and Globalization, 2020 (100), 109.

<sup>13</sup> Montembault, B., (2003). *La stabilization des contrats d'etat a travers l' exemple des contrats petroliers – Le Retour des dieux sur l' Olympe*. International Business Law Journal, 2003 (6), 627.



It is noteworthy that over the past decades, many petroleum and gas contracts have been concluded with the inclusion of such renegotiation clauses. Together with stabilization clauses, they provide both the host state and the investor with substantial protection, safeguarding perpetuation of the contract and the dispute resolution<sup>14</sup>.

According to Salih and Yamulki, over the past decades we have encountered two major categories of renegotiation clauses: The traditional and the modern ones. While they both aim at foreseeing the circumstances that may lead to imbalance of the contract, their content is different.

The traditional renegotiation clause aims at returning the parties to their position prior to the change of the contract's legal status. An illustrative example is the clause contained in *the Haitian Petroleum Agreement of 1979*. The clause contains an obligation to renegotiate either within a specific timeframe or *upon the outbreak of a certain event*<sup>15</sup>».

Moreover, traditional renegotiation clauses may alternatively link the renegotiation process to a specific event, explicitly mentioned. An illustrative example is *the 1974 Production Agreement of the Government of Ghana and Shell Exploration and Production Company of Ghana Ltd*<sup>16</sup>, according to which the events triggering renegotiation are "*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 on this Agreement*". As parties can only ask for renegotiation based on the aforementioned events, this type of clause is considered to have a restricted application<sup>17,18</sup>.

The other major type is the modern or economic equilibrium clause which has a mixed character of both stabilization and renegotiation objectives. This clause aims at defending the

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<sup>14</sup> Salih, M.S., Yamulki A., *Stabilisation and Renegotiation in Iraqi Kourdistan Oil and Gas Contracts: A comparative study*, supra note 12, 109.

<sup>15</sup> Id., The Service Contract between the Haitian State and Anschutz Oversea Corporation, (1979), article 3.3. It reads: "*It is agreed that the terms of this contract shall, upon the request of either party, be subject to renegotiation after seven (7) years from the date of pay-out or ten (10) years after the year end in which commercial production is reached, whichever time is late – provided however, that in no event shall 'renegotiation' be deemed to be tantamount to termination. Rather renegotiation shall be deemed to reflect the opportunity of the parties to adjust the economic terms and conditions of this contract to account for the then local and international conditions*".

<sup>16</sup> The Petroleum Production Agreement between the Government of Ghana and Shell Exploration and Production Company of Ghana Ltd, (1974), article 47, in Salih, M.S., Yamulki A., (2020). *Stabilisation and Renegotiation in Iraqi Kourdistan Oil and Gas Contracts: A comparative study*, supra note 12, 102

<sup>17</sup> Ibid., 110.

<sup>18</sup> Other clauses which link particular events with the renegotiation process are the PSA between the State Oil company of Azerbaijan Republic and a consortium of oil companies (1995); The supplementary agreement to the concession Agreement between the State of Kuwait and Aminoil (1961); The PSA between the Vietnam National Oil and Gas Corporation of the Socialist Republic of Vietnam, Lasmo Vietnam and C. Itoh Energy Development Co., Ltd for offshore block 04-2 (1992); the Model exploration and Production sharing Agreement of the State of Qatar (1994); the Model exploration and Production sharing Agreement of Turkmenistan (1997), in Al Qurashi, Z. (2005). *Renegotiation of International Petroleum Agreements*. Journal of International Arbitration, 22 (4), 286-287.

economic equilibrium of the contract from changes of a legal character, and is considered as the evolution of a freezing clause, the modern type of stabilization clause<sup>19</sup>. Recent examples are encountered in the *1999 Exploration Development and Production Sharing Contract of the State Oil Co of Azerbaijan and Kura Valley Development Co Ltd and Socar Oil Affiliate*. Under Article 24.2, «*In the event that any Governmental Authority invokes any present or future law, treaty, intergovernmental agreement, decree or administrative order which contravenes the provisions of this Agreement or adversely or positively affects the rights or interests of Contractor hereunder, including, but not limited to, any changes in tax legislation, regulations, or administrative practice, the terms of this Agreement shall be adjusted to re-establish the economic equilibrium of the Parties, and if the rights or interests of Contractor have been adversely affected, then SOCAR shall indemnify the Contractor (and its assignees) for any disbenefit, deterioration in economic circumstances, loss or damages that ensue therefrom*».

## **1.2. Renegotiation of oil and gas agreements *containing* a renegotiation clause**

Parties choose to induce renegotiation clauses in their contracts, because these guide them to agree upon the extent of their contractual modifications. The inclusion of such terms actually ensures the result of the renegotiation process<sup>20</sup>.

In practice, the insertion of such terms have come as a necessity for governments in their effort to attract foreign investors. Governments started to prioritize the inclusion of “competitive” terms for their investment contracts. This practice, which also applies for natural resources exploration agreements, eventually moved forward from the traditional use of stabilization clauses<sup>21</sup> to a formulation that combined stabilization and renegotiation provisions.<sup>22</sup>

However, the adoption of renegotiation clauses was not unanimously accepted. Although some scholars are in favor of inserting a renegotiation clause in the contract,<sup>23</sup> others propose that such clauses have serious disadvantages; they argue that renegotiation clauses increase contract

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<sup>19</sup> Salih, M.S., Yamulki A., (2020). *Stabilisation and Renegotiation in Iraqi Kourdistan Oil and Gas Contracts: A comparative study*, supra note 12, 102.

<sup>20</sup> Ibid., 110.

<sup>21</sup> Al Faruqi A., (2008). *Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium and Stability*, The Journal of World Investment and Trade, 2008 (113), 115

<sup>22</sup> Al Qurashi, Z., (2005). *Renegotiation of International Petroleum Agreements*, supra note 18, 285-286.

<sup>23</sup> Berger, K., (2003). *Renegotiation and adaption of international investment contracts: The role of contract drafters and arbitrators*. Vanderbilt Journal of Transnational Law, 36 (4), 1357-1358.

instability as well as the total cost of the agreement; others assert that such clauses may prove non-enforceable, especially if there is lack of dispute between the parties and therefore courts are unable to intervene. It is also proposed that courts may alter the clause in such a way that neither party will be happy with the outcome, or that because the events that trigger renegotiation are totally within the control of the host state, this always results as unfair for the investor<sup>24</sup>.

However, under certain circumstances, provided that the renegotiation clause is carefully drafted, an introduction of such a clause in the contract is beneficial for both parties, as it provides the contract with flexibility<sup>25</sup>.

### 1.2.1. The “Triggering” event

In order for a renegotiation clause to meet the effectiveness and the enforcement criterion it has to contain a minimum of provisions. The first important element is the definition of the triggering event. Renegotiation clauses generally include the triggering events in order to establish a legal basis on which the renegotiation phase will take place. According to some scholars, when the wording of the clause is more generic, it may apply to a broad variety of cases, adding more flexibility to the contract<sup>26</sup>. Clauses of this genre include phrases such as “a substantial change in the circumstances existing on the date of the agreement” or “a change of circumstances” without referring explicitly to a list of events. The avoidance of an exclusive list is the result of the argument that triggering events are unforeseen, complex and in many cases a result of economic turbulence<sup>27</sup>. Other scholars argue however that the vague formulation of triggering events may result in a wider interpretation of the contract, causing more uncertainty<sup>28</sup>. Therefore, one has to draw attention to the careful drafting of the clause so as to formulate a clause in general style, while at the time expressly define the triggering event<sup>29</sup>.

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<sup>24</sup> Gotanda, J. Y., (2003). *Renegotiation and Adaptation Clauses in Investment Contracts, Revisited*, Vanderbilt Journal of Transnational Law, 2003 (36), 1463.

<sup>25</sup> Ibid., 1469.

<sup>26</sup> Al Faruque A., (2008). *Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium and Stability*, supra note 21, 122.

<sup>27</sup> Berger, K., (2003). *Renegotiation and adaption of international investment contracts: The role of contract drafters and arbitrators*, supra note 23, 1362.

<sup>28</sup> Al Faruque A., (2008). *Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium and Stability*, supra note 21, 122; Gotanda, J. Y., (2003). *Renegotiation and Adaptation Clauses in Investment Contracts, Revisited*, supra note 24, 1463.

<sup>29</sup> Al Qurashi, Z., (2005). *Renegotiation of International Petroleum Agreements*, supra note 18, 290.

The review of some examples of triggering events, well known in international petroleum industry, illustrates some important aspects. The triggering events we encounter in petroleum contracts have different backgrounds. Some come as changes in the legal environment of the contract, mainly the imposition of new laws and regulations<sup>30</sup>; some refer to the event signaling the change, as the review of the parties' obligations in case there is an increase in benefits of the host state<sup>31</sup>. A financial and economic change of the circumstances, operating and marketing conditions concerning the oil industry is also encountered<sup>32</sup>.

A common feature of all the above clauses is that the effect of the triggering event must be explicitly stated in the contract<sup>33</sup>. Terms such as "*disproportionate prejudice*", "*substantial detriment*", and "*substantial economic imbalance*" may underline the effect of the change<sup>34</sup>. As per the consequence of the change of circumstances, the renegotiation clause usually states that the party claiming the change of circumstances will not suspend its performance while the renegotiation proceeds<sup>35</sup>.

### 1.2.2 Objectives of renegotiation

In their renegotiation clause, the contracting parties determine the objectives of renegotiation. The wording of the objectives of renegotiation may as well be subjective and generic, using open-ended phrases such as "*removing the unfairness*", or "*adopting an equitable solution*"<sup>36</sup>. Other scholars however propose that the scope of renegotiation must be more concrete, because

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<sup>30</sup> An illustrative example is the 1997 Turkmenistan Model Agreement (article 16.6). "*Where present or future laws or regulations of Turkmenistan or any requirements imposed on Contractor or its subcontractors by any Turkmen authorities contain any provisions not expressly provided for under this Agreement and the implementation of which adversely affects Contractor's net economic benefits hereunder, the Parties shall introduce the necessary amendments to this Agreement to ensure that Contractor obtains the economic results anticipated under the terms and conditions of this Agreement*". Another example is article 34.12 of the 1994 Qatar Model Exploration and Production Sharing Contract containing the following provision: "*Whereas the financial position of the Contractor has been based, under the Agreement, on the laws and regulations in force at the Effective Date, it is agreed that, if any future law, decree or regulation affects Contractor's financial position, and in particular if the customs duties exceed..... percent during the term of the Agreement, both parties shall enter into negotiations, in good faith, in order to reach an equitable solution that maintains the economic equilibrium of this Agreement*"

<sup>31</sup> Article 9 of the Aminoil Supplementary Agreement.

<sup>32</sup> The PPA between the government of Ghana and Shell Exploration and Production Company (1974). This clause's legal formulation has a proximity to a hardship clause, in Al Qurashi, Z., (2005). *Renegotiation of International Petroleum Agreements*, supra note 18, 289.

<sup>33</sup> The above Ghana/Shell agreement states that (the triggering event must) "*materially affect the fundamental economic and financial basis of the Agreement*", *ibid.*, 289-290.

<sup>34</sup> Ng'ambi, S., (2014). *Efficient and flexible: The case for renegotiation clauses in concession agreements*. Zambia Law Journal, 45, 21.

<sup>35</sup> Bernardini P., (2008). *Stabilization and adaptation in oil and gas investments*, supra note 7, 105.

<sup>36</sup> *Id.*

it serves as a guideline to the result of the process. The 1992 Vietnam Production Sharing Agreement is a good example of this argument as it clearly demonstrates the extent of contract change. It provides that the parties are obliged to renegotiate in order to “ensure that the contractor is restored to the same economics which would have prevailed if the new law and/or regulation or amendment had not been introduced<sup>37</sup>.”

On the contrary, the 1994 Model Exploration and Production Sharing Agreement of Qatar is an open-ended clause. By its wording, the clause does not clarify if the parties’ common intent is only the restoration of “the original contractual equilibrium” or if compensation of the aggrieved party or the safeguarding of the host state’s interests are taken into account<sup>38</sup>.

### 1.2.3 Procedure for renegotiation

Parties are expected to work together in order to reach an agreement in the renegotiation phase. Bernardini opines that the parties’ obligations should be defined in detail, the objectives of renegotiation worded in an open-ended manner and renegotiation should be conducted in good faith<sup>39</sup>. However, according to another opinion, if renegotiation is not stipulated in the contract, then one must examine the “inherent functions” of the clause. According to Berger “despite their unavoidable uncertainty, these kinds of clauses are not empty shells”. By agreeing to insert a clause, the contracting parties “are legally obliged to cooperate in the renegotiation procedure in an efficient manner. This requires flexibility, earnest efforts and the willingness to consider the needs and interests of the other party”. Furthermore, the scope of these clauses is to bring the contract towards the changed circumstances while there is a general prohibition to cause damages to the other party<sup>40</sup>.

According to unanimous international opinion<sup>41</sup>, the parties’ obligation *to do their utmost to reach an agreement* does not mean that the contracting parties *are obliged* to reach an

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<sup>37</sup> Al Qurashi, Z., (2005). *Renegotiation of International Petroleum Agreements*, supra note 18, 290.

<sup>38</sup> Bernardini P., (1998). *The renegotiation of the Investment contract*. *ICSID Review – Foreign Investment Law Journal*, 13 (2), 419.

<sup>39</sup> Bernardini P., (2008) *Stabilization and adaptation in oil and gas investments*, supra note 7, 105; Al Faruque A., (2008). *Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium and Stability*, supra note 21, 121.

<sup>40</sup> Berger, K., (2003). *Renegotiation and adaption of international investment contracts: The role of contract drafters and arbitrators*, supra note 23, 1364.

<sup>41</sup> Bernardini P., (2008) *Stabilization and adaptation in oil and gas investments*, supra note 7, 105; *Ibid.*, 1367.

agreement upon the revision of the contract<sup>42</sup>, and there is no breach of contract if they do not agree. In any case, the parties must conduct their negotiations in good faith and fairness, based on mutual trust, cooperation and in the context of preserving contractual equilibrium<sup>43</sup>, an issue examined by a judge or an arbitrator in case of failure of agreement<sup>44</sup>.

#### 1.2.4 Consequences of renegotiation

According to Al Faruque, after the conclusion of the renegotiation process, parties adapt the contract according to their mutual agreement. The restructuring of the contract may prove fruitful for both the host state and the investor. The latter continues to anticipate the benefits of the project, while the host state increases its financial, socio-political benefits by the reduction of the risks coming from the change of circumstances. A successful renegotiation also removes the risk of the host state unilaterally modifying the contract, restores the contractual equilibrium and ensures stability and fairness in the parties' relationship.

In case a renegotiation clause is expressly included in the contract and one of the parties refuses to renegotiate, this is an explicit breach of contract and the denying party has the obligation to compensate the counterparty<sup>45</sup>. On the contrary, if the parties act in good faith and the renegotiation is rendered unsuccessful, there is no breach<sup>46</sup> and this failure cannot give rise to any liability.<sup>47</sup> Significant in this direction is the case of the government of *Qatar vs. Wintershall A.G.* In this particular case, the parties had agreed that "*they would negotiate future arrangements for the use of natural gas not associated with oil discoveries, if commercial quantities of such "non-associated" gas were found at a later point in time in the contract area*". When these quantities were finally discovered, the parties entered into negotiations, which failed. The case was brought before an arbitral tribunal. The oil company alleged that the Qatari government had breached the contract because it had failed to agree during the negotiation phase. The arbitral tribunal however,

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<sup>42</sup> In the dispute between the American Independent Oil Company (Aminoil) and the Government of the State of Kuwait, the Arbitral Tribunal outlined the extent of the obligation to negotiate contemplated in art 9 of the Supplementary Agreement, concluding that 'an obligation to negotiate is not an obligation to agree', in Bernandini P., (2008). *Stabilization and adaptation in oil and gas investments*, supra note 7, 105.

