HARDSHIP IN INTERNATIONAL CONSTRUCTION CONTRACTS

I – The Notion of Hardship

As in most long term contracts, construction contracts carry some unforeseeable risks. Circumstances might change in the execution of long term contracts so fundamentally that they may alter the contractual. The situation in which the equilibrium of the contract is so frustrated that the execution of the contract might not be expected from one of the parties is called hardship in the practice of international commercial contracts.

Hardship may be a ground for a remedy such as renegotiation of the contract in order to restore the equilibrium or rescission provided that some conditions are satisfied. Accordingly, the frustrating events shall;

a) Lead to an excessive alteration in the equilibrium of undertakings, and this should result in an excessive difficulty or impracticability in the performance of his obligation,

b) Emerge or become known after the conclusion of the contract,

c) Be unforeseeable,

d) Be beyond the control of the disadvantaged party, and

e) The risk shall not be assumed by the disadvantaged party.

II - Hardship in Construction Contracts

Construction contracts are long term contracts by their nature and they are easily affected by natural and economical conditions. For this reason, there is always the possibility that some alterations happen in the execution of these contracts. The remedies in case of an alteration vary depending to the gravity of the alteration. In case if the requested change is not so fundamental as to frustrate the equilibrium of the undertakings and if the parties show the will to deal with this change within the system of their contract, it would be possible to adapt the contract according to the contractual clauses regarding alterations. The articles of the FIDIC (Fédération Internationale des Ingénieurs-Conseils) Conditions of Contract for Works of Civil Engineering [hereafter FIDIC Conditions] deserve particular attention as being the most referred rules on this matter.

It is not always possible to restore the contractual equilibrium within the system of the contract where a hardship situation renders the performance burdensome for one of the parties. For these situations, it would be helpful to insert a hardship clause in the contract or to make reference to a legal system which provides for this institution as the applicable law in order to enable third persons (this would probably be an arbitrator) to use it in order to restore the balance of the contract.

The FIDIC Conditions and the principles evolved in the arbitral case law provide for some remedies for the alterations in the execution of construction contracts. These remedies will be summarised below.

1) Alterations in the execution of the contract under the FIDIC Conditions

The fact that the practice of construction contracts is well established enables the parties to foresee most risks which might affect the execution of the contract. Model construction contracts often contain provisions on how to modify the contract without the intervention of the third persons in case of happening of foreseeable events. The articles 51 and 52 of the FIDIC Conditions are the most applied provisions as FIDIC being the most applied model construction contract. Accordingly, article 51 puts that the engineer is entitled to instruct the contractor to make necessary variations in the name of the employer. The article 52 regulates how to fix the rate or price of the altered works. According to the article 67 of the FIDIC Conditions, the contractor can have recourse to arbitration if he does not agree with the engineer on the indispensability of the variation.

However, in the FIDIC practice it is not always possible to resolve the problems arising from the alterations in the execution of the contracts and/or the valuation of them through negotiations between the parties. The article 67 of the FIDIC Conditions in paragraph one provides for the condition of referring the dispute to the engineer before having recourse to arbitration. In case if the decision of the engineer does not satisfy the parties or the engineer fails to give notice of his decision within eighty-three days, then the parties would be entitled to start arbitration proceedings.

2) Hardship in international construction arbitrations

Transnational rules evolved in the practice of international construction contracts have reached the level of a specific lex mercatoria in this field, with the words of Charles Molineaux, a lex constructionis. One of the principles of the lex constructionis is the principle of rebus sic stantibus. In brief, this principle provides that the parties shall not be bound by the contract in case of fundamental changes in the conditions on which the contract was made.

To insert hardship clauses in long term contracts on the grounds of this principle is a very common practice. Given that the construction contracts are usually long term contracts, it would be useful to insert such clauses also in construction contracts. As will be discussed below, the parties may either stipulate a hardship clause according to their needs or benefit from model hardship clauses or they may refer to a set of rules which contain a provision on hardship.

The main lines of a hardship clause that the parties may draft may be emerged from contract practice, legal writings and transnational codifications. Accordingly, a hardship clause shall contain the following elements:

i) More or less defined conditions of hardship Instead of an enumeration of the conditions, it would be more appropriate to define them broadly in terms of their effects on the contract. These effects may be defined either in objective terms (such as a defined amount of the alteration in the balance of the contract) or in subjective terms (such as an excessive difficulty in the execution of the contract for one of the parties).

ii) Legal consequences of hardship Here, the legal consequences mean remedies such as giving notice of the situation, requesting renegotiations, having recourse to arbitrators or other third persons, recognizing the power to the third persons to intervene into the contract in order to restore the balance of the undertakings and the right to rescind the contract in case of the failure of renegotiations. Here, it should be stressed that providing for time limits would be helpful to ensure the healthy functioning of the procedure.

a) The Hardship Clause of the ICC (International Chamber of Commerce) 2003 leads the model hardship clauses from which the parties may benefit. Since this clause is not drafted considering the construction contracts in particular, it is of a broad nature. The application of this clause in arbitral case law is very limited as it does not provide for recourse to arbitration. However, the parties may draft a hardship clause to fit their needs on the grounds of this clause.

b) Parties may use the hardship provisions of transnational codifications as a model for their hardship clause. In particular, the article 6.2 of the UNIDROIT Principles may be useful for this purpose. The paragraph 6.2.1 of this article reminds the sanctity of contracts and emphasizes the exceptional nature of hardship. The paragraph 6.2.2 makes a definition of hardship in objective terms and enumerates the conditions of it. The paragraph 6.2.3 provides for the legal consequences of hardship. Accordingly, the parties shall first renegotiate the contract and in case if the renegotiations fail or do not produce any result they may resort to arbitration. In this case, arbitrators may either terminate the contract or adapt it in order to restore its equilibrium.

Alternatively, the parties may benefit from the article 6:111 of the European Contract Law. There is no significant difference between this provision and the article 6.2 of the UNIDROIT Principles.

III – Conclusion

The execution of construction contracts and the execution of large size projects in particular may take long time and they may be affected by changing circumstances. It may not always be possible to deal with the supervening effects of these changes on the contractual balance within the framework of the system of the contract (and the system of FIDIC Conditions in particular). In such a situation, to ensure the healthy continuation of the contract would be of great importance for the parties. For this reason, the parties are suggested to insert a hardship clause into their contract and enable the arbitrators to resolve their controversies accordingly