

**FORCE MAJEURE AND UNFORESEEN CHANGE OF CIRCUMSTANCES.
THE CASE OF EMBARGOES AND CURRENCY FLUCTUATIONS
(RUSSIAN, GERMAN AND FRENCH APPROACHES)**

ILYA KOKORIN,

Buzko Kokorin Law Firm (St. Petersburg, Russia),

JEROEN VAN DER WEIDE,

Leiden Law School (Leiden, The Netherlands)

*Economic and political instability has become a characteristic of many societies around the globe. Recent examples revealing the volatility of the current state of affairs include the trade restrictions imposed by the Russian Federation in August 2014, and currency fluctuations experienced by many countries, including Russia and potentially Greece. In this situation, one may wonder whether contract law has a solution to offer to the parties affected. Traditionally dominated by the *pacta sunt servanda* principle, jurisdictions made their own choices. This paper analyses approaches adopted by Russian, German and French law in response to situations of force majeure (trade embargoes) and unforeseen change of circumstances (currency fluctuations). In search for an explanation of each given approach, we reviewed historical arguments, as history played a crucial role in the formation of German and French responses, though in a completely different way. Whereas Germany, heavily affected by the cataclysms of the World Wars, was eager to adopt a lenient view on the possibility of the judicial revision of contracts, France never gave up its suspicion of court interventions. As legal preferences are often connected with cultural factors, we looked at distinct cultural traits of the societies at issue, by using the Hofstede index. We realized that there could be compelling cultural reasons why France and Germany are situated at opposite poles, while Russia is somewhere in the middle. Lastly, we took into account considerations derived from law and economics, arguing that narrowly construed court intervention might be economically justified in cases of impossibility and impracticability, as ultimately decreasing transaction and risk-appraisal costs.*

Keywords: *force majeure; unforeseen change of circumstances; embargo; currency fluctuations; Russian law; German law; French law.*

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1. Introduction

2014 has witnessed great challenges in the world political and economic arenas. Constantly falling oil prices and related financial risks, political turbulence in Western Europe, terrorist attacks in Paris and the war in Ukraine have shown that Fukuyama's 'end of history'¹ is still a nice theory rather than a true description of the current state of affairs. In such difficult times it becomes evident how interrelated the worlds of politics and economics are, since only a stable and predictable state policy can guarantee a constant flow of investments. In this regard, we see law as being an indispensable element of policy, which can either stimulate economic growth or facilitate market depression.

In response to sanctions imposed by the EU, the USA, Japan and several other states in the spring and summer of 2014, the Russian government, by its Decree No. 778 of August 7, 2014, imposed a 1-year ban on the imports of a wide range of US and European food products, including poultry, beef, pork, fruit, cheese, milk and other dairy goods. Notably, the exports of food and raw materials to Russia were worth €12.2 billion in 2013,² Russia was the EU's second-biggest market for food exports (10% of total), after the US (13%).³ In light of the above figures, it is hard to overestimate the economic impact of the imposed embargo, both for Russian and European business partners.

¹ Francis Fukuyama, *The End of History and the Last Man* (Free Press 1992), available at <<http://www.social-sciences-and-humanities.com/PDF/The-End-of-History-and-the-Last-Man-.pdf>> (accessed Jul. 26, 2015).

² Jennifer Rankin, *Russia Responds to Sanctions by Banning Western Food Imports*, The Guardian (Aug. 7, 2014), <<http://www.theguardian.com/world/2014/aug/07/russia-retaliates-western-sanctions-ban-food-imports>> (accessed Jul. 26, 2015).

³ *Russia Hits West with Food Import Ban in Sanctions Row*, BBC News (Aug. 7, 2014), <<http://www.bbc.com/news/world-europe-28687172>> (accessed Jul. 26, 2015).

The purpose of this article is to analyse how modern legal systems address complex problems arising in cross-border economic turnover: trade sanctions (embargoes) and steep currency fluctuations. We will see how Russian, German and French legal systems have traditionally treated situations of physical and legal impossibility, most often referred to as *force majeure*, and which contractual consequences can be claimed in such circumstances. The second part of this article will be devoted to a separate legal concept, which is commonly referred to as unforeseen change of circumstances or hardship.⁴ The choice of this topic is primarily driven by the rising trend in currency volatility, particularly in oil-exporting countries. Besides, one does not have to be a prophet to see what drastic economic consequences are to follow, should Greece leave the Eurozone.⁵ The case of unforeseen change of circumstances is legally distinct from *force majeure*, as it makes contractual performance more onerous, albeit still physically / legally possible. Nevertheless, functionally, these two concepts are very similar: they both deal with the problem of loss allocation and risk imputation. In the words of Justice Holmes, 'one who makes a contract never can be absolutely certain that he will be able to perform it when the time comes.'⁶ This premise holds true for any supervening future event, including trade restrictions and currency devaluations.

The countries indicated above have been chosen for two main reasons. Firstly, taking into account the character of Russian sanctions (restriction on import of agricultural products), Germany and France were potentially among those most heavily affected in terms of absolute value.⁷ Therefore, it seems more practical to look at these particular jurisdictions, since a hefty number of international sales agreements involving sanctioned goods would likely include a party from one of them. And secondly, apart from close economic ties, the civil law traditions of these countries have a lot in common; they have historically been influenced by each other, at least to some degree. All jurisdictions covered in this article, to one extent or another, are familiar with concepts of *force majeure* (physical impossibility) and unforeseen change of circumstances (hardship). Moreover, all of them are signatories to the UN Convention on Contracts for the International Sale of

⁴ In this article we might also interchangeably use such terms as 'impracticability' and 'economic impossibility'.

⁵ In its press release of June 29, 2015, the Dutch Employers' organisation for logistics and transport (EVO) urged its members to check whether their international contracts are 'Grexit-proof.' EVO recommended that its members renegotiate current agreements with their Greek counterparts on the basis of an unforeseen change of circumstances. The press release is available at <<http://www.evo.nl/site/zijn-uw-contracten-grexit-proof>> (accessed Jul. 26, 2015).

⁶ *Day v. United States*, 245 U.S. 159, 161 (1917).

⁷ For numbers, see Susanne Kraatz, *The Russian Embargo: Impact on the Economic and Employment Situation in the EU* (October 2014), <[http://www.europarl.europa.eu/RegData/etudes/BRIE/2014/536291/IPOL_BRI\(2014\)536291_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2014/536291/IPOL_BRI(2014)536291_EN.pdf)> (accessed Jul. 26, 2015).

Goods,⁸ which could give an additional impetus for adopting a unified or, at least, non-conflicting approach to situations of trade embargoes and currency fluctuations.

There exists an almost universal consensus among the jurisdictions studied that contracts shall be performed, an ancient maxim of *pacta sunt servanda* (agreements must be kept). This is one of the major legal principles supporting such values as legal certainty and stability of economic relations. However, the principle of *pacta sunt servanda* has never been applied without exception. Even in Roman law not all contracts were considered binding under all possible circumstances, although *clausula rebus sic stantibus* (a contract is binding only as long and as far as matters remain the same as they were at the time of conclusion of the contract) doctrine was not known to Roman lawyers.⁹ The relative character of the inviolability of contracts has been determined by a coexistence with other important legal norms, such as justice, public interest, sanctity of life and private property, good faith and fairness. It is not always clear how these norms relate to each other should a conflict arise. It is even more interesting to determine the significance and the place of *pacta sunt servanda* theory among these other values. Each legal system developed its own set of legal theories and approaches to justify deviation from the strict adherence to contracts, as initially agreed upon by the parties.