<sup>43</sup> Al Faruque A., (2008). *Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium and Stability*, supra note 21, 121.

<sup>44</sup> Bernandini P., (2008). *Stabilization and adaptation in oil and gas investments*, supra note 7, 106.

<sup>45</sup> Al Faruque A., (2008). *Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium and Stability*, supra note 21, 130.

<sup>46</sup> Ibid., 133.

<sup>47</sup> Salacuse, J., (2000). *Renegotiating International Project Agreements*, supra note 11, 1334.

did not accept this argument on the grounds that the government had acted in good faith and “*the duty to negotiate in good faith does not include an obligation to accept proposals made by the other side*”. The arbitral tribunal decision also stated: “*the Qatari Government’s refusal to accept those proposals was based on reasonable commercial judgments*”<sup>48</sup>. Moreover, the same conclusion was drawn by the arbitral award of *Kuwait vs. Aminoil*, which accepted the *rebus sic stantibus* principle in international oil agreements, underlining that the obligation to negotiate does not extend to the obligation to agree<sup>49</sup>.

### 1.2.5. Failure of the renegotiation process, the role of arbitration

The revision of an agreement by a third party is much discussed and debated due to the contradiction between the traditional dogma of the *sanctity of contracts* against the parties’ freedom to adapt their agreement. This contradiction extends to the third party intervention. It is therefore argued<sup>50</sup> that third party intervention is not compatible with the freedom to adapt one’s agreement.

In case of changed circumstances triggering renegotiation, if parties do not agree and renegotiations fail, in practice, we come across three different solutions. Firstly, if the renegotiation clause itself is silent about the consequences of the failure, or if an attempt between the parties ends in failure, and the parties have renegotiated in good faith, then the arbitrator may proceed to determine that the contract can either be terminated or continued upon its initial terms. Moreover, if the parties fail to reach an agreement and the contract specifically refers the matter to a third party, (such as arbitration, a court, an expert or a conciliator), then the third party shall determine if the allegations of the aggrieved party meet the criteria of changed circumstances, in order to initiate the renegotiation procedure. In practice, the arbitrator draws some initial conclusions and usually invites the contracting parties to renegotiate upon them. Finally, the contract may appoint the matter to a third party with further specifications on the extent of the third party intervention<sup>51</sup>. In this final option, the arbitrator determines the manner in which the terms of the contract could be modified, in order to agree with the parties’ will, issues an award accordingly<sup>52</sup>.

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<sup>48</sup> *Wintershall v Government of Qatar*, id.

<sup>49</sup> Oyewunmi, T., (2011). *Stabilisation and Renegotiation Clauses in Production Sharing Contracts: Examining the Problems and Key Issues*, supra note 10, 11.

<sup>50</sup> Berger K., (2001), *Powers of Arbitrators to fill gaps and Revise contracts to make sense*, *Journal of International Commercial Arbitration*, 17 (1), 1.

<sup>51</sup> Al Faruque A., (2008). *Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium and Stability*, supra note 21, 139.

<sup>52</sup> Bernandini P., (2008). *Stabilization and adaptation in oil and gas investments*, supra note 7, 107.

According to Al Faruque<sup>53</sup> and Bernardini,<sup>54</sup> modification of the contract by a third party poses some “delicate issues” for three reasons: the first reason has to do with the third party’s lack of information regarding a complex long-term agreement, such as an oil or gas contract. The next reason has to do with the enforceability of the contract: one of the parties may refuse to recognize and enforce the revised agreement. The third reason has to do with the parties’ interests. Parties to a contract know best how to judge their own interests and how to find the optimal solution, more than a third party entitles itself to. In the *Aminoil case* the arbitral tribunal stated: “*There can be no doubt that, speaking generally, a tribunal cannot substitute itself for the parties in order to ...modify a contract unless that right is conferred upon it by law, or by the express consent of the parties...arbitral tribunals cannot allow themselves to forget that their powers are restricted. It is not open to doubt that an arbitral tribunal-constituted on the basis of a 'compromissory' clause contained in relevant agreements between the parties to the case...could not, by way of modifying or completing a contract, prescribe how a provision must be applied. For that, the consent of both parties would be necessary.*” From the above, we easily perceive that a third party intervenes only on the grounds of the parties’ “express consent” included within the contract or by the substantive law.

Moreover, Al Faruque argues that the idea that an arbitrator cannot adapt a contract by re-writing the relevant clauses is generally affected by the widely accepted view that arbitration is held only when there is legal dispute<sup>55</sup>. In the renegotiation phase, parties are not in conflict with one another and therefore their possible differentiation of opinion is not considered to be a conflict and thus is not arbitrable. A similar problem arises when parties decide to have their disputes resolved by the ICSID arbitration<sup>56</sup> due to article 25(1) of the ICSID Convention<sup>57</sup>.

The reason why arbitrators reflect upon their jurisdiction originates from the idea that if they exceed their powers there is ground for the non-enforcement and non-recognition of their awards at the request of one of the parties. The legal consequence is that if an award is deemed unenforceable under a particular jurisdiction it is very difficult to become enforceable in another jurisdiction<sup>58</sup>.

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<sup>53</sup> Al Faruque A., (2008). *Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium and Stability*, supra note 21, 140.

<sup>54</sup> Bernardini P., (2008). *Stabilization and adaptation in oil and gas investments*, supra note 7, 107.

<sup>55</sup> *Ibid.*, 140.

<sup>56</sup> Al Qurashi, Z., (2005). *Renegotiation of International Petroleum Agreements*, supra note 18, 23.

<sup>57</sup> Article 25 (1) of the ICSID Convention.

<sup>58</sup> Article V (1c&e) of the 1958 New York Convention in Ng’ambi, S., (2014). *Efficient and flexible: The case for renegotiation clauses in concession agreements*, supra note 34, 24-25.



### 1.2.6 Drafting a Renegotiation Clause

Renegotiation in oil and gas contracts is the outcome of a renegotiation clause. Therefore, drafting is very important for a successful renegotiation process. In drafting such clauses, contracting parties need to pay special attention to certain aspects.

Four are the main features of a successful renegotiation clause: the triggering events and the procedure of renegotiation must be clearly defined and carefully worded, so to avoid instability and misinterpretation of the contract. The extent of the contract change has to be also clearly outlined, as the renegotiation clause must serve as a guideline towards the result of the renegotiation process. Moreover, the renegotiation clauses have to define the obligations and the rights of the contracting parties, and ensure that the renegotiation process is conducted in good faith<sup>59</sup>.

An illustrative example of a well - constructed clause is the Lebanese PSC<sup>60</sup>.

*“In the event that the law no 132/2010 (OPR Law), any regulations adopted thereunder (including the decree no 10289/2013(PAR), or any other Lebanese laws are modified after the date of this EPA in any other manner (except as set forth in the next sentence) that substantially affects the economic or financial position of the Right Holders in respect of this EPA, then the Right Holders may notify the Minister and the Petroleum Administration that they wish to meet in order to discuss appropriate adjustments to the terms of this EPA to preserve such economic or financial position. The Right Holders may not provide any such notification if the relevant change in Lebanese law relates to the improvement of health, safety, environmental standards consistent with the evaluation of international standards and practices. If any such notification is provided, the Right Holders shall, together with such notice, provide an explanation in reasonable detail of the manner in which the relevant modifications substantially affect the economic or financial position of the Right Holders in respect of this EPA. The Parties shall thereafter engage in good faith discussion with a view to agreeing on such adjustments. Neither Party shall have an obligation to agree to any adjustment. If such discussions do not produce an agreement within ninety (90) days of the commencement of such discussions, then the Right Holders may submit the issue to a sole expert, who shall determine the adjustment that is necessary to preserve the economic or financial position of the Parties. Any adjustment agreed by the Parties or determined by a sole expert shall be*

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<sup>59</sup> Salih, M.S., Yamulki A., (2020). *Stabilisation and Renegotiation in Iraqi Kurdistan Oil and Gas Contracts: A comparative study*, supra note 12, 113.

<sup>60</sup> Exploration and Production Agreement for Petroleum Activities in Block 4, between the Republic of Lebanon and Total E&P Leban SAL, And Eni Lebanon B.V. and NOVATEK Lebanon SAL., (2018), article 28 (2018).

*submitted for approval by the Council of Ministers, and shall be effective only if such approval is granted”.*

The above clause clearly outlines the procedure of renegotiation for adjustment of the contract in case of alteration of the contractor’s financial position by a change in laws and regulations. The clause has limits as it excludes health, safety and environmental standards. The period of ninety days is determined by the clause as the timeframe within which an agreement must be conceived; otherwise, the contractor may submit the issue to a sole expert. Any adjustment agreed by the parties or determined by a sole expert needs a levelled approval of the Council of Ministers.

### **1.3 Renegotiation of an oil and gas agreement *without* a renegotiation clause**

Renegotiation is certainly an option when there is explicit provision in the agreement. However, there is an abundance of cases where no clause for renegotiation deals with the subject of changed circumstances. In this case, the applicable law of the contract, which the parties choose to govern their contract, also provides for the issue of changed circumstances. The applicable law is very important because it defines the particular conditions and the extent of the change of circumstances, as well as the legal effect in case of a failure in the renegotiation process. If parties do not induce a particular clause in their contracts to deal with the issue, then other terms of the contract or the parties’ choice-of-law become the keys of the ignition of the renegotiation process<sup>61</sup>.

Contracting parties have the option to choose among a national law to govern their contractual relationship or a combination of international and national law or general principles of law or may refer in the international petroleum industry practices. In such cases, arbitral tribunals apply the choice-of-law reflecting the parties’ will. If parties do not agree on the law applying to their contract, then different legal systems are applied. In this case, arbitrators usually apply the solutions proposed by different national laws in combination with “commercial usages.” If different legal systems are in conflict, then they choose solutions widely accepted and use the common principles<sup>62</sup>.

Other than the application of a national legal system, both parties may rely upon the principle of the change of circumstances (*rebus sic stantibus principle*), which is applicable even if

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<sup>61</sup> Al Qurashi, Z., (2005). *Renegotiation of International Petroleum Agreements*, supra note 18, 268-269.

<sup>62</sup> *Ibid.*, 269-270.

there is no particular clause in the contract, reflecting the notion mirrored in the Vienna Convention of the Law of Treaties<sup>63</sup>. Although the Vienna Convention applies to Treaties between states<sup>64</sup>, it is nevertheless widely accepted that the Treaty is “*a strong argument for the existence of a general legal principle which might also be relevant to transnational contract with or between private parties*”. In this aspect, in case of a change in circumstances, parties are due to renegotiate their contractual arrangements. This argument is also supported by various United Nations Resolutions and by OPEC members<sup>65</sup>. However, the *rebus sic stantibus* principle has been accepted by arbitrators and courts in few occasions, for the fear of misuse<sup>66</sup>.

Contracting parties to a long-term contract with no specific renegotiation clause may also choose to insert a force majeure or a hardship clause as a means of dealing with the issue of changed circumstances. Both force majeure and hardship clauses are encountered in petroleum and gas contracts, as a means to ignite the renegotiation process, as the literature on the subject demonstrates<sup>67</sup>. Force majeure clauses deal with unforeseeable economic and sociopolitical events at the time of the conclusion of the contract, or events, which are perceived as “an act of God” and render the performance of the party impossible. In comparison, the hardship concept aims at re-establishing the equilibrium of the contract<sup>68</sup> when performance is still possible, but exceedingly burdensome for the party.

Another option for parties to oil and gas contracts, particularly the ones that do not contain a specific provision on the issue, is to embed hardship clauses in their contracts. These clauses usually entitle parties to initiate the renegotiation process, by defining the various conditions relating to it. In this context, the clauses refer to the circumstances of hardship and define the obligations of each party vis-à-vis renegotiation. Some of the more “sophisticated” clauses even stipulate a method towards the process and a third party intervention, in case no agreement is achieved<sup>69</sup>.

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<sup>63</sup> It is worth mentioning that this particular article has limited application, in order to avoid uncertainty and preserve the sanctity of the contract’s principle stated in article 26, *ibid.*, 277.

<sup>64</sup> According to Article 2 of the Vienna Convention.

<sup>65</sup> Al Qurashi, Z., (2005). *Renegotiation of International Petroleum Agreements*, *supra* note 18, 278.

<sup>66</sup> Horn, N., (1985). *Changes in Circumstances and the Revision of Contracts in Some European Laws and in International Law*, in Norbert Horn (ed.), *Adaptation and Renegotiation of Contracts in International Trade and Finance*, Kluwer, London, 1985, 29 in <https://www.trans-lex.org/113700>, [accessed on 9/3/2021].

<sup>67</sup> Al Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*, *supra* note 4, 1

<sup>68</sup> Berger, K., (2003). *Renegotiation and adaption of international investment contracts: The role of contract drafters and arbitrators*. *Supra* note 23, 1350-1356.

<sup>69</sup> The clause inserted in the Superior Overseas Corporation and Phillips Petroleum Agreement (UK) Co Ltd v British Corporation as well as the clause originally cited in Schmitthoff, (1980) “Hardship clauses”, *The Journal OF Business Law* 84-85, in Al Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*, *supra* note 4, 5-7.

According to Berger, even today, when a change in the economic parameters of a contractual arrangement occurs, the principle of the “sanctity of contract” remains the prevailing doctrine. He argues that in practice, neither the host country nor the investor successfully rely on force majeure or hardship clauses in order to renegotiate their contracts in case of a change in circumstances. The reason is that the host state is usually the cause of the change of circumstances (i.e. the State imposes a change in legislation) and is regarded as holding the responsibility for the change. In the same manner, it is more unlikely for the investor to commence renegotiations upon the grounds of hardship or force majeure<sup>70</sup>.

In any case, the dispute resolution usually remains an issue for international arbitrators to deal with. In this context, arbitration actually decides upon adaptation or termination of the agreement.

## **2. THE HARDSHIP DOCTRINE AND THE CONTRIBUTION OF HARDSHIP CLAUSES IN OIL AND GAS CONTRACTS**

### **2.1. Introduction: The evolution of the doctrine and the contribution of the Unidroit principles**

The principle of hardship is traced back in the classic Roman Law<sup>71</sup>, as well as in the private law codifications of the 18<sup>th</sup> century. According to the theory, a substantial change in the circumstances affecting a contract in a manner so to render the performance of one of the parties more “burdensome,” would permit the affected party to invoke the *rebus sic stantibus clausula*<sup>72</sup>.

As time evolved, the principle was much criticized, mostly due to the emphasis on the party autonomy and eventually, in the 19th century, it was set completely aside. During the First World War, the doctrine resurfaced, through a particular case ruled by a French court, which made explicit reference to the doctrine<sup>73</sup>. Today, various national legislations provide an exemption from the performance of a contract when the last becomes impossible due to extreme circumstances (force majeure).

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<sup>70</sup> Berger, K., (2003). *Renegotiation and adaption of international investment contracts: The role of contract drafters and arbitrators*, supra note 23, 1352-1353.

<sup>71</sup> Schwenzer I., Munoz E., (2019). *Duty to renegotiate and contract adaptation in case of hardship*, *Revue du droit uniforme*, 2019, 2.

<sup>72</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*. *Oil Gas and Energy Law Intelligence*, 5 (2), 3.

<sup>73</sup> This is the case of the “*Compagnie generale d’ éclairage de Bordeaux*” v *The City of Bordeaux*, *Ibid.*, 4.

Hardship is however different from force majeure. Hardship means that an (unforeseen) event changes the contractual equilibrium of the parties involved, in such a manner, that performance is still possible, but “ruinous” for the performing party, in a way that “*it cannot reasonably be expected*”<sup>74,75</sup>. The event, which stipulates hardship is unforeseeable, out of the control of the performing party, occurs after the conclusion of the contract and alters significantly the equilibrium of the agreement<sup>76-77</sup>.

Hardship and its legal consequence -adaptation of the agreement- is not as widely propagated as the *pacta sunt servanda* doctrine. Surely, many legal systems globally have embedded hardship clauses in their jurisdictions and others in their case law and literature<sup>78</sup>. However, the concept of hardship is not unanimous among the various legal systems. In the French legal system we encounter the term “*imprévision*”, with emphasis on the prerequisite for hardship, in German jurisdiction the term “*Wegfall der Geschäftsgrundlage*”, namely the disappearance of the basis of the contract. The Italian code speaks of “*onerosità eccessiva sopravvenuta*”, which gives emphasis on the effect of the change in circumstances<sup>79</sup>. Adaptation is another term used in this concept, but the term refers mostly to the legal effects of hardship<sup>80</sup>. According to another view, the term adaptation is wider and includes hardship<sup>81</sup>.

The approach of the existing domestic legal systems has been criticized by scholars for creating “*a juridical babel*”<sup>82</sup>. The contradicting perspectives among the legal domestic solutions, have led to a different approach by the international commercial trade practice, according to which hardship is dealt with the insertion of specific clauses, which allow parties to adapt their contractual agreement to the changed circumstances<sup>83</sup>. Hardship clauses are introduced into contracts to

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<sup>74</sup> Baranauskas E., Zapolskis P. (2009). *The effect of change in circumstances on the performance of contract*, Jurisprudence, 2009, Nr. 4 (118), 198

<sup>75</sup> Melis, W. (1984). *Force Majeure and Hardship Clauses in International Commercial Contracts in View of the Practice of the ICC Court of Arbitration*. Journal of International Arbitration, Kluwer Law International, 215.

<sup>76</sup> Jenkins, S.H., (1998), *Exemption for nonperformance: UCC, CISG, Unidroit principles – A comparative Assessment*, Tulane Law Review, 1998 (72), 2027.

<sup>77</sup> In this context, the on-going Sars-CoV-2 pandemic is also perceived as a hardship event, in cases when performance is not completely impossible, but there is a significant economic disequilibrium in performance, in Berger, K., Behn D., (2020). *Force Majeure and Hardship in the age of Corona: A historical and comparative study*, McGill Journal of Dispute Resolution, 6 (4), 128-129.

<sup>78</sup> Maslow, D., (1992). *Hardship and Force majeure*. American Journal of Comparative Law, 40 (3), 658.

<sup>79</sup> Tallon, D. (2004). Hardship. Hartkamp et al, *Towards a European Civil Code*, 2004 (9), 499-501, 500. Available at <https://www.trans-lex.org/118150> [accessed on 15/01/2021].

<sup>80</sup> Baranauskas E., Zapolskis P. (2009). *The effect of change in circumstances on the performance of contract*, supra note 74, 201; Maslow, D., (1992). *Hardship and Force majeure*, supra note 78, 661.

<sup>81</sup> Al Qurashi, Z., (2005). *Renegotiation of International Petroleum Agreements*, supra note 18, 289

<sup>82</sup> Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 138.

<sup>83</sup> *Ibid.*, 149

ensure, that the change of circumstances will not interfere with the equilibrium of the parties' agreement and that there is potential for perpetuation of the contractual arrangement. Especially in long-term agreements, this is extremely important. A hardship clause serves as a legal basis for renegotiation of the contract by the disadvantaged party and if the negotiation fails, then it entitles the party to seek the court's assistance<sup>84</sup>.

In the context of unifying the different approaches offered by different legal systems the Unidroit Principles of International Commercial contracts, published by the International Institute for the Unification of Private Law<sup>85</sup> have served as a breakthrough. Despite the fact that the principles are a soft – law instrument<sup>86</sup> they manage to deal successfully with the legal aspect of changed circumstances by introducing the concepts of “hardship<sup>87</sup>” and “force majeure<sup>88</sup>” with special relevance to long-term agreements<sup>89</sup>. Particularly for hardship the Principles have demonstrated that the sanctity of contracts is not an absolute term and can be set aside when “*supervening events lead to a fundamental alteration*” of the contractual equilibrium<sup>90</sup>. Moreover, the Principles have served as a reconciliation instrument between common law and civil law legal systems. Last but not least, they have proposed that a court's decision is not only limited to the interpretation of law, but may also be oriented towards the adaptation of the contract<sup>91</sup>.

In case changed circumstances constitute hardship, the Principles read:

*“Where the performance of a contract becomes more onerous for one of the parties, that party is nevertheless bound to perform its obligations subject to the following provisions on hardship<sup>92</sup>”* and,

*“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;*

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<sup>84</sup> Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, The International Business Law Journal 2003 (4), 15.

<sup>85</sup> Articles 6.2.1, 6.2.2, 6.2.3 of the Unidroit Principles (2016), 217-226.

<sup>86</sup> Bonell M.J., (2018). *The Law governing international commercial contracts and the actual role of the Unidroit Principles*, Unif. Law Review, 2018 (23), 38.

<sup>87</sup> Articles 6.2.1 - 6.2.2- 6.2.3 of the Unidroit Principles (2016), 217-226.

<sup>88</sup> Article 7.1.7 of the Unidroit Principles (2016), 240-242.

<sup>89</sup> Article 6.2.2 of the Unidroit Principles (2016), 222.

<sup>90</sup> Article 6.2.1 of the Unidroit Principles (2016), 217.

<sup>91</sup> Maslow, D., (1992). *Hardship and Force majeure*, supra note 78, 663

<sup>92</sup> Article 6.2.1 of the Unidroit Principles (2016), 217.

(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<sup>93</sup>”.

Therefore, under the Principles, there is hardship when the events fundamentally alter the equilibrium of the contract. Moreover, the occurrence of the events took place or came in knowledge of the performing party after the conclusion of the contract (criterion of unforeseeability); second, the performing party could not have taken into consideration the event at the conclusion of the contract and third, the event was “*beyond the control*” of the said party<sup>94</sup>.

## 2.2. The definition of an onerous performance.

Articles 6.2.1 and 6.2.2 of the Unidroit Principles state: “*where the performance of a contract becomes **more onerous** for one of the parties, that party is nevertheless bound to perform its obligations...”, and, “there is hardship where the occurrence of events **fundamentally** alters the equilibrium of the contract” and other conditions exist<sup>95</sup>.*

It is widely proposed, that the performance of a contract becomes *more onerous* where the occurrence of events *fundamentally alters the equilibrium of the contract*. That means that *only* a fundamental alteration can justify the adaptation of the contract<sup>96</sup>, so it is justified only when it has an extraordinary character<sup>97</sup>.

According to the Articles’ commentary, the term “*fundamental*” is expressed in two different ways. Primarily, by a significant *increase of the cost of the performance*, for instance, an increase in the price of raw materials or the enactment of more expensive production procedures due to a change in safety regulations. Second, by a *significant decrease of the value of a performance*, monetary or not, which affects the receiving party, for example, major changes in the market condition such as increase of inflation. This alteration however, does not mean that normal financial risks should end up by being the burden of the other contractual party<sup>98</sup>. In any event, if an alteration is “*fundamental*” or not, that depends upon the specific circumstances of the case<sup>99</sup>.

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<sup>93</sup> Article 6.2.2 of the Unidroit Principles (2016), 218. The content of these articles contain similar provision as article 2.117 of the Principles of European Contract Law (PECL)

<sup>94</sup> Maslow, D., (1992). *Hardship and Force majeure*, supra note 78, 662

<sup>95</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 22

<sup>96</sup> Article 6.2.1 Unidroit Principles (2016), 218-219

<sup>97</sup> Maslow, D., (1992). *Hardship and Force majeure*, supra note 78, 661.

<sup>98</sup> *Ibid.*, 662

<sup>99</sup> Article 6.2.1 Unidroit Principles (2016), 219.

According to Fucci,<sup>100</sup> several cases in international case law which constitute a *fundamental change* in the performance of a contract, are: a) an alteration of more than 50% of the cost of the value of the performance<sup>101</sup>, b) a non-expected 80% devaluation of a country's currency, c) a ten-times augmentation of the price of storage due to a changed governmental regulation after the conclusion of the contract<sup>102</sup>, d) the unexpected disappearance of a market after the conclusion of a contract, e) the "change of the initial assumptions with respect to which the parties committed themselves"<sup>103</sup> f) the case of a company that risked to collapse<sup>104</sup>, by being forced to stay bound to its initial arrangement.

Furthermore, an illustrative case is the *CMS Gas vs. Argentina*. In 1992, Argentina privatized its natural gas transmission and distribution sector. CMS Gas, a private company, purchased 30% of *Transportadora de Gas del Norte* (TGN), one of the two natural gas transportation companies in the country. TGN's license contained a particular term that the tariffs would be in US dollars, while a conversion to pesos was to take effect at the point of the billing procedure. Moreover, the tariffs would be adjusted every semester, as well as every five years, in order to maintain the real value of the transaction. However, the economic situation in Argentina deteriorated in 1999. CMS Gas claimed devaluation of the currency and therefore inability to service its debt. Furthermore, it pointed that due to the devaluation, TGN operating costs had diminished and the investment value of CMS Gas, was seriously affected. CMS Gas claimed an adjustment of the TGN license and the Argentinean government raised a hardship argument. Surprisingly, the arbitral tribunal stated that the "*Argentine (economic) crisis*" was severe but "*did not result in total economic and social collapse*," thus not characterizing the economic crisis period a *fundamental* alteration<sup>105</sup>. The tribunal rejected Argentina's hardship claim.

### 2.3. The additional requirements for hardship

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<sup>100</sup>Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 22

<sup>101</sup> According to Maslow as well, an alteration of 50% suffices, in Maslow, D., (1992). *Hardship and Force majeure*, supra note 78, 662; On the contrary, according to Pirozzi, "*jurists, practitioners, judges and also arbitrators have continuously suggested that the alteration should be at least 100%*" in Pirozzi, R. (2012). *Developments in the Change of Economic Circumstances Debate?* Vanderbilt Journal, 106.

<sup>102</sup> In this case the price of waste storage went up 10 times, after the conclusion of a contract between the government and a party generating waste, in Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 22.

<sup>103</sup> Oppetit, B., (1974). *L' Adaptation des Contrats Internationaux aux Changement de Circonstances: La Clause de Hardship*, Clunet 1974, 797, available at: <https://www.trans-lex.org/127600> [accessed on 15.01.2021]

<sup>104</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 23

<sup>105</sup> *CMS v Argentina*, ICSID Case Nr. ARB/01/8 (May, 12.2005).



### 2.3.1. Events occur or become known after the conclusion of the contract. The “unforeseeability” of events

According to the Principles, the change of circumstances must eventuate, or become known to the aggrieved party, *after* the conclusion of the contract.

The change of circumstances cannot lead to a claim of hardship if the aggrieved party could take the change of circumstances into account *at the time of the conclusion of the agreement*. If the events were foreseeable, then the performing party should consider them at the conclusion of the contract<sup>106</sup>. In other words, the events should be unforeseeable, meaning that the disadvantaged party must not have “*assumed the risk of the change of circumstances*”. The assumption does not have to be specifically worded, but it can come as a conclusion derived from “*the nature of the contract*”<sup>107</sup>. For instance, if the parties have an indexation clause for prices in their contract, the modification of prices outside indexation clauses will burden the disadvantaged party<sup>108</sup>.

The Principles set the following illustration: “*A agrees to supply B with crude oil from country X at a fixed price for the next five years, notwithstanding the acute political tensions in the region. Two years after the conclusion of the contract, a war erupts between contending factions in neighboring countries. The war results in a world energy crisis and oil prices increase drastically. A is not entitled to invoke hardship because such a rise in the price of crude oil was not unforeseeable*”<sup>109</sup>. This illustration demonstrates that the rise of the price of crude oil was foreseeable, due to the political tensions in the region prior to the eruption of war<sup>110</sup>.

According to Fucci<sup>111</sup>, there are certain cases, which do not consist of unforeseeability. These events are for instance “*dramatic changes in markets for products*”<sup>112</sup>, non-favorable economic circumstances in a country<sup>113</sup>, severe fluctuations of currency, failure of a central bank to grant

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<sup>106</sup> Perillo, J.M., (1997). *Force majeure and hardship under the UNIDROIT principles of International Commercial Contracts*, Tulane Journal of International and Comparative Law, 1997 (5), 23.

<sup>107</sup> Unidroit Principles (2016), 221

<sup>108</sup> Mascow, D., (1992). *Hardship and Force majeure*, supra note 78, 663.

<sup>109</sup> Article 6.2.1 Unidroit Principles (2016), 220.

<sup>110</sup> Perillo, J.M., (1997). *Force majeure and hardship under the UNIDROIT principles of International Commercial Contracts*, supra note 106, 23

<sup>111</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 27.

<sup>112</sup> In ICC Award nr. 2216 (1974) the claim of the disadvantaged party was a decrease of the price of petroleum in between the period of the conclusion of the contract and the delivery of the product. The arbitral tribunal refused hardship on the grounds of the decrease of the price did not constitute a dramatic change of economic circumstances but a mere fluctuation of the market price of the product.

<sup>113</sup> In the case CMS v Argentina the arbitral tribunal accepted that the country's economic problems were not unforeseeable in Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 18

authorization in foreign currency, foreign exchange control regulations at the time of the conclusion of a contract<sup>114</sup>, war between two countries with a history of hostilities. Moreover, hardship can be evoked if the change of circumstances escalated “dramatically” during the existence of the agreement.<sup>115 116</sup>.

In the aforementioned case of CMS vs. Argentina, by rejecting the Argentinean claim, the arbitral tribunal in fact concluded that the economic events that the country faced were not unforeseeable, so the specific criterion was not met<sup>117</sup>.

Similarly, in both the 3099 and 3100 ICC cases, a buyer of petroleum products claimed change of circumstances<sup>118</sup> upon the refusal of its central bank to authorize payment in foreign currency. The tribunal however assessed that the foreign exchange regulations had already taken place at the time of the bank’s refusal and that the claiming party was already aware of the existing regulations and rejected the claim.

In another case<sup>119</sup>, a Norwegian company did not perform according to its purchase agreement because of the decrease of the price of petroleum by more than half during the period between the conclusion of the contract and the delivery of the product. The company based its claims on the “loss of foreign currency”. The tribunal argued that the non-payment due to the foreign currency fluctuation does not constitute unforeseeability<sup>120</sup>.

### **2.3.2. The concept of externality to the Party claiming hardship**

The events responsible for the change of circumstances must not appear as a misconduct of the disadvantaged party, claiming hardship. Otherwise, arbitral tribunals and courts would face the

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<sup>114</sup> Cases Nr. 3099 and 3100 of the ICC (1974).

<sup>115</sup> Article 6.2.1 Unidroit Principles (2016), 220; Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 22.

<sup>116</sup> The illustration of the Unidroit Principles is characteristic: “In a sales contract between A and B the price is expressed in the currency of country X, a currency the value of which was already depreciating slowly against other major currencies before the conclusion of the contract. One month thereafter a political crisis in country X leads to a massive devaluation of its currency of the order of 80%. Unless the circumstances indicate otherwise, this constitutes a case of hardship, since such a dramatic acceleration of the loss of value of the currency of country X was not foreseeable”, in Unidroit Principles (2016), 220-221.

<sup>117</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 14.

<sup>118</sup> Actually, the agreement contained a force majeure clause.

<sup>119</sup> ICC Nr. 2216 case (1974)

<sup>120</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 20

paradox of having to examine hardship, responding to a claim made by the party responsible for the change of circumstances<sup>121</sup>.

An intriguing question arises when the aggrieved party claiming hardship is a state company of the host country. Can i.e. a state company to an oil contract claim hardship if the event that triggers the change of circumstances is the outcome of government action? According to Berger<sup>122</sup>, the host state is never entitled to claim hardship if the event has occurred because of the state's action. An illustrative example of the concept of externality is demonstrated in two ICC cases<sup>123</sup> upon the sale of crude oil and refined oil products between two African countries. After the conclusion of the contract, the payment of the total sum of invoices did not take place at the agreed time. The claim of the disadvantaged party was that there was no way it could surmount the exchange control regulations of the country and obtain authorization for payment in US dollars in order to pay the seller. The Tribunal, considering the case in terms of externality assessed that this was "*an event which comes from outside the person who invokes it*"<sup>124</sup>.