As noted above, in this article we will deal with three legal systems and their treatment of *force majeure* and unforeseen change of circumstances, in particular. It is in this comparative character, that we will try to show the common and divergent trends peculiar to the legal traditions in question. It is true that not all of them have witnessed such disruptive events as economic sanctions and steep currency fluctuations. Or, to put it differently, even if they did, the magnitude of such events is incomparable. This unique experience can in part elucidate on modern attitudes to the concepts of impossibility and impracticability as developed in the jurisdictions studied herein. Historical arguments, however, present only part of the picture. Other considerations, including cultural differences (attitude to risk, level of individualism, etc.) and economic aspects (cost-benefit analysis) also play an important role. All these will be dealt with in the following pages. For cultural analysis we will use the Hofstede's cultural dimensions theory,¹⁰ which describes the effects of a society's

⁸ U.N. Comm'n on Int'l Trade Law, U.N. Convention on Contracts for the International Sale of Goods, U.N. Doc. A/CONF.97/18, U.N. Sales No. E.10.V.14 (1980), S. Treaty Doc. No. 98-9 (1983), 1489 U.N.T.S. 3, 19 I.L.M. 668 (1980), at <<http://www.uncitral.org/pdf/english/texts/sales/cisg/V1056997-CISG-e-book.pdf>> (accessed Jul. 26, 2015) [hereinafter CISG]. The concept of *force majeure* is covered by Art. 79 therein. The answer to the question whether or not Art. 79 CISG covers the concept of hardship is still a matter of ongoing debate.

⁹ Reinhard Zimmermann, *The Law of Obligations: Roman Foundations of the Civilian Tradition* 579 (Clarendon Press 1996).

¹⁰ For more information on the Hofstede's cultural dimensions theory, see: <<http://geert-hofstede.com/national-culture.html>> (accessed Jul. 26, 2015); Geert Hofstede et al., *Cultures and Organizations: Software of the Mind* (3rd ed., McGraw-Hill 2010). We are aware of the criticism of this theory, but believe that if wisely applied, it can make a valuable contribution to the study of law.

culture on the values of its members. The Hofstede's model consists of six dimensions, each indicating independent preferences for one state of affairs over another. Such preferences include individualism / collectivism, long term orientation / short term normative orientation, masculinity / femininity, etc. Each dimension is being assigned a country-specific score from 1 to 100, depending on the importance of a given value in a given society.

Before we start, it is important to note that it is not the purpose of this article to provide a formula or a scheme on how embargoes or currency fluctuations are to be treated in Russia, Germany and France.¹¹ We are not going to answer whether *force majeure* or unforeseen change of circumstances will be effectively embraced by courts in light of the recent political and economic events. Such an approach would most certainly lead to oversimplification and negate the complexities existing within the legal systems in question, let alone taken in their comparative overview. Despite the fact that in many cases application of Russian, German or French law will bring about the same result, one should always be aware of the persistent theoretical differences and the evolving character of laws and legal doctrines, which may have practical effects on resolving cases of supervening events.

2. Russian Law Approach: From One Crisis to Another

2.1. Force majeure and Embargoes

Provisions of Russian law related to the topic of this article can be found in Arts. 401 and 417 of the Russian Civil Code¹² [hereinafter RCC]. Article 401(3) is devoted to the issue of liability for violation of contractual obligations and establishes:

Unless otherwise stipulated by law or contract, a person acting in a commercial setting, who failed to perform an obligation or performed it in an improper way . . . shall be liable *unless* he can prove that due performance was impossible because of irresistible force, i.e. extraordinary circumstances, which were impossible to avert under the given conditions.

Article 417(1) deals with the termination of obligations and provides for such termination in full or in part if, due to an act of a state body or municipal authority, performance under the contract has become impossible in full or in part.

It is clear from the above, that: 1) Russian law provides for a no-fault or strict liability regime in B2B relations; 2) issues of termination of contractual obligations

¹¹ The inability to develop a coherent positive theory consistent with the typical outcomes in the recurrent cases has been recognized by Richard Posner. See Richard A. Posner & Andrew M. Rosenfield, *Impossibility and Related Doctrines in Contract Law: An Economic Analysis*, 6(1) J. Legal Stud. 83 (1977).

¹² The English translation of Parts I, II and III of the Russian Civil Code is available at <<http://www.russian-civil-code.com/>> (accessed Jul. 26, 2015).

and liability for non-performance / defective performance are treated separately; 3) discharge from liability is allowed only if the circumstances preventing performance are exceptional and unavoidable.

The first point entails that a party in B2B relations is liable for non-performance even in the absence of its fault, unless it can prove the existence of a *force majeure* event, which prevented proper performance. We will get back to the distinction between fault and strict liability regimes later on, as we consider German and French approaches to impossibility.

As we turn to the second issue raised, we need to point out that the exact relationship between Art. 401 (*force majeure*) and Art. 417 (impossibility of performance due to a state act) / Art. 416 (impossibility of performance) is unclear. Some of the authors believe that the former is an example of the latter.¹³ In any case, the sphere of application of Art. 417 remains uncertain and we were unable to find any cases where a court applied this article to situations of trade restrictions. Other scholars have noticed that Art. 417 was designed for cases of subsequent impossibility of performance, provided that such impossibility is permanent.¹⁴ Due to the fact that the majority of state acts and their consequences are *ab initio* temporal (e.g., they are either adopted for a definite period of time or can be revoked in the future), it is doubtful whether this article can at all be applied to situations of embargoes.

In line with this logic, but characterizing the concept of impossibility as such, Hüseyin Can Aksoy argues that ‘temporal impossibility is not impossibility in the technical sense’ and that ‘the concept of impossibility has a permanent and definite nature’.¹⁵ We would not be going so far as to deny the application of the impossibility doctrine to impediments of temporary nature.¹⁶ The only difference might be in the result. Whereas the continuation of contractual relations in cases

¹³ Будылин С.Л. Запрет на импорт: форс-мажор или непредвиденное обстоятельство? [Budylin S.L. *Zapret na import: fors-mazhor ili nepredvidennoe obstoyatel'stvo?*] [Sergey L. Budylin, *Prohibition of Import: force majeure or Unforeseen Event?*], Zakon.ru (Aug. 12, 2014), <http://zakon.ru/blog/2014/08/12/zapret_na_import_forスマazhor_ili_nepredvidennoe_obstoyatel'stvo> (accessed Jul. 26, 2015).

¹⁴ Комментарий к Гражданскому кодексу Российской Федерации. Часть первая (постатейный) [Kommentarii k Grazhdanskому kodeksu Rossiiskoi Federatsii [Commentary to the Civil Code of the Russian Federation. Part One (itemized)]] (Aleksander P. Sergeev, ed.) (Prospekt 2010); Карапетов А.Г. Расторжение нарушенного договора в российском и зарубежном праве [Karapetov A.G. *Rastorzhenie narushennogo dogovora v rossiiskom i zarubezhnom prave*] [Artem G. Karapetov, *Termination of Breached Contract in Russian and Foreign Law*] (Statut 2007). Some of Russian courts also emphasized that acts mentioned in Art. 417 should lead to an objective and unconditional impossibility of preserving future obligations. See, e.g., Ruling of the Federal Commercial Court of the Far Eastern District of April 29, 2010. Case No. A59-4825/2009.

¹⁵ Hüseyin C. Aksoy, *Impossibility in Modern Private Law: A Comparative Study of German, Swiss and Turkish Laws and the Unification Instruments* 172 (Springer 2014).

¹⁶ Compare, for instance, with a nuanced approach of German courts to cases of temporal impossibility. See *infra* Ch. 3.

of permanent impossibility seems illogical, temporal impediments shall not lead to automatic and unavoidable termination of contractual obligations. The result-driven approach allows avoiding a seemingly strained argument that impossibility becomes permanent when the date of performance is an essential component of the obligation, even though factors causing impossibility are temporal in nature.¹⁷ Unilateral termination of a contract under Russian law as a general rule is only warranted in cases of material breach (Art. 450 RCC), unless otherwise stipulated in the contract itself. The longer a temporary impediment exists, the more likely is the delay to be characterized as a fundamental breach of the contract.