### 2.3.3 The assumption of risk

Under the fourth subparagraph of the Unidroit principles the aggrieved party cannot claim hardship if it has assumed the risk of an event and the consequent change of circumstances. The risk does not have to be explicitly mentioned, but it can be linked with the nature of the contract<sup>125</sup>.

In the *CMS Gas v. Argentina case*, the government of Argentina based its claims upon the hardship provision of its civil code<sup>126</sup> asking for termination of the contract. The arbitral tribunal rejected the claims of the Argentine government, because it actually had taken into account the deterioration of its economic situation and it had assumed the risk<sup>127</sup>.

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<sup>121</sup> Ibid., 27

<sup>122</sup> Berger, K., (2003). *Renegotiation and adaption of international investment contracts: The role of contract drafters and arbitrators*, supra note 23, 1352.

<sup>123</sup> Supra note 114.

<sup>124</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 27.

<sup>125</sup> Article 6.2.2 Unidroit Principles (2016), 221.

<sup>126</sup> Article 1198 of the Civil Code.

<sup>127</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 14

## 2.4. Legal effects of Hardship

### 2.4.1 Termination or renegotiation of the contract?

When performance of a contract becomes more onerous than the disadvantaged party will not be able to perform under its initial obligations. Under article 6.3.3 of the Unidroit principles the disadvantaged party can claim renegotiations in order to modify the contract to the changed circumstances<sup>128</sup>, but is not entitled “to withhold performance”<sup>129</sup>. However, the Principles introduce an exemption only “in extraordinary circumstances”<sup>130</sup>. If the contracting parties do not agree upon revision of their contract, they can ultimately seek a solution by resorting to court or arbitration, within “a reasonable time-frame”. It is then up to the court to evaluate the situation and to either adapt the contract, as a way to restore its original equilibrium or decide upon its termination<sup>131-132</sup>. The Principles’ commentary point out the freedom of the court or the arbitral tribunal towards any direction<sup>133</sup>. On the contrary, under some national jurisdictions<sup>134</sup>, the aggrieved party must first claim termination of the contract and only under this prerequisite will the counterparty offer an adjustment of the contract terms<sup>135</sup>. Illustrative in this direction is again the case of *CMS Gas v. Argentina*, in which TGN argued that the hardship provision of the Argentinean Civil Code was in fact inapplicable because the aggrieved party had not resorted to court asking for termination of the contract and decided unilaterally upon the changes of its license term. The tribunal was influenced by this argument, stating that (indeed) “*this approach would have made any unilateral determination unnecessary*”<sup>136</sup>.

In any event, an aggrieved party must raise the issue of hardship well before the point where its contractual obligations are impossible. Then, it is up to the counterparty, to assess whether the

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<sup>128</sup> Perillo, J.M., (1997). *Force majeure and hardship under the UNIDROIT principles of International Commercial Contracts*, supra note 106, 25.

<sup>129</sup> Article 6.2.3 (2), Unidroit Principles (2016), 223

<sup>130</sup> Article 6.2.3 (4), Unidroit Principles (2016) 225

<sup>131</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 31.

<sup>132</sup> In the case of the Sars-CoV-2 pandemic, it is argued that courts and arbitrators have to take into consideration the exceptional character of the situation, so neither one of the contracting parties must bear the results of such an event alone, in Berger, K., Behn D., (2020). *Force Majeure and Hardship in the age of Corona: A historical and comparative study*, supra note 77, 128-129.

<sup>133</sup> Article 6.2.3 (4), Unidroit Principles (2016), 225-226.

<sup>134</sup> The Brazilian Code for instance.

<sup>135</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 31.

<sup>136</sup> *Id.*

disadvantaged party's claim constitutes a case for hardship according to national law or the international tribunal jurisprudence<sup>137</sup>.

#### **2.4.2. Negotiations in good faith and the exercise of efforts to overcome the effect of changes in circumstances**

Under the Unidroit Principles,<sup>138</sup> *“the disadvantaged party is entitled to request renegotiations”*. Since hardship constitutes a fundamental alteration of the equilibrium of the contract, the disadvantaged party may request renegotiations in order to adapt the contractual terms according to the changed circumstances<sup>139</sup>. The request must take place without undue delay, depending on the particular circumstances of the case. The commentary of the Principles points out that a delay may affect the judgment of the court on the question of the existence of hardship and the alleged alteration of the equilibrium of the contract. However, according to some authors a “delayed request” is not to be rejected automatically<sup>140</sup>.

Furthermore, the disadvantaged party has a duty to indicate in a complete context the grounds on which the request for renegotiations are based, meaning that an unsuccessful indication may result in dismissing the hardship claim.

In national legal systems where there is a provision of hardship and the disadvantaged party has raised such claim, the counterparty cannot simply refuse to consider or disregard the claim<sup>141</sup>, the contracting parties having the duty to cooperate in good faith. Although good faith is not expressly mentioned in the relevant articles of hardship in the PICC, good faith and the obligation to renegotiate are subject to this general principle of law, by indirect reference to articles 1.7 (fair dealing) and 5.1.3 (duty of co-operation) of the principles. As their commentary points out: *“The disadvantaged party must honestly believe that a case of hardship actually exists and not request renegotiations as a purely tactical manoeuvre”*,<sup>142</sup> meaning that the contracting parties must act *“in a constructive manner”* by *“providing all the necessary information,”* avoiding obstructions. Moreover, *“a party who negotiates or breaks off negotiations in bad faith is liable for the losses*

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<sup>137</sup> Ibid., 32

<sup>138</sup> Article 6.2.3 Unidroit Principles (2016), 223.

<sup>139</sup> Id.

<sup>140</sup> Perillo, J.M., (1997). *Force majeure and hardship under the UNIDROIT principles of International Commercial Contracts*, supra note 106, 25.

<sup>141</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 32

<sup>142</sup> Article 6.2.2 Unidroit Principles (2016), 221.

caused to the other party. In the event the parties do not reach agreement either party may apply to the court”<sup>143</sup>.

The duty to negotiate in good faith is not always accompanied by the obligation to indemnify the disadvantaged party. This is particularly true for oil and gas contracts. While someone would expect the insertion of an indemnification provision in a hardship clause, this is seldom the case<sup>144</sup>.

## 2.5. The role of the Court

Even though the contracting parties act in good faith, they do not always reach an agreement; in this case, a failure to agree is not attributed to the parties and does not indicate a breach of contract<sup>145</sup>.

If adaptation of the contract is not achieved, the contractual agreement will continue to be valid unless otherwise indicated by the parties. In the international trade practice, parties to a contract not reaching an agreement resort to court “within a reasonable time”.<sup>146</sup> Courts (or arbitrators) are entailed to determine the terms of adaptation<sup>147</sup>. This is stipulated in the 2478 Award<sup>148</sup>. In this arbitral award, which involved a transaction of crude oil, the parties had inserted a clause providing for the renegotiation of the contract, should the rate of exchange be modified. The oil prices increased and one of the parties claimed hardship upon the “change in the monetary balance”. Negotiations failed. The performing party asked for discharge of performance. The case was brought before arbitration. The arbitral tribunal concluded that a price rise did not amount to a change of the currency balance, so the claiming party should not have asked for renegotiations. In addition, it stressed out that the failure of the parties to agree did not constitute breach of contract as the obligation of the parties was just to negotiate in good faith and that the failure to agree would not bring termination of the contract, because this was not the will of the parties expressed in their contract.

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<sup>143</sup> Perillo, J.M., (1997). *Force majeure and hardship under the UNIDROIT principles of International Commercial Contracts*, supra note 106, 25

<sup>144</sup> Montembault, B., (2003). *La stabilisation des contrats d’etat a travers l’exemple des contrats petroliers – Le Retour des dieux sur l’Olympe*, supra note 13, 626-627.

<sup>145</sup> Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 154

<sup>146</sup> Article 6.2.3 Unidroit Principles (2016), 225.

<sup>147</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 34.

<sup>148</sup> ICC Award Nr. 2478 in Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 154.

According to Professor Schmitthoff, hardship clauses dealing with economic imbalance must always be accompanied by sanctions<sup>149</sup>, meaning that the legal effects of lack of agreement must be provided for in the contract.

In case of failure of negotiations, the court or the arbitrator has actually four alternatives<sup>150</sup>.

The first of them is re-adaptation of the contract in order to restore its contractual equilibrium in which the court usually assesses “*a fair distribution of the losses between the parties*”<sup>151</sup> that may include a price adaptation or not. In case the court decides upon the inclusion of an adaptation term it will not considerate the full loss of the aggrieved party since it will examine the counterparty’s benefit from the anticipated performance. Such demonstration of the “*fair distribution of losses*” is demonstrated in the CMS award in which the Tribunal stated “*Argentina should not entirely assume the economic consequences of the License’s adjustment procedures*” in spite of the fact that it rejected the hardship claim of the Argentinean government. In the case of ICC Award Nr. 2508<sup>152</sup>, the seller claimed that the augmentation of the petroleum world price by triple, amounted to hardship. The seller proposed that the prices should increase so as to equalize the world petroleum market prices and the tribunal considered this proposal an equitable solution, resolving the case in a way so to render the “*performance bearable*”<sup>153</sup> taking into consideration the counterparty’s interests.

Except for the “*fair distribution of the losses between the parties*”, international arbitration cases indicate similar standards in order to maintain an equilibrium between the parties’ interests. These provisions are summarized as follows: a) adjustment of the contract so as “to eliminate the cause of hardship”, b) insertion of an alternative term which “reasonably allows for the consequences of the event”, c) re-establishment of the contractual equilibrium, d) “granting a reduced purchase price to the buyer while allowing a sufficient profit margin to the seller”, e) the avoidance of the strict application of contractual clauses, without a “modification of the economics of the agreement”<sup>154</sup>.

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<sup>149</sup> Id.

<sup>150</sup> Jenkins, S.H., (1998). Exemption for nonperformance: UCC, CISG, Unidroit principles – A comparative Assessment, supra note 76, 2029.

<sup>151</sup> Article 6.2.3 Unidroit Principles (2016), 226.

<sup>152</sup> Nr. 2508 (1976) ICC Award, in Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 37.

<sup>153</sup> Id.

<sup>154</sup> Ibid., 38

The court's second and third choice is to direct the parties to return to their negotiations in order to reach an agreement or confirm the terms of the contract, as they originally stand.

The last alternative is termination of the contract. The contract is terminated by the court only when there is good reason for termination. In this case, the court decides upon the date and the respective termination terms. Otherwise, the court adapts the contract itself<sup>155</sup>.

## 2.6. Special considerations when drafting a hardship clause

Long-term agreements are particularly vulnerable to economic crises. Fortunately, in most legal systems the contracting parties in a long-term oil or gas contract, enjoy some freedom in designing their hardship clauses, should they choose to include one in their contractual arrangement. It is therefore considered wise for drafters to extensively study the provisions of the law governing the contract on hardship, as well as their interpretation by courts, and if they seem reasonable, then the contract may not include a particular hardship clause.

On the contrary, if the standards of the law of the contract chosen by the parties proves too liberal and does not serve this purpose in an efficient manner, then the contracting parties should define more clearly the triggering events and the terms of adjustment of the contract. The incorporation of certain indexation and stabilization clauses is also advisable in order to "create a system of internal regulation"<sup>156</sup> should a hardship claim arises. Thus, the combination of price review and hardship clauses may serve as adequate protection in the face of severe economic disruptions: the price review clauses deal with foreseeable changes but the addition of a hardship clause offers an *extra* protection vis-à-vis the changes not foreseen by the price review scheme<sup>157</sup>.

Furthermore, crucial is the inclusion of a provision that the parties should negotiate in good faith. Although the parties are not obliged to agree, the inclusion of such a provision is important because even if parties fail to agree, the obligation to negotiate in good faith may become enforceable by courts<sup>158</sup>.

Another feature, common in international investment agreements, is the inclusion in the hardship clause of a provision of third party intervention, in case the contracting parties disagree on

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<sup>155</sup> Mascow, D., (1992). *Hardship and Force majeure*, supra note 78, 663.

<sup>156</sup> Kemp, K. (1983). *Applying the hardship clause*. *Journal of Energy and Natural Resources Law*, 1(2), 119.

<sup>157</sup> *Id.*

<sup>158</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 41



the adjustment of their contract. The parties are also free to agree if this third party intervention will have a mandatory or advisory role. If mandatory, the parties are obliged to respect the intervention<sup>159</sup>.

In general, a hardship clause should be designed in a way as to serve a double purpose. In its first part, the clause should specify the -unforeseeable at the conclusion of the contract- circumstances and in its second part the legal consequences of the hardship situation. Initially the hardship clause may contain a general indication of the circumstances changed, expressed in a broad way so to include more cases. General provisions such as “*in case of a serious occurrence of a political economic or financial nature*” or “*if the monetary situation were to change*” or even more analytical clauses can be observed, such as “*in the case of new import or export laws*”. However, the best practice is considered to use clauses expressed generally with specific hypotheses used as indications. In its second aspect a hardship clause usually refers to the legal consequences should a hardship situation appears, such as temporary suspension of performance, renegotiation, modification, arbitration, or even termination.

As a first solution, parties may choose to join forces in order to adapt their contract, ascertaining its contractual balance, using different criteria, which vary from objective to subjective. Objective criteria include formulas such as *adjustment of prices to a specific level* while subjective ones involve general principles, such as good faith and equity<sup>160</sup>.

The case of the dispute of *Superior Overseas Development Corporation and Phillips Petroleum Co. LTD vs. British Gas Corporation* marked several issues, which may arise from the drafting of a hardship clause. The case illustrates the major problems that can arise through a general and vague drafting of a clause, a problem that was finally resolved by the court. The transaction concerned several long-term agreements on the supply of natural gas between British Gas Corporation and Phillips Petroleum and contained a price review and a hardship clause. The producers claimed hardship against British Gas. The parties’ disagreement was based on the wording of the hardship clause and specifically the provision of “*substantial economic hardship*” included in the clause. The second point of disagreement had to do with the quantity of the remedies involved. The British Gas claimed that only hardship after the issuing of the decision should

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<sup>159</sup> Ibid., 42.

<sup>160</sup> Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 151-153.

be taken into consideration, while the producers considered as effective date the date of the inception of hardship. The Court of Appeal decided in favor of the producers<sup>161</sup>.

Another clause, cited by professor Schmitthoff,<sup>162</sup> clearly illustrates the circumstances under which the performance of the party is considered to be imbalanced by hardship. The clause reads: *“When entering into this Agreement the parties contemplate that the effects and/or consequences of this Agreement will not result in economic conditions [which are substantial Hardship] to any of them; provided that they will act in accordance with sound marketing and efficient operating practices. They therefore agree on the following: Substantial Hardship shall mean if at any time, or from time to time during the term of this Agreement, without default of the party concerned, there is the occurrence of an intervening event or change of circumstances beyond said party’s control when acting as a reasonable and prudent operator, such that the consequences and effects of which are fundamentally different from what was contemplated by the parties at the time of entering into this Agreement (such as, without limitation, the economic consequences and effects of a novel economically available source of energy), which consequences and effects place said party in the situation that then and for the foreseeable future all annual costs (including, without limitation, depreciation and interest) associated with or related to the processed gas which is the subject of this Agreement exceeded the annual proceeds derived from the sale of said gas. Notwithstanding the effect of other relieving or adjusting provisions of this Agreement the party claiming that it is placed in such position as aforesaid may by notice request the other for a meeting to determine if said occurrence has happened and if so to agree upon what, if any, adjustment in the price then in force under this Agreement and/or other terms and conditions thereof is justified in the circumstances in fairness to the parties to alleviate said consequences and effects of said occurrence. Price control by the Government of the state of the relevant Buyers(s) affecting the price of natural gas in the market shall not be considered to constitute substantial Hardship”*.

Apart from the circumstances indicating hardship, the clause also provides for a special procedure that the parties should follow in order to evaluate hardship; in this particular clause the parties are entitled to meet in order to decide whether hardship has occurred as well as the adjustments necessary for the viability of the project<sup>163</sup>.

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<sup>161</sup> Kemp, K. (1983). *Applying the hardship clause*, supra note 156, 120-121.

<sup>162</sup> Al-Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*, supra note 4, 5-6.

<sup>163</sup> *Ibid.*, 7.

The clause of hardship contained in the “*Ekofisk Natural Gas sales agreement*”<sup>164</sup> demarcates many of the provisions illustrated by the Unidroit principles such as the externality of the changed circumstances to the party claiming hardship, the unforeseeability of the event, the fundamentality of events, specified economic consequences and the effective date of the hardship situation. According to the clause, “if during the term of this Agreement, *without default of the party concerned*, there is the occurrence of an intervening event or change of circumstances *beyond the said party's control* when acting as a reasonable and prudent operator, such that the consequences and effects of which are fundamentally different from what was contemplated by the parties at the time of entering into this Agreement ..... which consequences and effects place said party in the situation that then and for the foreseeable future all annual cost, associated with or related to the processed gas which is the subject of this Agreement exceed the annual proceeds derived from the sale of said gas.”

This clause is considered a well - drafted example of a hardship clause.

## **2.7. The International Commercial Chamber (ICC) hardship clauses**

ICC hardship clauses<sup>165</sup> are model clauses that parties choose to incorporate into their contractual arrangements rather than drafting their own. However, as many experts point out, these model clauses should also be modified, according to the trade in issue.

The model clause is actually repeating the Principles in many aspects. Primarily, it links hardship with an excessively onerous circumstance. It points out that the event must be outside the party's reasonable control, and that it must appear after the conclusion of the contract. Last of all, it demarcates the unforeseeability of the event and the fact that contracting parties could not have avoided its effects. It is, however, different from the principles in the aspect of the legal consequences. While the principles do not refer to the termination of the contract according to the free will of the parties, the ICC model clause does<sup>166</sup>.

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<sup>164</sup> Ekofisk natural gas sales agreement in Phillips Petroleum Cy., Norway Group and the Gas de France Group in Kemp, K. (1983). *Applying the hardship clause*, supra note 156, 122.

<sup>165</sup> The March 2020 ICC hardship clause in <https://iccwbo.org/content/uploads/sites/3/2020/03/icc-forcemajeure-hardship-clauses-march2020.pdf>, accessed in 30.03.2021.

<sup>166</sup> Kessedjan, C., (2005). *Competing approaches to Force Majeure and Hardship*, International Review of Law and Economics, 2005 (25), 424-425.

### 3. FORCE MAJEURE AND THE CONTRIBUTION OF FORCE MAJEURE CLAUSES IN OIL AND GAS CONTRACTS

#### 3.1 Introduction

Similarly to Hardship, force majeure also derives from Roman Law,<sup>167</sup> the principle being inherent in almost all national legal jurisdictions. The term, which is used to describe supervening events which render a performance impossible, is referred to as an “Act of God.” The Iran-US Claims Tribunal has accepted that force majeure is qualified as a general principle of law, applicable even when the contract does not contain a relevant provision<sup>168</sup>.

According to the Unidroit Principles’ relevant article<sup>169</sup>, under force majeure, the party is excused if it proves that the non-performance was due to an impediment beyond its control, and the party could not reasonably be expected to have taken it into consideration at the time of the conclusion of the contract or to have avoided or overcome it or its consequences.

The Principles’ contribution to the principle is particularly noteworthy. The Principles include the doctrine in the chapter of non-performance, separating it from the relevant but not identical concepts existing in common and civil law countries<sup>170</sup>. They also explicitly underline the significance of the doctrine for long-term contracts<sup>171</sup>. What is more important is that the PICC have assessed that due to the capital intensity and duration of long-term contracts, parties may be interested in continuing rather than ending their contractual arrangements. Consequently, the PICC actually provide that the parties may choose to continue their business relationship and resort to termination only as a last option<sup>172</sup>.

According to Article 7.1.1, the performing party is liable for its failure to perform, unless it proves that “*the non-performance was due to an impediment beyond its control*”. The no fault prerequisite mirrors the “*principle of strict contractual liability*”, also followed by other domestic

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<sup>167</sup> Berger, K., Behn D., (2020). *Force Majeure and Hardship in the age of Corona: A historical and comparative study*, supra note 77, 90.

<sup>168</sup> In Case Nr. 167 (1986), *Anaconda – Iran Inc., v The National Iranian Copper Industries Company*, in Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, supra note 84, 5; Van den Berg, A., (1998). *International Arbitration of Petroleum disputes: The development of a Lex Petrolea*, Commercial Arbitration Yearbook 1998, Kluwer Law International, 1998 (23), 16.

<sup>169</sup> Article 7.1.7. Unidroit Principles (2016), 240.

<sup>170</sup> Pichonnaz, P., (2015). *Ch. 7 Non-performance, S.1: non-performance in general, Art. 7.1.7. Commentary on the Unidroit Principles of International Commercial contracts*, PICC, Oxford Legal Search Library, 2

<sup>171</sup> Article 7.1.7 Unidroit Principles (2016), 240-242.

<sup>172</sup> Comment 5 § 2 of the Unidroit Principles (2016), 242.

common and civil law systems. Under article 7.1.1 of the PICC, the occurrence of an external event (force majeure) excuses the party from liability. This actually means that when an event, qualified as force majeure, occurs, and this event triggers non-performance, the party is exempted from liability for damages<sup>173</sup>. The performing party is entitled to prove that it has done its utmost towards achieving the result expected by the contractual agreement<sup>174</sup> and the aggrieved counterparty may ask for termination.

It is argued that force majeure contains four basic elements: an event of an external nature takes place, in the sense that the impediment is not part of “the sphere of risk” of the performing party (attributability criterion); the event is unforeseeable, in the sense that the impediment that the performing party did not foresee at the time of the conclusion of the contract, does not deem the party free from liability “if overcoming the impediment was reasonable and possible” (unforeseeability criterion); last, the event’s consequences are unavoidable, (insurmountability criterion); the event renders the performance impossible for a certain period or indefinitely.<sup>175</sup>

The qualification of an event as force majeure “shields” the performing party from its obligation to be held liable for damages. This “default rule” is applicable only when parties have not included a relevant force majeure clause in their contract. When parties do insert a specific clause they may change the legal consequences surrounding the issue, broadening or narrowing the extent of the excuse to the point that they do not produce a “grossly unfair result” as indicated in article 7.1.6 of the PICC<sup>176</sup>.

Unlike hardship, which renders the performance of the party claiming it more onerous, under the force majeure concept, the performance of the aggrieved party is impossible, temporarily or permanently. Moreover, while the aim of hardship is to perpetuate the contract, in force majeure cases we usually deal with termination, at least temporarily<sup>177</sup>. In this context, hardship stands for adaptation, while force majeure does not<sup>178</sup>. Both force majeure and hardship concepts however,

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<sup>173</sup> Firoozmand, M.R. (2016), *Force Majeure Clause in Long Term Petroleum Contracts: Key Issues in Drafting*, Journal of Energy & Natural Resources Law, 24 (3), 425

<sup>174</sup> Pichonnaz, P., (2015). *Ch. 7 Non-performance, S.1: non-performance in general, Art. 7.1.7. Commentary on the Unidroit Principles of International Commercial contracts*, supra note 170, 1-2.

<sup>175</sup> Schwenger I., (2008). *Force Majeure and Hardship in International Sales Contracts*, VUWLR, 2008 (39), 714-719; Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, supra note 84, 5.

<sup>176</sup> Pichonnaz, P., (2015). *Ch. 7 Non-performance, S.1: non-performance in general, Art. 7.1.7. Commentary on the Unidroit Principles of International Commercial contracts*, supra note 170, 3-4.

<sup>177</sup> Id.

<sup>178</sup> Pirozzi, R. (2012). *Developments in the Change of Economic Circumstances Debate?* Supra note 101, 9103; Al Emadi opposes this argument in Al Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*, supra note 4, 1. Moreover, the Principles also stand for the continuation of the contract, ibid nr. 174, 1-2

are related to events with fundamental character, and they are applied “*when the contract performance has reached its limit of sacrifice*”<sup>179</sup>.

### 3.2. Events that constitute Force Majeure

In order to identify an event as one that constitutes force majeure, an important question arises from the nature of the event itself. Natural calamities are generally perceived as a classical category of force majeure events. Force majeure provisions include natural disasters, such as fire, floods, earthquakes, hurricanes etc, but also human events such as man-made events (war, riots, revolutions, strikes, changes in legislation) or man-caused events (explosions, nuclear catastrophes, accidents)<sup>180</sup>.

In general, crucial for the identification of an event as force majeure is not only the eventuation of the impediment, but most importantly, the answer to the question if there is proof of a causal link between the impediment and non-performance<sup>181</sup>.

In order to understand the different aspects of force majeure one has to examine how arbitral tribunals have interpreted the different concepts of the doctrine in petroleum and gas contracts, mainly the attributability, unforeseeability and insurmountability criteria of the party claiming Force Majeure<sup>182</sup>.

#### 3.2.1 Economic change as a Force Majeure event

Macroeconomic crises may affect a state’s ability to perform its contractual obligations in a timely framework. Therefore, due to the lack of an international bankruptcy law, the obligor may have to invoke other legal solutions, such as the force majeure doctrine. In one of the most illustrative cases, the tribunal underlined that “*parties cannot claim unawareness of the risks of macro-economic adversities. Their effects may be extreme but are nonetheless within the*

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<sup>179</sup>Al-Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*, supra note 4, 4.

<sup>180</sup> Horn, N. (1985), *Adaptation and renegotiation of contracts in International Trade and Finance*, Kluwer 1985, 132-133.

<sup>181</sup> Pichonnaz, P., (2015). *Ch. 7 Non-performance, S.1: non-performance in general, Art. 7.1.7. Commentary on the Unidroit Principles of International Commercial contracts*, supra note 170, 5-6

<sup>182</sup>Firoozmand, M.R., Zamani J., (2017). *Force majeure in International contracts: current trends and how international arbitration practice is responding*, *Arbitration International*, 2017 (33), 396.

*contemplation of the signatories*<sup>183</sup>. In uniformity with this approach, other awards, i.e. the *CMS Gas v. Argentina* case, held that “traditional legal excuses, such as force majeure, are not available in this case as the events discussed were foreseeable and foreseen<sup>184</sup>”.

This means that arbitral awards have rejected macroeconomic crises as events that constitute force majeure, due to the lack of the unforeseeability criterion. In the *Russian Indemnity case*<sup>185</sup>, the court held that the payment of a small amount of money (6 million francs) would not constitute as “leading to ruination the interests of a state”. We can therefore assume that in international trade, there is general belief that financial health is a factor always taken into account by the contracting party<sup>186</sup>. A series of awards arising from the price fluctuations of fossil fuels in the Middle East in the 1970s demonstrated again that “deterioration of the oil market was foreseen and foreseeable”, thus rejecting the force majeure claim<sup>187</sup>.

### 3.2.2. War as an event of Force Majeure

Force majeure may be attributed to war and military conflicts, as in these events the contracting parties may actually become particularly unable to perform. Non-performance is not only attributed to physical obstacles but also to human life threat (i.e. a party’s employees). In *ICC Case No. 19299 of Gujarat Petroleum Corporation v. Yemen*, the arbitral tribunal held that the ongoing situation in Yemen constituted a force majeure situation because “it prevented the consortium from sending its personnel in Yemen to acquire seismic data”<sup>188</sup>.

Force Majeure may serve as defense for the party claiming it, if it successfully proves that certain acts of war have rendered its performance impossible. As in the case of the Arab-Israeli war, “force majeure would be relevant if the war prevented the party from putting goods on board ship”. Similarly, in other cases, international tribunals asserted that an event is qualified as force majeure event, if it “materially renders the obligation impossible”<sup>189</sup>.

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<sup>183</sup> The “Himpurna v. Republic of Indonesia case”, *Ibid.*, 411

<sup>184</sup> *Ibid.*, 413

<sup>185</sup> The Russian Indemnity Case, The Hague reports, (1912), 297, *ibid.*, 412.

<sup>186</sup> Perillo, J.M., (1997). *Force majeure and hardship under the UNIDROIT principles of International Commercial Contracts*, *supra* note 106, 16.

<sup>187</sup> Firoozmand, M.R., Zamani J., (2017). *Force majeure in International contracts: current trends and how international arbitration practice is responding*, *supra* note 182, 410.

<sup>188</sup> Childs T., (2018). *The current state of international Oil and Gas Arbitration*, *Texas Oil and Gas & Energy* 13(1), 10.

<sup>189</sup> Firoozmand, M.R., Zamani J., (2017). *Force majeure in International contracts: current trends and how international arbitration practice is responding*, *supra* note 182, 397.

As far as the unforeseeability criterion, significant for the qualification of an event as force majeure, arbitral tribunals have judged that the requirement of unforeseeability was not properly met in two cases. In the first<sup>190</sup>, a Hungarian oil enterprise claimed that it refrained from the delivery of an agreed amount of crude oil due to the deterioration of the international oil market, which followed the eruption of the Iran-Iraq war, the claim being rejected by the tribunal with the assertion that “*this development could not be considered as unprecedented*”. In the second case<sup>191</sup>, the court rejected the Turkish claim of force majeure due to the involvement of the Turkish government in the war.

Therefore, a claim of force majeure based on the allegation of war does not automatically render the claim accepted. The claim must certainly survive both the impossibility and unforeseeability tests.

### 3.3.3. Revolution as an event of Force Majeure

By revolution we mean “a change in the way a country is governed, usually to a different political system and often using violence or war”<sup>192</sup>.

During the Iranian rebellion of 1978, many American nationals and contractors had to deal with huge delays or termination of several projects. The companies involved argued that due to the turbulent situation they were faced with force majeure circumstances. These claims brought about a series of cases, where the tribunal accepted the US arguments, because “*the Islamic revolution had created classic force majeure conditions*”.<sup>193</sup>

Similarly to the cases examined in the event of war, the tribunal upheld that force majeure is not only created when there is physical impossibility to perform, but even when a potential threat to the life of the employees lead an enterprise to a decision of evacuation of the country that hosts a project<sup>194</sup>.

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<sup>190</sup> Hungarian State enterprise v Jugoslavenski naftovod (Yugoslav Crude Oil Pipeline) Ad hoc Award, (1984) Yb Comm Arb 69, 70, *ibid.*, 398.

<sup>191</sup> The Michel Makri case (1928), *id.*

<sup>192</sup> The Cambridge Dictionary, available at: <https://dictionary.cambridge.org/dictionary/english/revolution> [accessed on 02.02.2021]

<sup>193</sup> The Gould Marketing, Inc vs. Ministry of National Defence case, in Firoozmand, M.R., Zamani J., (2017). *Force majeure in International contracts: current trends and how international arbitration practice is responding*, *supra* note 182, 399

<sup>194</sup> The Lockheed Corporation v. The Government of Iran, *ibid.*, 400



Noteworthy in the context of force majeure, is also the difference in the way the tribunal has dealt with a plea of force majeure, if invoked by a company or a state. In the first case, the examination of all relevant case studies demonstrates that the tribunal was in favor of the force majeure claim, while in the case of a state alleging vis major the tribunal relates its decision according to the result of the uprising. If it has failed then the allegation of vis major is more likely to be upheld and vice-versa. For example, the Iran-United States Claims tribunal treated differently the Iranian plea of vis major, relating it with the timing of the violent upheavals. For example in the Phillips<sup>195</sup> and the Mobil Oil cases<sup>196</sup>, with direct references to the era prior to the new Islamic administration, the tribunal held that both the companies and the government of Iran were to be released from their contractual obligations due to vis major. On the contrary, in the IBEX case, the tribunal opined versus Iran's force majeure claim because *"there was no causal link between the revolutionary commotions and a given non-performance"*<sup>197</sup>.