The situation with the application of Art. 417 has been further complicated by the recent amendments to the RCC,¹⁸ which now provides that if an act of a state body is held void or repealed, the obligation shall not cease, unless otherwise agreed by the parties or follows from the nature of the obligation, or if the creditor has not refused to perform an obligation within a reasonable time. Thus, Art. 417 creates a fiction that an obligation never ceased to exist, even though the impediment might have appeared indefinite in the first place. In our opinion, this provision creates legal uncertainty, as an obligation may cease to exist due to the adoption of a state act (outside the sphere of influence of the contracting parties), but then suddenly reappear after the state act is held void or is repealed. It is not a usual or normal thing to expect that a state act is held void or repealed, especially when adopted for a definite period of time. Sadly, the new version of Art. 417 also does not clarify its application to situations of temporal impossibility. In our view, a better solution (both economically and morally, from the perspective of the principle of party autonomy in contract law) would be to let the contracting parties decide when contractual obligations are to be terminated. In case of a dispute, it would be for the court, guided by the considerations of reasonableness and fairness to decide whether circumstances of a particular case warrant such termination.

As follows from the wording of Art. 401(3), circumstances preventing performance must be exceptional and unavoidable. The Russian Supreme Commercial Court clarified that the exceptional nature of irresistible force (*force majeure*) entails something ‘going beyond the “normal” and ordinary course, extraordinary for a particular life situation . . . which can never be taken into account’.¹⁹ The Court further emphasized that *force majeure* has in its substance objective, and not subjective unavoidability. For instance, the Court refused to consider fire a *force majeure* event since the objective criteria of unavoidability were not satisfied, *i.e.* the number of fire fighters involved, being a subjective criterion, was relevant in preventing fire from

¹⁷ Aksoy, *supra* n. 15, at 172.

¹⁸ Introduced by the Federal Law No. 42-FZ of March 8, 2015, which entered into force on July 1, 2015.

¹⁹ Ruling of the Presidium of the Supreme Commercial Court of the Russian Federation of June 21, 2012. Case No. A40-25926/2011-13-230.

damaging the property.²⁰ So when the consequences of a supervening event are capable of being mitigated or prevented by the parties concerned (e.g., by sending an additional number of fire fighters to the fire scene), such an event would not release a debtor from its liability. The criterion of objectivity will not play an important role in case of embargoes, when the illegality of performance is indisputable and cannot be changed by the parties.

The Russian Supreme Court highlighted that supervening events should also be objectively unforeseeable.²¹ This last element of the *force majeure* test turns out to be the most problematic, when it comes to state acts and currency fluctuations. For example, in a recent case the court refused to treat the temporary restriction on the import of live animals from the EU imposed in March 2012 as a *force majeure* event. The court argued that such restrictions were not unique and could have been found in the past. In particular, the information on such previous restrictions in this case was publicly available on the website of the Russian Federal Service for Veterinary and Phytosanitary Surveillance (*Rosselkhoznadzor*).²² This is, in our view, a rather far-reaching conclusion, effectively depriving parties of *force majeure* defence in all or nearly all cases of state-issued export or import bans.

It is hard to justify such a strict approach on the basis of risk of loss that every contracting party should be deemed to have assumed ('commercial risk'), since particular types of embargoes (embargoes imposed on a particular product from a particular country) are almost impossible to predict, unless one has supernatural powers. This is why in this case 'allocation of the risk to one or the other party cannot operate as an incentive for the party to invest in order to reduce such a risk'.²³ Though the statement that 'there is nothing new under the sun' may hold true, the mere fact that restrictive measures such as trade bans were imposed in the past does not, in our view, create a sufficient level of foreseeability.²⁴ The court's logic is a good example of the hindsight bias, signifying an inclination to consider an event as being predictable, after the event has occurred, despite little or no objective basis for predicting it. Transaction costs of negotiating the allocation of all possible risks in

²⁰ Ruling of the Presidium of the Supreme Commercial Court of the Russian Federation, *supra* n. 19.

²¹ Decision of the Supreme Court of the Russian Federation of March 14, 2012. Case No. AKPI12-69.

²² Ruling of the Federal Commercial Court of the North-Western District of June 27, 2014. Case No. A21-8837/2012.

²³ *Unexpected Circumstances in European Contract Law* 49 (Ewoud Hondius & Hans C. Grigoleit, eds.) (Cambridge University Press 2011).

²⁴ Restrictions on the import of various categories of food products have regularly been imposed by the Russian Federal Service for Veterinary and Phytosanitary Surveillance. For instance, such embargoes concerned pork and pigs (Letter No. FS-GGVI/7340 of July 17, 2009), poultry, hatching eggs, down and feather (Letter No. FS-NV-2/510 of January 25, 2010), fruits (apple, pear, cherry, apricot, plum, etc.) (Letter No. FS-AS-3/13028 of July 18, 2014), alcoholic drinks (cognac, wine (including sparkling wine)) (Letter of the Chief State Sanitary Doctor No. 0100/3835-06-23 of April 4, 2006).

situations where the occurrence of a risk is remote and largely improbable, if we take together all relevant transactions, might outweigh post-contractual loss multiplied by the probability of such a loss. The result so achieved will be the net welfare loss. This situation would certainly contravene the purpose of the law to 'reduce the costs of contract negotiation by supplying contract terms that the parties would probably have adopted explicitly had they negotiated over them.'²⁵

It appears to be a different scenario when a party has or should reasonably have knowledge about the proposed embargo, as in the case of public discussions of a respective bill or draft government decree, or when the unforeseen regulation entered into force after a due date for performance of a contractual obligation.²⁶ The *force majeure* argument will also fail in situations when state acts have a secondary or accidental effect on contractual relations, i.e. they are not the primary cause of impossibility (legal or factual) to perform.²⁷ The courts would equally refuse to release a party from its liability when the performance is technically possible, e.g. by contracting with new suppliers residing in countries outside the sanctions list,²⁸ or by using rented premises for purposes of storing food coming from non-sanction countries, even if such were primarily used for storage of the sanctioned goods before.²⁹

The International Commercial Arbitration Court at the RF Chamber of Commerce and Industry [hereinafter ICAC] has also shown reluctance in accepting the *force majeure* argument in cases concerning state-imposed impediments. For instance, the ICAC refused to consider a ban on international currency transfers imposed by the Central Bank of Russia in 1998 as *force majeure*.³⁰ In that case an Italian company (seller) claimed the purchase price from a Russian company (buyer) for the goods delivered under the contract. The buyer argued that he had made payment orders to the Russian bank, which was unable to effect the transfer due to the above ban. While refusing to release the buyer from contractual liability, the tribunal argued that the failure to perform contractual obligations was caused by a third party, namely the Russian bank, and that the defendant failed to prove that such third party, if sued,

²⁵ Posner & Rosenfield, *supra* n. 11, at 88.

²⁶ Ruling of the Federal Commercial Court of the North-Western District of June 4, 2007. Case No. A21-4850/2006.

²⁷ For instance, in a number of judgments Russian courts refused to consider the economic crises of 1998 and 2008 as *force majeure* events, arguing that mere financial difficulties fall within the assumed commercial risks inherent to business activity. See: Ruling of the Federal Commercial Court of the North-Western District of April 17, 2001. Case No. 4327; Ruling of the Fifteenth Appellate Commercial Court of April 26, 2010. Case No. A53-18991/2009; Ruling of the Ninth Appellate Commercial Court of March 15, 2010. Case No. 91450/2009.

²⁸ Decision of the Commercial Court of the City of Moscow of April 2, 2015. Case No. A40-209173/14.

²⁹ Ruling of the Thirteenth Appellate Commercial Court of May 29, 2015. Case No. A56-71546/2014.

³⁰ Award of the ICAC at the RF CCI of July 30, 2001. Case No. 198/2000.

would have been exempt from liability.³¹ The absurdity of this argument is evident from the fact that in the case at hand currency transfers were not allowed, regardless of bank involvement.

The jurisprudence cited above reveals the unwillingness of Russian courts and some arbitration tribunals to admit the applicability of *force majeure* defence in cases related to state conduct. This conclusion goes in line with the findings of other scholars.³² Therefore, it is well advised to allocate all risks related to state actions and temporary export and import bans, in particular, by using contractual arrangements. Only those circumstances which fall under the legal definition of *force majeure*, *sensu stricto*, will be treated as such.³³ This, however, shall not prevent parties from agreeing on the consequences of certain events, whether referred to as *force majeure* or not.³⁴ After all, Art. 401(3) RCC has a dispositive character and may be departed from. However, while balancing contractual risks and allocating liability, one should keep in mind that liability for intentional breach of contract cannot be limited (Art. 401(4) RCC), just like in German and French law. Other restraints of contractual freedoms could stem from consumer protection laws and other specific legislation.

2.2. Economic Instability and Currency Fluctuations

So far, we have looked at the issue of trade restrictions and the applicability of force majeure rhetoric with relation to such state actions. Now we will turn to another topical subject, namely currency fluctuations. The Swiss franc jumped by 30% in a matter of minutes in January 2015. During 2014, the Russian rouble fell by 40% against the dollar, while the Canadian and Australian dollar have recently both dropped to six-year lows against the US dollar.³⁵ The question arises whether such economic processes could have any contractual effect in agreements where the

³¹ The tribunal decided the case on the basis of CISG. Nevertheless, the case is relevant, since Russia is a signatory to CISG and the wording of Art. 79 is similar to Art. 401 RCC.

³² Schlechtriem & Schwenzer: *Commentary on the UN Convention on the International Sale of Goods (CISG)* 1071 (Ingeborg Schwenzer, ed.) (3rd ed., Oxford University Press 2010); Николюкин С.В. Основания освобождения от ответственности в практике международного коммерческого арбитража // Право и экономика. 2009. № 5. С. 96–101 [Nikolyukin S.V. Osnovaniya osvobozhdeniya ot otvetstvennosti v praktike mezhdunarodnogo kommercheskogo arbitrazha // Pravo i ekonomika. 2009. No. 5. S. 96–101 [Stanislav V. Nikolyukin, *Grounds for Release from Liability in Case Law of International Commercial Arbitration*, 2009(5) Law and Economics 96–101]].

³³ For instance, in a recent ruling, dated April 21, 2015 (Case No. A43-28160/2014), the Commercial Court of Nizhny Novgorod Region held that ‘extension of the list of events capable of relieving a party from liability for non-performance is prohibited by Art. 401 RCC, which sets out that *force majeure* shall presuppose events which are extraordinary and unavoidable.’

³⁴ Amendments to the RCC introduced by the Federal Law No. 42-FZ of March 8, 2015, explicitly allow parties in B2B transactions to agree on the compensation of losses caused by impossibility (Art. 406(1) RCC).

³⁵ *Why Currency Volatility Has Got Worse*, The Economist (Feb. 3, 2015), <http://www.economist.com/blogs/economist-explains/2015/02/economist-explains-2> (accessed Jul. 26, 2015).

price is set in foreign currency, e.g., in releasing a defaulting party from its liability or allowing for a change in contractual terms through judicial means.

Russian legislation generally allows a contract to be terminated or amended in court, should the circumstances in which the contract was made have changed materially (Art. 451 RCC).³⁶ Apart from the fundamental character of change, in order to rely on this article, a debtor will have to prove that the change of circumstances was insurmountable, unforeseeable and external to the parties. These turn out to be a high threshold to pass. Some of the commentators even noted that for the whole period of the RCC's existence, there has only been one event recognized by courts as satisfying the criteria of Art. 451, namely the default of 1998.³⁷ As we will show below, even the economic crisis, which hit Russia in the second half of the 1990^s, was hardly considered as an unforeseen change of circumstances.

In times of economic turmoil, parties often attempt to enhance their position by claiming that the contract should be brought to an end or amended in their favour. However, as we pointed out above, the respected claim may only be successful when the change of circumstances is unforeseeable, the requirement similar to the one attributable to *force majeure*. Unlike trade bans, however, currency fluctuations are a characteristic element of the world economy. They are 'a natural outcome of the floating exchange rate system that is the norm for most major economies'.³⁸ Accepting this argumentation, Russian courts do not consider devaluation of a national currency as valid ground for terminating or amending a contract under the above material change of circumstances doctrine.³⁹ In one of the decisions, while noting a general economic volatility of Russia, the court summed up that the conclusion of a loan agreement, regardless of whether it was made in a foreign

³⁶ Despite the fact that Art. 451(4) RCC provides that an agreement may be amended only in exceptional circumstances, while the termination is a general rule, in practice courts almost equally terminate and revise contracts. See Петрищев В.С. Существенное изменение обстоятельств: правоприменение ст. 451 ГК РФ и опыт стран общего и континентального права: Препринт WP10/2007/06 [Petrishchev V.S. *Sushchestvennoe izmenenie obstoyatel'stv: pravoprimenenie st. 451 GK RF i opyt stran obshchego i kontinental'nogo prava: Preprint WP10/2007/06* [Vadim S. Petrishchev, A Fundamental Change of Circumstances: The Practice of Application of the Art. 451 of the Civil Code of the Russian Federation and the Legal Experience of the Common and Continental Law Countries: Preprint WP10/2007/06]] 32 (Higher School of Economics 2007), available at <https://www.hse.ru/data/2010/05/06/1216457923/WP10_2007_06.pdf> (accessed Jul. 26, 2015).

³⁷ Брагинский М.И., Витрянский В.В. Договорное право. Книга пятая. В двух томах. Т. 1 [Braginsky M.I., Vitryansky V.V. *Dogovornoe pravo. Kniga pyataya. V dvukh tomakh. T. 1* [Mikhail I. Braginsky & Vasiliy V. Vitryansky, Contract Law. 1 Book Five]] (Statut 2006).

³⁸ *The Effects of Currency Fluctuations on the Economy*, Investopedia (Aug. 8, 2013), <<http://www.investopedia.com/articles/forex/080613/effects-currency-fluctuations-economy.asp>> (accessed Jul. 26, 2015).

³⁹ See: Ruling of the Federal Commercial Court of the Moscow District of January 4, 2001. Case No. KG-A40/6004-00; Decision of the Supreme Commercial Court of the Russian Federation of April 28, 2007. Case No. A75-2991/2006.

currency or in roubles entails the risk of changing circumstances. This, as the court argued, was derived from the constant inflation processes.⁴⁰

This unwillingness of the Russian judiciary to consider currency fluctuations as a ground for termination or revision of contracts might have its cultural explanations. According to the Hofstede's index, Russian society is extremely risk-averse (score 95 in uncertainty avoidance) and prefers certainty and predictability. This explains a complex bureaucratic system, existing in Russia from time immemorial.⁴¹ This also accounts for the rigid interpretation and application of laws and regulations. As a matter of fact, what could be more stable than limited intervention or better, no intervention at all? Based on the same index, the Russian approach to unforeseen change of circumstances may also have its backing in the long term orientation (81), signalling a pragmatic mind-set. Allowing Art. 451 RCC defence in the aftermath of the 1998 crisis could have had a tremendous effect on the Russian economy, undermining performance of hundreds or possibly thousands of contracts. Lastly, low scores for masculinity (36) and indulgence (20) indicate a pessimistic view of the present and future. No wonder economic instability is seen as something indispensable and 'normal'!

It is true that changing currency exchange rates are characteristic of international economic turnover. However, we would not go as far as to claim that any degree of change represents a normal or ordinary situation. The issue of foreseeability should be considered in light of the degree of currency volatility and previous economic history of a particular country. We assume that there might be situations in which a jump in currency exchange rates or inflation would be so drastic and unexpected that the considerations of justice, fairness and good faith might require the adjustment or termination of a contract. Recent amendments to the RCC elevated the principle of good faith to the level of general principles of contract law (Art. 1(3) RCC). According to this principle, the parties to a contract shall act not only in line with the law and contractual provisions, but also in accordance with the principles of good faith and fair dealing. They should also provide the necessary assistance to achieve the purpose of the contract (Art. 307(3) RCC). We believe that good faith could be used as a legal ground for restoring the shattered contractual equilibrium in cases of unforeseen change of circumstances. We will turn to this issue in the next chapter looking at the German response to the post-World War I economic debacle. The difficulty would naturally lie in determining where the line for court intervention has to be drawn.⁴² For instance, the depreciation in the value of national currency

⁴⁰ Ruling of the Federal Commercial Court of the West-Siberian District of January 11, 2007. Case No. F04-8719/2006.