### 3.3.4 Strikes as an event of force majeure

Strikes are recognized as unforeseeable and unavoidable events in many jurisdictions. As these two elements are more or less inherent in notion, the question of inevitability remains. Civil law countries and common law countries take a different approach: while civil law accepts strike as a classic version of force majeure and in the event of it, the employer is not held liable, common law countries regard strikes in a more "restrictive" way.<sup>198, 199</sup>

In the event of the Iranian strikes and more specifically in the Phillips Petroleum case, just as in the event of revolutions, the arbitral tribunal upheld force majeure conditions regarding "strikes and work stoppages in the oil industry" until the substitution of monarchy by the new Islamic government. After the new regime got into place, the tribunal rejected the Iranian claim<sup>200</sup> on force majeure, on the grounds that the strike of the Iranian personnel was attributed to Iran's practices to call the population for strikes.

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<sup>195</sup> Phillips Petroleum Co Iran vs Iran et al, Award nr. 425-39-2 (29 June 1989) id.

<sup>196</sup> Mobil Oil v Iran, Award nr. 16 Iran-US CTR, 38-39 in Van den Berg, A., (1998). *International Arbitration of Petroleum disputes: The development of a Lex Petrolea*, supra note 168, 16.

<sup>197</sup> The IBEX case, Firoozmand, M.R., Zamani J., (2017). *Force majeure in International contracts: current trends and how international arbitration practice is responding*, supra note 182, 401.

<sup>198</sup> Ibid., 402.

<sup>199</sup> Caltex Oil Pty Ltd vs. Howard Smith Industries Pty Ltd, id.

<sup>200</sup> Van den Berg, A., (1998). *International Arbitration of Petroleum disputes: The development of a Lex Petrolea*, supra note 168, 16.

Consequently, the plea of force majeure before international tribunals depends upon the merits of a case. It is therefore probable that a tribunal will reject it, if the particular conditions of the strike can be attributed to the party claiming force majeure, namely a state party to a contract.

### 3.3.5. Supervening illegality as an event of Force Majeure

The right of a contracting party to refrain from performing if a change in the laws impose a prohibition concerning the performance of a contract is accepted in many legal systems. Laws or governmental decrees and regulations that “ban” the performance of a contract, can cause supervening illegality. The case of *National Oil Corporation (Libya) vs. Libyan Sun Oil Company (US)*<sup>201</sup>, concerning a PSA for an oil exploration project in 1980, is characteristic. The political tensions that arose soon afterwards the beginning of the decade, resulted in a prohibition for US citizens to travel to Libya. Due to the restriction, Sun Oil did not let its US personnel to fly to Libya, and claimed force majeure<sup>202</sup>. The case was brought before ICC arbitration with Sun Oil as the defendant. Initially, the ICC Tribunal upheld that the travel prohibition on US passport travelers was an unforeseen and insurmountable event. However, force majeure did not pass the attributability test. The tribunal questioned whether “*Sun Oil could have found non-US technicians on the oil market*” to continue its operations in Libya. The Tribunal, concluded that Sun Oil failed to show evidence that it was not possible for it “*to hire non-US personnel either from within the Sun group of companies or from outside sources . . .*”, “*to add a sufficient number of non-US scientists to its scientific personnel and to send them to Libya from time to time to supervise the local work*”. The testimony of two other US companies, which had been able to perform in Libya during the same period, despite the travel restrictions, contributed to the rejection of the force majeure plea<sup>203</sup>.

### 3.3.6 Sars-Cov-2 as an event of Force Majeure

Although the SARS-Cov-2 pandemic is not considered a force majeure event by itself, “*the legal effects, of the public health crisis,*” such as lockdowns, travel restrictions, curfews and other

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<sup>201</sup> National Oil Corporation (Libya) v. Libyan Sun Oil Company (US), (1980), in Firoozmand, M.R., Zamani J., (2017). *Force majeure in International contracts: current trends and how international arbitration practice is responding*, supra note 182, 406

<sup>202</sup> Id.

<sup>203</sup> Van den Berg, A., (1998). *International Arbitration of Petroleum disputes: The development of a Lex Petrolea*, supra note 168, 24

governmental preventive measures are perceived as a force majeure situation<sup>204</sup>. Consequently, even though countries, such as China, have very early issued force majeure certificates due to the pandemic<sup>205</sup>, these may create an effect only for a domestic court of the issuing country<sup>206</sup>.

The prerequisites in order to qualify Sars-CoV-2 pandemic as a force majeure situation are these of externality, unavailability, unforeseeability and the causal link between the event and the party's performance.<sup>207</sup> In spite of various scientific predictions, which had warned about the risk of augmentation of pandemics compared to the previous decades, the pandemic is perceived as an external and unforeseeable event<sup>208</sup>. As per the unavailability requirement, the aggrieved party has to demonstrate that it could not have overcome or avoid the effects of the pandemic. However, the universal and severe consequences of the pandemic actually render the party's invocation of force majeure, easier<sup>209</sup>.

In international practice, invocation of an event as force majeure, relies on the parties' choice of law, or their choice of a force majeure clause with a relevant content<sup>210</sup>. This applies to the Sars-Cov-2 pandemic as well. In order for parties to successfully invoke force majeure in the case of the pandemic, they must have enlisted an epidemic or a pandemic type event in their force majeure clause, before the outbreak of the event. In case there is no explicit mention of epidemics in the clause, then the aggrieved party has the alternative to invoke the epidemic's indirect effects, such as restrictions, quarantines, lockdowns, if these restrictions were the ones listed in the force majeure clause<sup>211</sup>. In case parties have structured an open-ended clause, the acceptance of force majeure depends on the interpretation attributed to the clause<sup>212</sup>.

### **3.4. Obligations of the party claiming force majeure**

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<sup>204</sup> Berger, K., Behn D., (2020). *Force Majeure and Hardship in the age of Corona: A historical and comparative study*, supra note 77, 91.

<sup>205</sup> China's Council for the Promotion of International Trade has issued 6.454 force majeure certificates to companies until 25.03.2020, Id.

<sup>206</sup> Ibid., 92.

<sup>207</sup> Ibid., 109-110.

<sup>208</sup> In Europe, before February 2020, Ibid., 110-111.

<sup>209</sup> Ibid., 111-112

<sup>210</sup> Nita, C., (2020). *Coronavirus and Force Majeure Impact on International Trade Contracts*. Conferinta Internationala de Drept, Studii Europene si Relatii Internationale, 2020, 574

<sup>211</sup> Id.

<sup>212</sup> Phrases such as "events beyond the reasonable control of the parties" Ibid., 575.

In the event of a force majeure situation, parties are obliged to act in good faith and notify each other about the occurrence of events affecting the performance of the contract. In order to be released by its obligations the party claiming it, bears the burden of proof. This means that the party has to deliver positive evidence about the existence of the event or negative evidence that it has not made any error or that it not burdened by negligence that can be attributed to it<sup>213</sup>.

In the 1703 ICC Award, one of the contracting parties, responsible for a plant construction, had to stop its works, due to the outbreak of hostilities. After the termination of hostilities, the party continued to refuse finishing the project on the grounds of impossibility to ensure the return of its employees. More specifically, the party alleged lack of possibility to obtain the necessary visas, as well as the termination of its financial back up by the government. The arbitral tribunal accepted the force majeure claim for as long as the hostilities remained and a period of twenty days after their termination. However, it decided that force majeure did not exist for the period thereafter: the visas could have been obtained if the claimant had taken the necessary actions with the consulate of the country, and alternative financial resources could have been found.<sup>214</sup> Arbitration outlined that *“if the defendant had given the claimant further notice... the claimant, considering the national importance of the project, could have made it possible for the defendant to have the contract performed”*. Furthermore, it argued that the defendant had not made the necessary efforts to continue his works. Therefore, if a party claims force majeure, *“failure to give notice makes the failing party liable in damages for loss which otherwise could have been avoided”*<sup>215</sup>.

However, if an agreement includes a specific mode of notification, then, the failure to comply with this provision may substitute the party responsible for breach of contract, even if the other party knew, or should have be informed of the event<sup>216</sup>. Another scholar argues that the lack of notification will lead the party to a failure to *“fulfill its burden of proof”*.<sup>217</sup>

### 3.5. Legal consequences

Force majeure situations influence the performance of an agreement, leading to different consequences. These consequences are usually defined in detail by the force majeure clause.

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<sup>213</sup> Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, supra note 84, 11-12.

<sup>214</sup> ICC Award nr. 1703 (1971), *ibid.*, 11.

<sup>215</sup> Firoozmand, M.R. (2016), *Force Majeure Clause in Long Term Petroleum Contracts: Key Issues in Drafting*, supra note 173, 432.

<sup>216</sup> *Id.*

<sup>217</sup> Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, supra note 84, 11.

In contracts where timeframe plays a key role, non-performance within the agreed time due to an event of force majeure may lead to termination of the contract, meaning that parties are no more required to perform under their contractual obligations. On the other hand, if the time element is of secondary importance, then the force majeure event usually leads to suspension of the contract. In this latter case, the party affected must deliver as soon as the impediment affecting performance is over<sup>218</sup>.

In case of total impossibility of performance, the contract can be either terminated or renegotiated by the parties. This provision is dealt with explicitly in the Unidroit Principles: «*the parties may wish to provide in their contract for the continuation, whenever feasible, of the business relationship even in the case of force majeure, and envisage termination only as a last resort*»<sup>219</sup>. Renegotiation is envisaged due to the fact that in long-term agreements parties should be *encouraged to continue their contractual relationship rather than dissolving it*<sup>220</sup>. Renegotiation provides for a readjustment of the contract in order for it to remain viable<sup>221</sup>.

Except for termination or renegotiation, there are cases of partial impossibility of performance. In long-term agreements, there are frequently “chained” obligations bound to one another. For example, in order to construct an oil refinery, one has to build refining facilities, pipelines, storage tanks etc. What is the answer if a force majeure event affects negatively the performance of other stages of the contract? In this example, despite the separation of obligations to build refining facilities and pipelines, the projects are not totally independent from one another. A number of court decisions dealing with the issue, have accepted the contract’s viability, only if the performance of the remaining parts of the agreement can be economically justified for the other party<sup>222</sup>.

If there is no force majeure clause contained in the agreement, then, a successful plea of force majeure exempts the invoking party from liability. This means that the party is no longer liable to pay damages, as it is a general principle of law that damages are due only in cases of negligence and force majeure suggests the absence of negligence<sup>223</sup>. If, on the contrary, there is a force majeure clause in the contract, parties have the alternative to change the extent of legal consequences of

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<sup>218</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, Business Law International, 8 (2), 166.

<sup>219</sup> Article 7.1.7 Unidroit Principles (2016), 242.

<sup>220</sup> Id.

<sup>221</sup> Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, supra note 84, 15.

<sup>222</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, supra note 218, 167.

<sup>223</sup> Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, supra note 84, 15

their clause in a broader or a narrower way<sup>224</sup>. The exemption of damages concerns not only liquidated damages, but penalties as well<sup>225</sup>. However, if payment of money is due, then the party is not relieved, except if the force majeure event renders all money transfers impossible<sup>226</sup>.

In any case, the impact of the claim of force majeure on the contract depends on the nature and consequences of the impediment itself<sup>227</sup>.

### 3.6. Special considerations when drafting a force majeure clause

In international business agreements, parties are free to select any contractual term suitable for their particular transaction. According to a uniformly accepted principle of law, a contract is governed by the applicable law of the contract, which also includes the change of circumstances due to supervening events. Moreover, in case where there is no express clause dealing with force majeure then the change of circumstances will be decided upon by the governing law.<sup>228</sup> Furthermore, the parties are free to choose another law or no law in order to stipulate their force majeure clause, even if their agreement is governed by a different choice<sup>229</sup>.

A well-structured force majeure clause is of great importance, because it can actually save the contracting parties from serious and costly consequences if a risk eventuates. The definition of and the careful drafting of the clause may save both parties from unnecessary recourse to arbitration and courts. Thus, what is generally important is the requirements of the relevant market and the good understanding of the law, governing the contract<sup>230</sup>.

Usually, the force majeure clause contains specific elements. The first and most important element is the definition of the force majeure event. In spite of the fact that the listing of every possible event would be very practical, in real terms, it is hard to compile a list of all events beforehand, either because it is hard to foresee all events, or because reaching an agreement upon

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<sup>224</sup> Pichonnaz, P., (2015). *Ch. 7 Non-performance, S.1: non-performance in general, Art. 7.1.7. Commentary on the Unidroit Principles of International Commercial contracts*, supra note 170, 11-12.

<sup>225</sup> Schwenger I., (2008). *Force Majeure and Hardship in International Sales Contracts*, supra note 175, 719.

<sup>226</sup> Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, supra note 84, 14.

<sup>227</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, supra note 218, 166.

<sup>228</sup> Firoozmand, M.R. (2016), *Force Majeure Clause in Long Term Petroleum Contracts: Key Issues in Drafting*, supra note 173, 424.

<sup>229</sup> Draetta U., (1996), *Force majeure clauses in international trade practice*, *International Business Law Journal*, 1996 (5), 550.

<sup>230</sup> Firoozmand, M.R. (2016), *Force Majeure Clause in Long Term Petroleum Contracts: Key Issues in Drafting*, supra note 173, 425.

each and every one is difficult and timely<sup>231</sup>. Consequently, often, the design of the clause provides a definition of force majeure circumstances accompanied by a phrase such as “*including but not limited to*”, in order to underline the non-exhaustive character of the list<sup>232</sup>. This particular phrase is a wrap – up clause, interpreted ejusdem generis<sup>233</sup>.

A review of the clauses included in oil and gas contracts demonstrates two ways to stipulate a force majeure event or circumstance. To define force majeure, the parties usually refer to a specific national legal system or international law. An example of the latter is the Douala Basin Model Contract of Association according to which “*The intention of the Parties is that the term force majeure receives the interpretation which complies the most with the principles and customs of international law*”. This solution provides the parties with the advantage to harmonize their force majeure clause with the law that governs their contract, but on the other hand, there might be issues left unsolved by the governing law<sup>234</sup>.

However, in the great majority of the oil and gas contracts parties choose to describe the circumstances in a more detailed way. A characteristic example is the 1996 Exploration Agreement between Oman and Triton which reads: “*Force Majeure*” within the meaning of this Agreement shall be any act of God, insurrection, riot, war, strike and other labour disturbances, fires, floods, change of government, violent storms, tidal waves, cyclones, thunderstorms, navigation dangers, earthquakes, explosions, fires, destruction of machinery or installations, hostilities, blockades, embargoes, insurrections, acts of terrorism, civil or criminal disturbances, national emergencies, the inability to obtain, import or use any of the required materials, equipment or services, the inability to obtain the necessary rights of passage, or any other cause not-due to the fault or negligence of the Party claiming Force Majeure, whether or not similar to the foregoing, provided that any such cause is beyond the reasonable control of such Party<sup>235</sup>”.

From the review of the clause, we contemplate that this clause gives a definition of force majeure with a non-exhaustive list of specific events. The clause contains the phrase *whether or not similar to the foregoing*, which consists of a wrap – up clause.

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<sup>231</sup> Al-Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*, supra note 4, 13.

<sup>232</sup> Draetta U., (1996), *Force majeure clauses in international trade practice*, supra note 229, 551.

<sup>233</sup> There are different opinions on the interpretation of a wrap-up clause. According to the English common law the force majeure clause containing a wrap-up clause should not be interpreted as “ejusdem generis”. To avoid such issues drafters tend to design a very detailed clause containing every possible type of risk’, in Firoozmand, M.R. (2016), *Force Majeure Clause in Long Term Petroleum Contracts: Key Issues in Drafting*, supra note 173, 431.

<sup>234</sup> Model Contract of Association of Douala Basin (1995), *ibid.*, 426.