⁴¹ It has been noted that bureaucratic behavior is notoriously risk averse. See Niklas Luhmann, Risk: A Sociological Theory 190 (Rhodes Barret, trans.) (De Gruyter 1993).

⁴² For instance, Schwenzer argues that in international contracts a price increase or decrease mandating adjustment or termination of a contract shall be 150–200%. See Ingeborg Schwenzer, *Force Majeure and Hardship in International Contracts*, 39 Vict. U. Wellington L. Rev. 709, 717 (2008), available at <<http://www.austlii.edu.au/nz/journals/VUWLawRw/2008/39.pdf>> (accessed Jul. 26, 2015).

in Russia or France has never reached such depths as in Germany during the 1920^s or 1930^s. We can only speculate whether the magnitude of the possible economic consequences could have changed the Russian approach.

As a separate note, we believe that consumer loans in foreign currency may dictate a more nuanced approach, specifically in a setup where a bank induces the conclusion of a loan agreement, by advertising it or emphasizing the stability of exchange rates.⁴³ In a recent case,⁴⁴ a court ordered a bank to recalculate the amount to be paid back under the loan agreement made in USD, based on a fixed currency rate, twice as low as the current USD to RUB exchange rate. In doing so, the court took into account the status of the parties involved (on the one hand, a consumer having no prior knowledge of the financial markets and a professional credit institution, on the other), the fact that it was a mortgage loan, the behaviour of the bank (consultations confirming the stability of the exchange rate),⁴⁵ unfair contractual provisions related to risk allocation and reduction of negative consequences. Notably, the court characterized the situation of a steep drop in the value of the Russian currency as a *force majeure* event, relieving the non-performing party of any penalties. This is rather strange, bearing in mind that *force majeure* under Russian law requires impossibility of performance, physical or legal.

In any case, court interference in the area of contractual relations should be limited, be it B2B or B2C transactions. Even in situations of consumer loan agreements in foreign currency, caution must be paid so as not to encourage ill-judged consumer behaviour. The recalculation of loans could also have a bearing on the economic balance in the banking industry as a whole, because the risks related to loans in foreign currency would ultimately be shifted to other consumers, e.g., in the form of increased interest rates.

Ewoud Hondius and Hans Christoph Grigoleit have divided the European jurisdictions into two categories: 'closed' and 'open' regimes. Legal systems with an established general doctrine, specifically addressing the issue of unexpected circumstances, that can lead to an adjustment of contracts are referred to as 'open' (Germany, the Netherlands, Spain, etc.). Conversely, 'closed' systems (Belgium, England, France, etc.) either lack a general exceptional remedy addressing unforeseen circumstances or, even if the respective doctrine exists, it cannot lead to contractual adaptation, as a general rule.⁴⁶ As we have shown above, Russia would probably fit into the category

⁴³ Ruling of the Presidium of Belgorod Regional Court of March 28, 2013. Case No. G-44-17.

⁴⁴ Decision of the Pushkin City Court of Moscow Region of February 4, 2015. Case No. 2-878/2015. This decision has been overruled by the Moscow Region Court, whose ruling is not yet available.

⁴⁵ False assurances related to future currency exchange rates given by the bank to a consumer may be regarded as misrepresentation. This, according to Art. 431(2) RCC, shall entitle the consumer to claim damages arising out of such misrepresentation.

⁴⁶ Ewoud Hondius & Hans C. Grigoleit, *Introduction: An Approach to the Issues and Doctrines Relating to Unexpected Circumstances*, in *Unexpected Circumstances in European Contract Law*, *supra* n. 23, at 3, 11.

of 'open' jurisdictions, from the purely doctrinal point of view. It clearly provides for termination or adjustment of contracts in cases of unforeseen circumstances (Art. 451 RCC). At a closer look, however, it is clear that the Russian judiciary is rather reluctant to grant relief in situations of unexpected circumstances. Notably, the same holds true for the restrictive application of the *force majeure* doctrine.

3. German Law Approach: Complexity and Flexibility

3.1. Force majeure and Trade Restrictions

Unlike the Russian system of civil liability, which as a general rule accepts strict liability in business relations (Art. 401(3) RCC), German law is characterized by the principle of fault (*Verschuldensprinzip*).⁴⁷ Liability for a failure to perform contractual obligations would require at least negligence on the side of the performing party.⁴⁸ A person is considered as acting negligently if he fails to exercise reasonable care, § 276(2) of the German Civil Code (*Bürgerliches Gesetzbuch*)⁴⁹ [hereinafter BGB]. Therefore, situations of unavoidable and extrinsic events rendering performance of a contract impossible would usually not require special treatment and reference to specific legal provisions related to *force majeure*.

Import and export restrictions can be seen as developments creating legal impossibility (*rechtliche Unmöglichkeit*) to perform under a sales agreement. As opposed to absolute (physical) impossibility, delivery of goods remains possible, since such goods are available on the international market. However, trade bans imposed by public authorities render such performance illegal, thus creating objective impossibility whereas neither the debtor nor anybody else is able to perform. We presume that no one can be obliged or expected to break the law, even if punishment does not follow, as for instance, in the case where trade restrictions are not enforced by the authorities.

In addition to the doctrine of fault liability, § 275(1) BGB directly provides that '[a] claim for performance is excluded to the extent that performance is impossible for the obligor or for any other person.' As follows from the above provision, impossibility of performance relieves the party from the claim of specific performance, regardless whether impossibility is caused by such a party. For the purposes of applying § 275(1) BGB it is also irrelevant whether impossibility is initial or subsequent, objective or subjective, partial or total.⁵⁰ Similar to Russian law, application of German

⁴⁷ Philip Ridder & Marc-Philippe Weller, *Unforeseen Circumstances, Hardship, Impossibility and Force Majeure under German Contract Law*, 22 European Review of Private Law 371, 373 (2014); Wolfgang Fikentscher & Andreas Heinemann, *Schuldrecht* 320 (10th ed., De Gruyter 2006).

⁴⁸ Ridder & Weller, *supra* n. 47, at 373.

⁴⁹ English version of the German Civil Code is available at <http://www.gesetze-im-internet.de/englisch_bgb/> (accessed Jul. 26, 2015).

⁵⁰ Fikentscher & Heinemann, *supra* n. 47, at 188; Das neue Schuldrecht 108 (Barbara Dauner-Lieb et. al., eds.) (C.F. Müller 2002); Peter Schlechtriem, *Schuldrecht: Allgemeiner Teil* 151 (Mohr Siebeck 2003).

law does not lead to automatic termination of the contract – the contract remains valid.⁵¹ Its enforcement, however, could not be mandated. The debtor remains liable, unless he can prove that he is not responsible for the impediment or that he could not have known about it, in case of initial impossibility (§ 280, § 311a BGB).

Driven by the considerations of good faith, German law protects the defaulting party from contractual liability, provided that certain conditions are satisfied. At the same time, obligations deriving from the contract are kept in force and the contract remains valid and binding upon the parties. This rule ensures security of commercial dealings, as the non-defaulting party might still be interested in keeping contractual relations alive, even though performance of the contract might temporarily become impossible.⁵² In case of impossibility of performance, the creditor is entitled to unilaterally revoke the contract, without the need of providing additional time for performance (*Nachfrist*) (§ 326(5) BGB).⁵³ The creditor's right to terminate the contract is not affected by the nature of the impossibility and whether the debtor is in any way responsible for the impediment.⁵⁴

The question arises whether temporary impossibility of performance, such as in case of most trade restrictions, always mandates termination of the contract by the creditor. We could think of situations where such a termination could be unjust and lead to disproportionate losses on the side of the debtor. Such losses may take form not only in damages to be paid under § 280 BGB (in case the debtor knew or should have known about the proposed trade ban), but also preparation and delivery costs. There is no special provision in the BGB addressing the issue of temporal impossibility.

In practice, German courts take a nuanced approach, analysing all relevant facts of a particular case and balancing parties' mutual interests.⁵⁵ A creditor does not always have a right to terminate an agreement due to a delay in performance, caused by temporal impossibility. This is especially so when time is of no essence. On the flipside, even if the impossibility is temporal in nature, it can nevertheless be equated with a permanent impossibility, if it is not foreseeable whether or when a particular impediment will cease to exist.⁵⁶ Temporal impossibility is also treated as permanent

⁵¹ Unexpected Circumstances in European Contract Law, *supra* n. 23, at 58.

⁵² The BGB does not make a distinction between absolute impossibility of performance, e.g. when a specific thing to be delivered under the contract is destroyed, and temporal impossibility, e.g. when importation of goods is temporarily restricted. See Fikentscher & Heinemann, *supra* n. 47, at 191.

⁵³ Similar mechanisms can be found in other jurisdictions, such as the Netherlands. See Art. 6:81 of the Dutch Civil Code, at <<http://www.dutchcivillaw.com/civilcodebook066.htm>> (accessed Jul. 26, 2015).

⁵⁴ Basil S. Markesinis et al., *The German Law of Contract: A Comparative Treatise* 407 (2nd ed., Hart Pub. 2006).

⁵⁵ See also Peter Mazzacano, *The Treatment of CISG Article 79 in German Courts: Halting the Homeward Trend*, 2012(2) Nordic Journal of Commercial Law, available at <http://njcl.fi/2_2012/mazzacano_peter.pdf> (accessed Jul. 26, 2015).

⁵⁶ Christoph Brunner, *Force Majeure and Hardship under General Contract Principles: Exemption for Non-Performance in International Arbitration* 251 (Kluwer Law International 2009).

if the achievement of the contractual purpose is called into question by such an impediment,⁵⁷ i.e. when time is of the essence. Thus, the German legal system, more so than the Russian one, considers legitimate interests of a creditor and debtor in determining whether impossibility mandates termination of the agreement. As we argued before, trade bans are usually imposed for a definite period of time, as in the case of the recent Russian embargoes. However, they could be either prolonged or revoked ahead of time, depending on the current political and economic situation. Taking this elusive nature of trade restrictions, we believe that a case-by-case approach to the issue of termination of contractual relations is well justified.

The second question that we need to address is under which conditions mandatory rules prohibiting contractual performance (e.g., imposition of trade bans) may excuse non-performance. As we pointed out above, impossibility under § 275(1) BGB corresponds to real impossibility, but also includes legal impossibility.⁵⁸ This means that the debtor cannot overcome the impediment by any legal means. In this respect, the Russian and German approaches are similar as the economic impossibility (hardship) does not fall under the general concept of *force majeure*. However, there are some important differences to be highlighted. Under Russian law, force majeure is characterized by such elements as unavoidability, unforeseeability, extraordinary and objective nature. German law and § 275(1) BGB, in particular, does not make a distinction between objective and subjective impossibility, impossibility caused by the debtor or independent impossibility, initial or subsequent impossibility.⁵⁹ For the purposes of this article we will review only the initial-subsequent impossibility and the related issue of foreseeability.⁶⁰

Initial impossibility exists when the impeding factor is present at the time of contract formation. Importantly, initial impossibility does not affect the validity of a contract, which remains fully effective (§ 311a(1) BGB), even though specific performance is barred.⁶¹ Regardless whether impossibility is initial or subsequent, the debtor is liable in damages, unless he can prove that he was not aware of the obstacles to performance when entering into the contract and that the lack of

⁵⁷ Brunner, *supra* n. 56, at 252.

⁵⁸ Fikentscher & Heinemann, *supra* n. 47, at 197.

⁵⁹ Aksoy, *supra* n. 15, at 11.

⁶⁰ Our decision is based on the presumption that, most of the time, embargoes lead to objective impossibility (impossibility for all and not just for the debtor), which is independent of the debtor (the debtor does not cause trade restrictions and cannot stop them). Thus, the most relevant elements to be compared are the time of occurrence of the impediment (prior or after conclusion of a contract) and foreseeability (whether imposition of trade restrictions was foreseeable at the time of conclusion of a contract).

⁶¹ This was different under the former law, which considered initial impossibility a ground for holding a contract void, following the Roman maxim *impossibilium nulla est* (of things simply impossible completely and physically, there is no obligation).

awareness was not imputable to him (§ 311a(2) BGB). In other words, liability is fault dependent, while fault is presumed. In order to avoid liability the debtor has to show that he did not know and should not have known of the existing impediment. This is logical and economically justified, as the debtor is usually in a better position to know and explain circumstances, which prevented him from performing accordingly.⁶² In other words, the debtor would usually be a superior risk-bearer. In cases of embargoes, when the text of the legal act imposing trade restrictions was made public in line with the applicable rules, in B2B transactions⁶³ there should be an irrefutable presumption of such knowledge. Russian law would follow the same logic, even more so due to the application of the no-fault liability regime.

The situation gets more complicated as we move from initial impossibility to a subsequent one, in which the obstacle to performance appears after the contract is concluded. It has been stressed in the literature that in case of subsequent impossibility, 'fault is determined in relation to whether the promisor is responsible for the impediment to performance,'⁶⁴ and not whether he knew or should have known of such an impediment. It goes without saying that normally state-imposed embargoes are independent of the will of the debtor, and thus cannot be attributed to him. But what if the plans for adopting trade restrictions are announced prior to the conclusion of the contract, so that such restrictions could have been foreseen at the time of the conclusion? We have shown above that in this case, even in the absence of specific information on the proposed state course of action but merely considering prior history of trade bans, Russian courts might be willing to accept the foreseeability of embargoes and thus deny the *force majeure* defence.

German law does not explicitly state the requirement of unforecastability. However, it can be inferred from the doctrine of initial impossibility, because the debtor has to inquire whether he is actually capable of performing the contract before he enters into it. If it is well known that the trade embargo will be imposed during the term of the contract, thus impeding its execution, considerations of good faith and risk allocation dictate that the debtor bears full responsibility for non-performance. It seems irrelevant that at the time of entering into a contract there are no trade restrictions in place, as long as it is sufficiently certain that contractual performance will be barred in the future. It can be argued that foreseeable obstacles are presumed

⁶² An interesting scenario is when either the creditor or both parties are (or should be) aware of a situation of initial impossibility at the time of entering into the contract. In such a case it seems unfair to impute all the blame on the debtor. We think that this situation can be characterized as contributory negligence. Therefore, liability of the defaulting party should be reduced, or eliminated at all, since the creditor could not have reasonably believed that the debtor would be able to perform the contract. There is no breach of the promise to perform as such.

⁶³ We assume that B2B transactions are most affected by trade restrictions.

⁶⁴ Markesinis et al., *supra* n. 54, at 485.

to be included in the equilibrium of the contract at the time of its formation. The most problematic issue is the level of precision of a future event, *i.e.* embargo, required for imputation of risks to the debtor. In our view, in B2B transactions, in case of threatened trade restrictions,⁶⁵ parties should adjust their contractual relations accordingly. This, however, does not go as far as to accept the logic that previously imposed periodic trade bans make all future embargoes foreseeable, as this would make the whole concept of initial impossibility meaningless. Moreover, it would substantially increase transaction costs related to the parties taking precautionary measures for risks, which are neither envisaged nor avoidable.

3.2. Currency Depreciation, Lessons from History

Now we will turn to the issue of currency fluctuations. As we have shown above, § 275(1) BGB only deals with factual impossibility (*impossibility sensu stricto*). Cases of economic impossibility (hardship), *i.e.* when performance becomes excessively burdensome, but still possible, have to be addressed with reference to § 275(2) or § 313 BGB. The exact relations between the two are not always clear as both of them deal with the situation of increased onerousness of the performance.⁶⁶

Section 275(2) BGB permits the debtor to refuse performance if, and as long as such performance requires expenses and effort which, taking into account the subject matter of the obligation and the requirements of good faith, are grossly disproportionate to the interest in performance of the creditor. It has been argued that the prevention of extreme cases of waste of resources is the macroeconomic goal of § 275(2) BGB and that the criterion of reasonability is examined in a cost-utility-analysis.⁶⁷ Therefore, it is the creditor's interest in obtaining performance that is decisive in the application of § 275(2) BGB. So long as this interest remains constant or changes to an insignificant extent while the debtor's obligation becomes grossly burdensome, the debtor shall be entitled to invoke impossibility as a defence / plea (*Einrede*).⁶⁸

We will not go deep into analysing various facets in the application of § 275(2) BGB, because we believe it to be inapplicable to situations of currency fluctuations. The reason being that market fluctuations (*e.g.*, price and currency changes) affect interests of both creditors and debtors, so that performance under the contract does not become grossly inefficient. For instance, a fall in the value of national

⁶⁵ This has to be determined on a case-by-case basis, taking into account the clarity of public statements, official position of a person making statement, likelihood of imposition of trade restrictions, etc.