<sup>235</sup> Exploration Agreement between Oman and Triton of 1996, *ibid.*, 427.

The second important element of a force majeure clause has to do with the invoking party's obligations, should a force majeure event occurs. Even if a contract is silent, parties are due to perform in good faith and are obliged to work together in order to mitigate the consequences of an unexpected event. In this aspect, the party with a force majeure plea is obliged to notify the other performing party of any problems in regard with the performance of the contract, in order to avoid unpleasant surprises. Moreover, unless a contract contains a different provision, failure to notify the contractual partner concludes leads the other party to a denial of the force majeure claim<sup>236</sup>. So, clauses should be drafted in a manner as to oblige the party to undergo specific actions within a given timeframe and stipulate the consequences in case of failure<sup>237</sup>.

In this context, an illustrative example of a detailed notice provision is the Preliminary Caspian Offshore Consortium Agreement. It reads: *“Upon the event of Force Majeure, the Party affected by such Force Majeure shall notify the other affected Party immediately after it became aware of such circumstances, providing a sufficiently detailed description of such Force Majeure, the alleged impact such Force Majeure has on affected Party's compliance with this Agreement, the expected duration of such impact and the actions that the affected Party proposes to undertake to remedy the state resulting from Force Majeure and mitigate the impact of Force Majeure in compliance with Article 35.3. The aforementioned notice shall be periodically renewed to the extent required to warrant that such notice accurately conveys the circumstances pertaining to Force Majeure, in any case, however, the notice shall be renewed not less than once a month ... if such notice is not served by this Party within 30 (thirty) calendar days from the date this Party became aware of the event of Force Majeure, and the service of such notice was not precluded or delayed by reasons of Force Majeure this Party shall be liable for any damages suffered by any other Party due to this notice not being served “*

A typical force majeure clause also deals with the consequences should a force majeure risk materializes. More specifically it may stipulate whether the force majeure event will give the parties the right to suspend, terminate or renegotiate the contract. This third element, which deals with the consequences of the force majeure event, is considered to be of high importance<sup>238</sup>. Often, parties deal with supervening events by providing their contracts with a clause that introduces suspension of the contract. The 1994 South African Model Joint Operating Agreement reads: *“The*

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<sup>236</sup> Nassar, N. (1995). *Sanctity of Contracts Revisited*. Dordrecht, Boston, London (1995), page 202, available at : <http://www.trans-lex.org/105700> [accessed in 16.02.2021].

<sup>237</sup> Al-Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*. supra note 4, 13.

<sup>238</sup> Id.



*obligations of each of the Parties hereunder ... shall be suspended during the period and to the extent that such Party is prevented or hindered from complying therewith by vis major*<sup>239</sup>. The parties also deal with supervening events with an extension of the timeframe of their projected tasks. Illustrative in this aspect is the clause below: *“the term of this Agreement and all rights and obligations hereunder shall be extended for a period equal to the delay caused by the Force Majeure occurrence plus such period of time as is necessary to re-establish operations upon removal or termination of Force Majeure*<sup>240</sup>.

Renegotiation is also another option. Renegotiation means modification of the contract as a whole, or alteration of the parts of the contract affected by force majeure. The Vietnam Production Sharing Contract of 1993 stipulates: *“If the cause of Force Majeure is not removed within twelve (12) months the Parties shall enter into negotiations in good faith to discuss the continuance of this Contract.*<sup>241</sup>” In case of failure of renegotiation, arbitration or another means of dispute resolution may be agreed upon by the parties. Although in a long-term agreement, such as a gas or oil agreement, it is to the advantage of the parties to elongate their contractual relationship, sometimes this is not the case, since a contract cannot be forever suspended.

The fourth element of a force majeure clause is the provision of specific actions in order to overcome the consequences of a force majeure event. This is either achieved by the provision of every possible measure to eliminate the force majeure situation or by the minimization of its effect on the performance of the party affected.<sup>242</sup> One illustrative example is the clause from the gas Joint Venture Agreement between Qatar Petroleum, Exxon Mobile, and LNG Japan<sup>243</sup>, which indicates: *“Upon the giving of notice, the parties shall meet to discuss what action, if any, is practicable to take, to mitigate or overcome the effects of the event or circumstance of Force Majeure. If the event or circumstance arises in the State of Qatar, the parties shall, if appropriate, seek the assistance of the Government, in removing or mitigating such event or circumstance”*.

Since the effects of a force majeure must be inevitable, it is argued that a force majeure clause should contain a measurement of the inability to perform. In this aspect, a due diligence

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<sup>239</sup> South African Model Joint Operating Agreement of 1994, in Firoozmand, M.R. (2016), *Force Majeure Clause in Long Term Petroleum Contracts: Key Issues in Drafting*, supra note 173, 435.

<sup>240</sup> Article 20(1) of the Amoco Group Agreement on Exploration, Development & Production Sharing for Prospective Structures Ashrafi, Dan Ulduzu & Area Adjacent in the Azerbaijan Sector of the Caspian Sea, (1996), *ibid.*, 430.

<sup>241</sup> Article 20(5) of the 1993 Production Sharing Contract between Vietnam Oil & Gas Corporation and Russian Foreign Economic Association, 'Zarubezhneft,' BHP Petroleum (Dai Hung) Pty Ltd and Petronas Carigali Overseas Sdn Bhd, Total Vietnam and Dai Hung Oil Development (Japan) Ltd

<sup>242</sup> Draetta U., (1996), *Force majeure clauses in international trade practice*, supra note 229, 551.

<sup>243</sup> Ras Laffan Liquefied Natural Gas Company Limited Joint Venture Agreement, (2002), in Al-Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*, supra note 4, 13.

obligation which burdens the party alleging force majeure should be introduced in the clause, in order to determine whether the effects of an event could be avoided or not.<sup>244</sup>

### 3.7. The International Commercial Chamber (ICC) force majeure clauses

The ICC Force Majeure clause of 2020 -long and short version-<sup>245</sup>, is an indicative example of a model clause for parties wishing to incorporate pre-drafted clauses in their contracts. The long version of the clause may be used either as reference, or as a pre-drafted clause to insert in a contract. The short version may be incorporated as such.

In its definition, the new ICC Force Majeure clause provides for a similar definition as in the Principles, repeating the same preconditions. The new long version clause however, differs from the Principles in that it incorporates a criterion of listed events<sup>246</sup>. According to the ICC clauses explanatory note, *“the Presumed Force Majeure Events commonly qualify as Force Majeure. It is therefore presumed that in the presence of one or more of these events the conditions of Force Majeure are fulfilled, and the Affected Party need not prove the conditions (a) and (b) of paragraph 1 of this Clause (i.e. that the event was out of its control and unforeseeable), leaving to the other party the burden of proving the contrary. The party invoking Force Majeure must in any case prove the existence of condition (c), i.e. that the effects of the impediment could not reasonably have been avoided or overcome”*. That means that the burden of proof is shifted to the obligor only in the latter case. The working group defines this solution as *“a reasonable compromise between the need for a general definition of force majeure and the current practice of including a list of typical events”*.

In general, the ICC clause gives a more detailed definition of the legal consequences if force majeure occurs. It actually refers to relief from obligations, exemption from liability and *“from any other contractual remedy for breach of contract”*. Furthermore, the ICC clause and the Principles differ in the context that under the ICC clause, the parties reserve the right to terminate the contract while the Principles give the alternative of a continuation of the business transaction.

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<sup>244</sup> Konarski, H. (2003). *Force majeure and hardship clauses in international contractual practice*, supra note 84, 8.

<sup>245</sup> ICC 2020 Force majeure clause in <https://iccwbo.org/content/uploads/sites/3/2020/07/icc-forcemajeure-introductory-note.pdf>

<sup>246</sup> Kessedjian, C., (2005). *Competing approaches to Force Majeure and Hardship*, supra note 166, 425.

## 4. A COMPARATIVE APPROACH OF DOMESTIC LEGAL SYSTEMS ON CHANGED CIRCUMSTANCES

### 4.1. The Civil law and Common law approach

Long-term contracts, such as these in the oil and gas trade, involve private entities, States or their nationals. Parties to these contracts are free to choose the law governing their contract by inserting a specific choice-of-law clause. Otherwise, the arbitrator may apply the conflict-of-law rule of the seat of arbitration or the law of the state party of the contract, participating in the arbitration process. Moreover, the arbitral tribunal is free to apply other legal systems.

In general, the application of a national legal system is considered by a part of scholars as the commonest choice for contracting parties<sup>247</sup>. According to other scholars however, although parties are autonomous in their choice of law, if this choice results in the adoption of the legal system of the counterparty, then this becomes the least popular choice<sup>248</sup>. Except for the application of a particular domestic legal system, parties are free to incorporate hardship or force majeure clauses in their contracts to deal with the issue of changed circumstances. By including such clauses the parties are more flexible to delimitate the application, the scope and the legal effects of the changed circumstances. Respectively, courts will apply the rule that the parties have introduced and will not follow the domestic law provisions<sup>249</sup>.

In any case, civil or common law systems, have a different view vis-a-vis changed circumstances.

Civil law countries introduce provisions of adaptation or termination of the contract to deal with the issue, while in common law countries there is no provision of adaptation of the contract nor “relief” of the party claiming the change<sup>250</sup>. Moreover, in common law jurisdictions it is argued that the terms of contracts should be respected and that parties should insert appropriate clauses

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<sup>247</sup>Bockstiegel, K.H., (2002), *The Application of the Unidroit Principles to contracts involving states or intergovernmental Organizations*, available at: [https://library.iccwbo.org/content/dr/ARTICLES/ART\\_0044](https://library.iccwbo.org/content/dr/ARTICLES/ART_0044)

<sup>248</sup>Bonell M.J., (2018). *The Law governing international commercial contracts and the actual role of the Unidroit Principles*, supra note 86, 17.

<sup>249</sup> Katsivela, M. (2007). *Contracts: Force Majeure concept or Force Majeure Clauses?*, supra note 9, 101-110; Al-Emadi T.A., (2011). *The Hardship and Force majeure clauses in International Petroleum Joint Venture Agreements*, supra note 4, 1-2

<sup>250</sup> Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 138.

in order to ensure adequate protection in their contractual arrangements<sup>251</sup>. Therefore, in common law countries, non-performance raises liability of the party in default<sup>252</sup>. The origin of the differences between the two legal systems goes back to the fact that civil law countries have greatly suffered from the destructive economic impact of world wars<sup>253</sup>.

The most indicative legal structures of common law legal systems to deal with changed circumstances are those of frustration and commercial impracticability. On the other hand, in civil law countries we encounter doctrines such as the French one of *imprevision*, or the German "*Wegfall der Geschäftsgrundlage*". There are also other different legal structures, according to each country's particular legal tradition and culture<sup>254</sup>.

#### 4.1.1 The frustration doctrine

Frustration is considered more or less the corresponding doctrine of *force majeure* for common law countries, although other scholars suggest that it corresponds to the hardship provision<sup>255</sup>. Under frustration, the obligor's performance is still possible but is no longer of use to the recipient, at least for the purpose initially agreed by the parties.<sup>256</sup>

Application of the principle throughout the existing case law demonstrates the *pacta sunt servanda* principle's paramount importance<sup>257</sup>. In the well-known case *Paradine v. Jane*, the court

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<sup>251</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 2.

<sup>252</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, supra note 218, 173.

<sup>253</sup> Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 138.

<sup>254</sup> Id., French and Belgian law deal with changed circumstances only if the performance is impossible in absolute terms, (*force majeure* doctrine), while there is no provision for hardship for commercial contracts, also in Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 5.

<sup>255</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, supra note 218, 173; Pirozzi, R. (2012). *Developments in the Change of Economic Circumstances Debate?*, supra note 101, 107.

<sup>256</sup> Pirozzi, R. (2012). *Developments in the Change of Economic Circumstances Debate?*, supra note 101, 107

<sup>257</sup> Indicative is the famous Coronation case of *Krell v Henry* (1903), as well as the cases *Paradine v Jane* (1647), and *Taylor v Caldwell*, in Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 139; Baranauskas E., Zapolskis P. (2009). *The effect of change in circumstances on the performance of contract*, supra note 74, 201-204.

decided that when the party has undertaken an obligation, the contract must in any case be respected, otherwise the party should have made explicit provision of the contrary in its contract<sup>258</sup>.

As time evolved, the doctrine became less strict, incorporating an important element, *the radical change* of circumstances. This means that the changed circumstances have completely transformed the contract into something new. In any case, the radical change in the frustration doctrine is not equivalent to the excessively onerous performance in case of hardship. This is particularly evident through a line of cases where the claim of frustration was rejected, because performance was not *radically different* in relation with the initial agreement, although someone might consider the performance excessively onerous.

A review of the existing case law demonstrates that the English legal system is usually oriented towards a “fixed” perspective of the contract, in the sense that the performing party must bear the consequences of the changed circumstances or that in case of changed circumstances the parties are sometimes entitled to “*a premature termination of the contract*”<sup>259</sup>.

Under frustration, the contract is terminated automatically. This fact usually affects the obligations due, after the frustration claim and does not affect those already fulfilled. This is the reason for the enactment of the 1943 Law Reform Act, which deals with these issues<sup>260</sup>. In any event, the fact that English courts consider that the only solution according to the English Law is termination of the contract does not seem satisfactory by many scholars. It is even criticized as being “in direct contrast with any modern system of trade law”.<sup>261</sup>

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<sup>258</sup> Ibid, 201.

<sup>259</sup> In Viscount Simon in *British Movietonews Ltd v London and District Cinemas Ltd* (1952), and in the Suez Canal cases, in Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 140. The contract was frustrated because the new circumstances had rendered performance entirely different.

<sup>260</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, supra note 218, 177.

<sup>261</sup> Schmitthoff C.M., (1980). *Hardship and intervener clauses*, *Journal of Business Law*, 92-91, 91, in Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 142.

#### 4.1.2. Commercial impracticability

The American concept of commercial impracticability is based on the provision of Section 2-615 of the Uniform Commercial Code, which regulates the Sales of goods<sup>262</sup>. According to the commentary of the provision, “*the seller to a contract is excused from the timely delivery of the goods where his performance has become commercially impracticable because of unforeseen supervening circumstances not within the contemplation of the parties at the time of contracting*”<sup>263</sup> and applies only to the seller of Article 2 of UCC.

As the existing literature demonstrates, the doctrine differs from frustration in the sense that frustration deals with an increase of the cost of performance while commercial impracticability usually deals with the decrease of value of performance<sup>264</sup>. Also in comparison with the frustration doctrine, the American structure of commercial impracticability reserves a broader regard towards changed circumstances. While in the English legal system the “legal impossibility of performance”, “the death of a person” or “the destruction of the subject matter of a contract” constitute good reasons to exempt the disadvantaged party from performance, the US doctrine goes even further, and is more liberal in its view of changed circumstances<sup>265</sup>. In fact, in their interpretation of the doctrine, American courts have incorporated cases of economic hardship. Indicative in this aspect is the *Transatlantic Financing Corp v United States* case, which contributed to the definition of the doctrine by clarifying that “*a thing is impossible when it is not practicable and a thing is impracticable when it can only be done at an excessive and unreasonable cost*”<sup>266</sup>. Consequently, US courts are generally regarded as more flexible in their effort to resolve cases of economic contingency<sup>267</sup>. However, according to some experts<sup>268</sup>, even in their intention to answer the difficult cases of economic hardship, American courts still “tend to interpret the concept of impracticability in a very narrow sense.”

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<sup>262</sup> Jenkins, S.H., (1998), *Exemption for nonperformance: UCC, CISG, Unidroit principles – A comparative Assessment*, supra note 76, 2022.

<sup>263</sup> Fucci, F.R., (2007), *Hardship and Changed circumstances as excuse for non-performance of contracts – Practical considerations in International infrastructure Investment and finance*, supra note 72, 6

<sup>264</sup> Pirozzi, R. (2012). *Developments in the Change of Economic Circumstances Debate?*, supra note 101, 107.