⁶⁶ Fikentscher & Heinemann, *supra* n. 47, at 200. According to German legal doctrine, § 275 BGB has priority over § 313 BGB; when § 275 BGB and § 313 BGB are both potentially applicable, one should apply § 275 BGB.

⁶⁷ Hannes Rösler, *Hardship in German Codified Private Law – In Comparative Perspective to English, French and International Contract Law*, 15 European Review of Private Law 483, 494 (2007), available at <http://papers.ssrn.com/abstract_id=1154004> (accessed Jul. 26, 2015).

⁶⁸ Markesinis et al., *supra* n. 54, at 413.

currency may have a negative impact on the local producer,⁶⁹ whose production has become more onerous due to the fact that the component parts or raw materials are being delivered from abroad and thus paid at prices fixed in foreign currency, while the revenue is received in the denominated currency. Meanwhile, a buyer who entered into a contract with such a producer may win from the currency drop. The reason being that the local market would sooner or later react by raising prices (as happened after the rouble depreciation), so that the buyer would not be able to enter into a new contract for the same 'bargain' price, as before the fall. General market conditions will be different.

The cases of hyperinflation and dramatic currency fluctuations are not unfamiliar to Germany. In the aftermath of the World War I, the purchasing power of the German currency fell by 80%.⁷⁰ At the end of 1921, prices were 35 times higher than before the War. A year later they had risen to a level that was 1,457 times higher.⁷¹ In light of such unprecedented economic developments, the *pacta sunt servanda* principle traditionally praised by German judiciary could no longer provide an adequate solution to the problem felt by the society as a whole. No longer could risk be regarded as being assumed by transacting parties, as in the words of Professor Dawson, 'it was another thing to require that [a party] bear the risk of blind and capricious changes in the purchasing power of money'.⁷²

Reacting to these catastrophic events and taking a largely political decision, German courts first applied § 275(1) BGB by terminating the imbalanced contracts. It soon, however, became clear that the termination of contracts affected by unreasonable and unforeseeable hardship went too far and could have had disastrous economic consequences. Indeed, a one-sided and blunt breakdown of commercial relations would be inconsistent with the need for the equitable distribution of currency risks. Instead, the German *Reichsgericht* started applying the concept of a 'disturbance of the foundation of the transaction' (*Störung der Geschäftsgrundlage*), which at that time was based on § 242 BGB – the rule of good faith.⁷³ The court authorized the revalorization or adjustment of the contract price, noting, however,

⁶⁹ Or for that matter anyone else whose income is calculated in the depreciated national currency, e.g. borrower, who receives income in the national currency different from the currency of the loan.

⁷⁰ Rösler, *supra* n. 67, at 491.

⁷¹ *Id.* at 487.

⁷² John P. Dawson, *Effects of Inflation on Private Contracts: Germany, 1914–1924*, 33(2) Mich. L. Rev. 191 (1934).

⁷³ Before embracing the good-faith doctrine, some of the courts in Germany endeavored to ascertain the parties' initial intention and determine the 'implied' terms of the contract. The theory of 'implied' terms was used to discharge a party of an obligation, whose implementation subsequently turns out to be extremely burdensome. See Mahmoud R. Firoozmand, *Changed Circumstances and Immutability of Contract: A Comparative Analysis of Force Majeure and Related Doctrines*, 8(2) Bus. L. Int'l 171 (2007). On the *Störung der Geschäftsgrundlage* doctrine, see also Fikentscher & Heinemann, *supra* n. 47, § 27.

that ‘the fact alone that a subsequent change in the conditions is not foreseeable and could not be foreseen does not suffice.⁷⁴ What is really required is ‘such a fundamental and radical change in the relevant circumstances that it would be an intolerable result, quite inconsistent with law and justice, to hold the party to the contract.’⁷⁵

However, it seems that such a requirement was relatively easy to pass, as in the 1930^s the courts held that the devaluation of the national currency by 30% was sufficient to satisfy a substantial change criterion of the *Störung der Geschäftsgrundlage* doctrine.⁷⁶ In one reported case a devaluation of only 13% was held to be enough.⁷⁷ This low threshold is hard to reconcile with the German approach to inflation, which required the inflation to be extraordinary to satisfy the above test. We cannot come up with any reasonable explanation of this outcome, as the nature and consequences of inflation and devaluation of the national currency are to a great extent similar, i.e. they lead to the distortion of the equivalence of exchange. The only difference is that in case of inflation it is the creditor who suffers the negative effects, since the debtor’s contractual burden is substantially alleviated, whereas depreciation in the value of the national currency primarily hits the debtor, because it makes performance of the foreign-currency obligation more burdensome.

It is interesting how far away from each other the German and Russian doctrinal approaches may seem to be when it comes to the consequences of unforeseen changes of circumstances. Whereas the German ideal is to maintain the contract as far as possible and simply adjust it to the changed situation (manifestation of the principle *favor contractus*),⁷⁸ Art. 451(4) RCC permits adjustment only in exceptional circumstances, e.g. when termination of a contract results in damage to the parties far exceeding the costs necessary for the execution of the contract on revised terms. The position of the RCC is explained by the desire to avoid situations in which parties are bound together in a continuing hostile relationship and one or both of them are compelled to perform a contract on previously un-agreed terms.⁷⁹ Whatever the reasons for these divergent approaches might be, practical differences are rather overstated, as is evident from the fact that Russian courts are equally ready to amend contracts.⁸⁰ Additionally, termination of a contract pursuant to Art. 451 RCC can be accompanied

⁷⁴ RGZ 100, 129.

⁷⁵ BGH NJW 1959, 2203.

⁷⁶ RGZ 141, 212 (216); RGZ 163, 324 (333); RGZ 155, 137 (reported in Unexpected Circumstances in European Contract Law, *supra* n. 23, at 222).

⁷⁷ RGZ 147, 286 (289) (reported in Unexpected Circumstances in European Contract Law, *supra* n. 23, at 222).

⁷⁸ BGH NJW 1984, 1746.

⁷⁹ Брагинский М.И., Витрянский В.В. Договорное право. Книга первая: Общие положения [Braginsky M.I., Vitryansky V.V. Dogovorne pravo. Kniga pervaia: Obshchie polozheniya [Mikhail I. Braginsky & Vasily V. Vitryansky, Contract Law. Book One: General Provisions]] 359 (Statut 1998).

⁸⁰ See *supra* n. 36.

by various consequences determined by the court. These can include the payment of damages or the return to the other party of that which had been performed under the contract. In other words, some part of the obligations or even new obligations can bind the parties even after termination of the contract by the court.

The case law cited above gave the necessary guidelines to the German legislator, who in 2002 introduced a new provision into the BGB, *i.e.* § 313. This provision allows the judicial adaptation of a contract if the underlying circumstances (basis of a contract) have significantly changed, so that the parties would not have entered into the contract or would have entered into it on different terms, had they foreseen this change.⁸¹ Paragraph 313 embodies a rich tradition of German case law with its well-thought application of the *Störung der Geschäftsgrundlage* doctrine, requirements of unforeseeability and contract-saving bias.