<sup>265</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, supra note 218, 177,178; Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 142-145.

<sup>266</sup> *Transatlantic Financing Corp v United States*, *ibid.*, 178.

<sup>267</sup> *Id*; *ibid.*, 144.

<sup>268</sup> *Id*.

In any case, in both the doctrines of frustration and impracticability, the performing party is relieved from performance, termination being the only solution<sup>269</sup>. However, in contradiction with the English concept, American judges are deemed, to some degree, more flexible towards an adaptation or renegotiation of the contract.

#### 4.1.3. Imprévision

The French Civil Code does not contain any provision in case performance becomes more burdensome for one of the parties. A party to a contract may be relieved from performance only in case of absolute impossibility to perform its contractual obligations, due to an external factor, notably in three cases; the first case is force majeure, the second an accidental event and the third “a *cause étrangère*”. French courts steadily apply the three concepts to resolve cases where performance becomes impossible due to objective reasons<sup>270</sup>, and are very strict in applying the *pacta sunt servanda* doctrine. In the light of this notion, termination of the contract is the only accepted solution.

Unlike civil courts, administrative courts have been more flexible in applying the concept of imprévision, in particular the French Administrative Supreme Court (Conseil d’Etat).<sup>271, 272</sup> The idea that links the concept to administrative cases only, derives from the notion that continuity of a contract which safeguards the common welfare must be secured at all costs<sup>273</sup>.

The rigid application of the *pacta sunt servanda* doctrine of French courts has been in favor of the insertion of specific clauses, such as indexation clauses or hardship clauses with the purpose of resolving the issues that appear because of the changed circumstances<sup>274</sup>.

#### 4.1.4. The German legal doctrine of “*Wegfall der Geschäftsgrundlage*”

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<sup>269</sup> This is a substantial difference in view of the solution offered by the PICC.

<sup>270</sup> Baranauskas E., Zapolskis P. (2009). *The effect of change in circumstances on the performance of contract*, supra note 74, 199-200.

<sup>271</sup> *Ibid.*, 200.

<sup>272</sup> A famous case is the aforementioned in this thesis case of *Gaz de Bordeaux*, dated in 1916, *id.*

<sup>273</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, supra note 218, 168-169.

<sup>274</sup> Baranauskas E., Zapolskis P. (2009). *The effect of change in circumstances on the performance of contract*, supra note 74, 201.

Under German Law<sup>275</sup> “the debtor is relieved from his obligation to perform, if the performance becomes impossible because of a circumstance, for which he is not responsible, occurring after the creation of the obligation.” According to this provision, a party is relieved from its contractual obligations in case an unexpected event has rendered its performance impossible. If the new circumstances have rendered the performance impossible, the continuance of the contract in its initial terms would constitute bad faith for the performing party. In this case, the core of the contractual agreement is considered “destroyed”<sup>276</sup>.

Firoozmand argues that the German doctrine is applicable even in private contracts, but only in case of appearance of a physical or a legal impediment. If there is economic impossibility the doctrine is not applicable<sup>277</sup> following the provision of the German Law in which the debtor “remains bound” to his debt even if he declares bankruptcy<sup>278</sup>.

Moreover, courts are empowered to alter the contract so to render the contractual agreement viable, while termination of the contract is considered a solution only in rare occasions, “where the contract has no reason for be kept alive”. However, German courts altogether apply the doctrine rarely and in a strict manner<sup>279</sup>.

#### 4.5. The Greek law on changed circumstances

The Greek Civil Code deals with changed circumstances in Article 388 CC<sup>280</sup>. According to its reading : a) Changed circumstances effect upon the performance of the contract, while this change is viewed under the subjective criteria of “good faith” and “common usages”, b) the change is based upon unforeseeable and extraordinary reasons, c) the performance of the debtor becomes “excessively onerous”.

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<sup>275</sup> 275(1) BGB

<sup>276</sup> Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 149.

<sup>277</sup> Firoozmand, M.R. (2007), *Changed Circumstances and Immutability of Contract: Comparative analysis of Force Majeure and Related doctrines*, supra note 218, 170.

<sup>278</sup> RGZ 133, 177 (1931) id.

<sup>279</sup> Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 149.

<sup>280</sup> 388 CC reads, “If, in view of the requirements of good faith and common usages, the circumstances upon which the parties mainly founded the conclusion of a reciprocal contract have subsequently changed for extraordinary reasons which could not have been foreseen, and the performance of the debtor, taking also into consideration the counter-performance, has as a result of the change become excessively onerous, the court may, at the request of the debtor and according to its appreciation, adjust the debtor’s performance to the appropriate extent or decide upon the dissolution of the contract, wholly or to the extent of its non-performed part. If the dissolution has been decided upon, the obligations to perform arising therefrom shall be extinguished and the contracting parties shall be reciprocally obliged to return the performances they received according to the provisions on unjust enrichment.”



In the case of article 388 CC, “onerous performance” does not mean “completely ruinous performance” or merely difficulties in performing. It has the meaning that performance is exceedingly onerous in a way that the burden, which the performing party is suffering, is unreasonable<sup>281</sup>. The basic provisions of the article remit to the hardship doctrine of the PICC. Both set as prerequisite extraordinary and unforeseen conditions, which alter significantly the equilibrium of the contract and set forth third party intervention, based on a party’s request. What is different between the two doctrines is that the Greek Law includes the general principles of “good faith” as well as the “common usages” in the actual wording of the provision, while the relevant article of the PICC does not<sup>282</sup>. As per the national judge’s alternatives, the solutions offered also resemble to the hardship doctrine of the Unidroit principles, as Greek courts may either adjust the contract and if there is no ground for adjustment, decide upon its termination partially or totally. In the Greek literature dissolution of the contract is a last resort alternative of the court<sup>283</sup>.

An overview of the Greek case law demonstrates a gradual shift from the rigid application of the *pacta sunt servanda* rule by the Greek courts, towards an effort of “intervention” in the contractual scheme. It is noteworthy, that after the adoption of the principle by the Greek Civil Code, the Greek Supreme Civil Court in its initial decisions dismissed the *rebus sic stantibus clausula*, even when it judged cases of extreme devaluation of the currency affecting seriously the performance of a contract (!). Overtime however, the Greek Supreme Court adopted a more equitable glance towards the issue<sup>284</sup>.

The Greek Civil Code adopts a legal provision with respect to force majeure, under article 336 of the Greek Civil code<sup>285</sup>. Similarly to the Unidroit principles, the Greek code links the excuse of performance to the absence of responsibility on the debtor’s part.” The Greek case law suggests that the three cumulative conditions that characterize an event as force majeure, namely unforeseeability, externality and irresistibility<sup>286</sup> are equally present in the Greek legal system and recognized by the respective case law.

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<sup>281</sup> Karampatzos, A. (2005). Supervening hardship as subdivision of the general frustration rule: A comparative analysis with reference to the Anglo American, German, French and Greek Law, *European Review of Private Law*, 13 (2), 142.

<sup>282</sup> Article 1.7 of the Unidroit Principles (2016).

<sup>283</sup> Karampatzos, A. (2005). Supervening hardship as subdivision of the general frustration rule: A comparative analysis with reference to the Anglo American, German, French and Greek Law, *supra* note 281, 142.

<sup>284</sup> AP 1733/1986, Nomiko Vima, *ibid.*, 143.

<sup>285</sup> According to the article “The debtor is excused of performance of any obligation caused by his inability to perform if he proves that his inability is due to an event for which he was not responsible. The debtor has the obligation to notify the creditor immediately after he becomes aware of his inability to perform”

<sup>286</sup> AP 67/2003 Nomos in Katsivela, M. (2007). *Contracts: Force Majeure concept or Force Majeure Clauses*, *supra* note 9, 103.

The externality factor refers to events which are situated outside the “debtor’s sphere” as well as events generally attributed by scholars to force majeure, such as acts of God, acts of war, employees’ strikes<sup>287</sup>. The unforeseeability prerequisite suggests that the event must have been unforeseeable at the time of the conclusion of the contract<sup>288</sup>. The irresistibility condition, which leads to impossibility of performance, is also contemplated in Greek courts’ decisions. According to the case law, especially irresistibility includes “incidents which cannot be avoided by acts of utter diligence and prudence of the debtor” thus inserting a more detailed and elevated standard of precaution. Moreover, an irresistible event must not be attributed to the party claiming force majeure. In this case, the party is not exempted from performance<sup>289</sup>.

Unlike the Unidroit Principles, in the event of force majeure, the law does not entitle Greek courts to decide upon the adaptation of the contract according to the changed circumstances, but only allows them to decide with regard to excuse or no excuse of the performing party. In this aspect, the Greek Law offers a more restricted management of changed circumstances. In addition, the debtor is entitled to fulfill secondary obligations, such as the obligation to announce his inability, but he is not subject to indemnification <sup>290</sup>.

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<sup>287</sup> Under certain conditions. Areios Pagos 1303/2004 Nomos in Katsivela, M. (2007). *Contracts: Force Majeure concept or Force Majeure Clauses?* Supra note 9, 104.

<sup>288</sup> Even if hostilities or war or other destructive events could be foreseen at the time of conclusion of the contract, then the criterion is not actually met, *ibid.*, 105.

<sup>289</sup> Piraeus Court of Appeal, (Maritime section) 682/2004 Nomos. According to the decision, bad, foreseeable weather conditions were not assumed irresistible.

<sup>290</sup> Vathrakokilis, V.,(2003). Interpretation and case law of the Greek Civil Code, Sakkoulas Editions, Athens 2003.

## CONCLUSIONS

It is incontestable that the *pacta sunt servanda* doctrine has served its purpose through the centuries, safeguarding that contracting parties stay true to their commitments and agreements are honored in good faith. The doctrine has also enhanced contractual security, trust and lack of useless litigation between parties. Nevertheless, although security and trust remain a key issue for present and future agreements, the current rapid political, technological, economic and commercial changes worldwide, tend to render the doctrine less rigid than before<sup>291</sup>.

The current era characterized by the velocity with which changes of circumstances appear, may easily put a contractual party's welfare at stake. In this context, the *rebus sic stantibus* principle gains ground and makes the necessity for legislators and judges, to find the optimal balance between the two doctrines, more concrete than ever. Of course, there are no uniform solutions to apply in all cases, especially as courts and arbitrators decide upon the merits of each specific case individually, taking into consideration "the nature of the contract, its subject matter and the conditions of the market in which the contract was concluded"<sup>292</sup>. However, a greater sensitivity towards contractual unfairness and disequilibrium will probably be displayed in court decisions and arbitral awards in the future<sup>293</sup>.

Although there are different scholar approaches as to whether renegotiation, hardship or force majeure clauses should be applied in contracts, the fact remains, that the longevity of oil and gas contracts renders the parties particularly vulnerable to changes of circumstances, which may seriously affect the "life" of the agreement. Furthermore, these types of contracts are prone to various investment risks, which trigger renegotiation<sup>294</sup>. In spite of the disadvantages mentioned above, the introduction of specific clauses, which will enhance the renegotiation process, providing

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<sup>291</sup> Lando, O. (1980). *Renegotiation and Revision of International Contracts*, German Yearbook of International Law, 1980 (23), 37-58; Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 135-138.

<sup>292</sup> Berger, K., Behn D., (2020). *Force Majeure and Hardship in the age of Corona: A historical and comparative study*, supra note 77, 128.

<sup>293</sup> Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 135-138; Edlund H.H., (2009), *Imbalance in Long -Term commercial contracts*, ERCL 2009 (4), 427-445

<sup>294</sup> Salih, M.S., Yamulki A., (2020). *Stabilisation and Renegotiation in Iraqi Kourdistan Oil and Gas Contracts: A comparative study*, supra note 12, 111.

for the smooth continuation of the contractual arrangement seem a more beneficial solution for both parties<sup>295</sup>.

The insertion of a renegotiation, a hardship or a force majeure clause in a contract however, does not serve as *panacea*. The role of renegotiation is to provide parties with a reasonable solution vis-à-vis a change of circumstances and this process relies considerably on the structure of the respective clause. Therefore, different aspects in drafting should be taken into consideration. Clauses of this genre should clearly define the triggering events, the procedure, the scope and the effects of renegotiation as well as third party intervention in case the process of negotiating in good faith has proved fruitless for the parties<sup>296</sup>. Sars-Cov-2 pandemic is a characteristic example of the necessity for a carefully worded clause, where the induction of an exhaustive or exemplifying version of a hardship or a force majeure clause significantly affects the admission or rejection of the doctrine<sup>297-298</sup>.

Apart from traditional renegotiation clauses found in oil and gas contracts, the issue of supervening events is the subject of rules of many domestic jurisdictions, with each legal system reserving its own different approach in accordance with its own legal origins and traditions. Therefore, the solutions offered by national legal systems do not reflect the growing needs of international commercial trade. The reason for this inefficacy is that national jurisdictions seem to govern cross-border trade transactions in a partial, inadequate manner. Although the law of the contract stems from the parties' autonomous choice, parties prove rather reluctant in accepting the legal system of their counterparty. In addition, if the legal forum governing the contract is not contractually established, the complexity among various national provisions of private international law, renders the equation even more complex<sup>299</sup>.

In this aspect, the Unidroit Principles of International commercial contracts constitute a real "novelty" as they establish a legal mechanism to deal with several international trade issues, including the problem of the changed circumstances. Drafted by experts belonging to different legal

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<sup>295</sup> Gotanda, J. Y., (2003), *Renegotiation and Adaptation Clauses in Investment Contracts, Revisited*. From the selected works of John Y Gotanda, supra note 24, 1461-1473; Berger, K., (2003). *Renegotiation and adaption of international investment contracts: The role of contract drafters and arbitrators*, supra note 23, 1347-1380.

<sup>296</sup> Salih, M.S., Yamulki A., (2020). *Stabilisation and Renegotiation in Iraqi Kourdistan Oil and Gas Contracts: A comparative study*, supra note 12, 113.

<sup>297</sup> Berger, K., Behn D., (2020). *Force Majeure and Hardship in the age of Corona: A historical and comparative study*, supra note 77, 128.

<sup>298</sup> Nita, C., (2020). *Coronavirus and Force Majeure Impact on International Trade Contracts*, supra note 210, 574-575.

<sup>299</sup> Bonell M.J., (2018). *The Law governing international commercial contracts and the actual role of the Unidroit Principles*, supra note 86, 15-41.

systems worldwide, the PICC mirror “a restatement of international contract law.” The reason of their success is that they principally have a “broad scope”. To deal with several trade issues in a more effective manner, in their 2016 edition they include special considerations for long-term contracts and insert clauses, adapted to the special needs of cross-border trade<sup>300</sup>. What is more important, they deal explicitly with the issue of supervening events in a broad, efficient manner.

Although it is argued that, the Unidroit principles jeopardize the sanctity of contracts, on the basis that they may favor uncontrollable changes that bring lack of faith and insecurity among the parties,<sup>301</sup> recent arbitral awards are starting to pay special tribute to the principles, even in cases where they are not set as the choice-of-law rules of the contract. Arbitrators already make express reference to them in their effort to demonstrate the conformity of national rules with international practice. Even more, in particular cases, they already accept adaptation of the contract even if there is no explicit provision in the contract<sup>302</sup>. This tendency indicates that they contribute significantly as “guidelines” for international commercial transactions and that they are bound to contribute as a future aspect of *lex mercatoria*.

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<sup>300</sup> *Ibid.*, 23.

<sup>301</sup> F. Bartolotti, (1977). *Diritto dei contratti Internazionali – Manuale di diritto Commerciale Internazionale*, Padua, Cedam 1997, 108-109 in Zaccaria. E.C., (2005). *The effects of changed circumstances in International Commercial Trade*, supra note 6, 173-174.

<sup>302</sup> Bockstiegel, K.H., (2002), *The Application of the Unidroit Principles to contracts involving states or intergovernmental Organizations*, supra note 247, 5-7.

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