On the face of it, the German approach to unforeseen change of circumstances seems to be similar to the Russian one. Both of them require a sufficient degree of change, which shall not be foreseeable at the time of conclusion of the contract. However, the example of inflation and currency fluctuations shows that, in practice, the application of analogous categories of foreseeability, imputation of risk, exceptionalism may yield different results. Russian courts have demonstrated obstinate reluctance to intervene in contractual relations, both in the aftermath of the default of 1998 and afterwards, whereas the German judiciary showed readiness to restore contractual equilibrium. Apart from the historical considerations described above, this could be partially explained by cultural traits. High scores for masculinity (66) and individualism (67) under the Hofstede's model predetermined a strong belief of the German society in the ideal of self-actualization and appreciation of achievement and success. This is, to a certain degree, counterbalanced by the high score in uncertainty avoidance (65), which on the fertile German soil with the philosophical heritage of Kant, Hegel and Fichte entailed a strong preference for deductive thinking. As a result, we can witness a well-developed and elaborate law system, designed to cover a broad spectrum of situations and protect against possible abuses. Details create legal certainty, and this may explain why German judges and society as a whole were ready to accept and apply the *Störung der Geschäftsgrundlage* doctrine.

Despite the fact that it was exactly the inflation and devaluation of the national currency which gave rise to the doctrine of hardship in Germany, we believe it is rather improbable that German courts would be willing to amend contracts in cases of 'normal' or even 'above-average' currency fluctuations. It is important to

⁸¹ Cf. Art. 6:258(1) of the Dutch Civil Code (1992): 'Upon the demand of one of the parties, the court may modify the effects of a contract or it may set it aside, in whole or in part, on the basis of unforeseen circumstances of such a nature that the other party, according to standards of reasonableness and fairness, may not expect the contract to be maintained in unmodified form. The modification or setting aside may be given retroactive effect.'

understand that the overwhelming inflation and currency depreciation which struck Germany after the World War I were unprecedented. The radical turn made by *Reichsgericht* at the beginning of the 1920^s was dictated by the urgent need of saving the national economy and preventing gross injustice. As stated above, currency fluctuations have become a part of the modern economic set-up and no party is protected against them. Nevertheless, the German approach will certainly fall into the category of 'open' regimes according to the criteria proposed by Hondius & Grigoleit.⁸² Germany has a developed and tested doctrine specifically designed to address the issue of unexpected circumstances (Art. 313 BGB). In this respect, it stands along with Russia. However, in practical terms, the German system seems to be more 'open' than the Russian one.

4. French Law Approach: Contradiction and Individualism

4.1. Force majeure and Impossibility

The concept of *force majeure* in French law could be found in Art. 1148 of the *Code civil*⁸³ [hereinafter CC] which states that '[t]here is no occasion for any damages where a debtor was prevented from transferring or from doing that to which he was bound ... by reason of *force majeure* or of fortuitous event (*cas fortuit*)'.⁸⁴

Just like German law, French law following a Roman tradition, in principle accepts the fault-based liability regime. This type of liability is generally applicable to the so-called obligations of means (*obligations de moyens*), whereas the debtor undertakes to 'use all reasonable means to obtain the result, [so that] he is not bound to the result itself'.⁸⁵ This type of obligation could be derived from Art. 1137 CC. At the same time, the rule of strict liability could be inferred from Art. 1147 therein, which provides that '[t]he debtor is required ... to pay damages, whether for non-performance of the obligation or for the delay in its performance ... even though there is no bad faith on his part' (emphasis added). This article refers to the so-called obligations of result (*obligations de résultat*), which entail an obligation to reach a particular result, e.g. deliver a thing or complete works.⁸⁶

⁸² Ewoud Hondius & Hans C. Grigoleit, General Comparative Remarks: Converging Tendencies, Remaining Differences and the Unsolved Mystery of Adjustment, in Unexpected Circumstances in European Contract Law, *supra* n. 23, at 643, 643.

⁸³ The English translation of the Code Civil is available at <http://www.legifrance.gouv.fr/content/download/1950/13681/.../Code_22.pdf> (accessed Jul. 26, 2015).

⁸⁴ The terms 'force majeure' and 'cas fortuit' are used as synonyms.

⁸⁵ Pauline Rémy-Corlay, *Structural Elements of the French Civil Code*, in The Architecture of European Codes and Contract Law 33, 50 (Stefan Grundmann & Martin Schauer, eds.) (Kluwer Law International 2006).

⁸⁶ Philippe Malaurie et al., *Les obligations* 499 (5th ed., Defrénois 2011); François Terré et al., *Les obligations* 582 (10th ed., Dalloz 2009).

For the purposes of this article, we do not need to conduct an in-depth analysis of the niceties in the distinction between obligations of means and result, as these two would mostly affect the allocation of the burden of proof.⁸⁷ As we have shown with reference to the Russian (no-fault liability in B2B relations) and German (fault-based liability) legal systems, practical distinctions between fault and no-fault types of liability may be overstated. In both scenarios, in *force majeure* cases the debtor is excused from performing the primary obligation (specific performance), which becomes logically impossible, as well as the secondary obligation (payment of damages). In both scenarios, it is the debtor who has to prove the existence of an exception or the non-existence of fault. The only difference is that in fault-based systems, the court will assess the fault of the debtor (which is apparently missing in cases of *force majeure*), whereas in a strict liability regime, the court will analyse whether one of the exemptions to the strict liability of the debtor applies. We agree that, in effect, the 'French system appears to be almost identical to the concept of strict liability, where the debtor is only freed from liability in damages if the non-performance is excused.'⁸⁸ This is even more so for situations of non-performance due to imposed trade restrictions, as such situations would usually fall under the 'obligations of result' heading.

The regulation of consequences of *force majeure* under French law is similar to the Russian and German one, namely, contractual obligations remain in effect, while claims for specific performance and damages are precluded. This result is driven by the principle of protection of contract, which as we will see later on, has been deeply incorporated into French contract law. In case of the debtor's non-performance, the creditor acquires the right to apply to the court to have the contract terminated – he cannot, as a general rule, unilaterally terminate the contract extra-judicially (Art. 1184 CC),⁸⁹ unless otherwise agreed by the parties. This is different from Russian law, which warrants such a termination in case of material breach (Art. 450 RCC) and German law, under which, as a general rule, a creditor may unilaterally terminate a contract if the debtor fails to perform it within a notice period set by the creditor – *Nachfrist* (§ 323(1) BGB).⁹⁰ We believe that the application to the court may be welcome, and

⁸⁷ The lack of due care in *obligations de moyens* has to be proved by the creditor. Whereas it is the debtor in *obligations de résultat*, who has to adduce evidence of a legitimate excuse for non-performance; the creditor must only prove that the required result was not achieved.

⁸⁸ Brunner, *supra* n. 56, at 67.

⁸⁹ In several decisions, though, the *Cour de cassation* (Court of Cassation) stated that '[t]he seriousness of a contracting party's behavior may justify the unilateral termination of the agreement by other party.' See Yves-Marie Laithier, *Comparative Reflections on the French Law of Remedies for Breach of Contract*, in Comparative Remedies for Breach of Contract 103, 119 (Nili Cohen & Ewan McKendrick, eds.) (Hart Pub. 2005); see also Malaurie et al., *supra* n. 86, at 469.

⁹⁰ Notably, in case of impossibility (§ 275(1)–(3) BGB), German law (§ 326(5) BGB) releases the creditor of the need to specify an additional time (*Nachfrist*) for performance under the contract.

the French approach is thus preferable in cases of temporal impossibility, where termination of the contract may be unwarranted.⁹¹

As we pointed out above, the impossibility to perform due to *force majeure* does not in itself lead to the termination of a contract; it exempts the debtor from liability for non-performance. Since French law takes the position that an obligation to do the impossible is void (*impossibilium nulla obligatio*), initial impossibility shall render the contract void, with restitution and other ensuing consequences. According to McKendrick, the same should hold true for subsequent impossibility when the breached obligation or obligations 'are essential to the debtor's performance as a whole'.⁹² We do not adhere to this view and believe that nullity of the contract does not automatically follow from a subsequent impossibility. This also seems to be the approach adopted by the French legal doctrine: 'La stabilité des contrats a été pour notre jurisprudence le principe essentiel' ('The stability of contractual relations is a cornerstone of our case law').⁹³

In determining the grounds and consequences of impossibility, the French judiciary exercises a certain degree of flexibility. This discretion is however more limited than the one found in German law which, driven by the considerations of good faith, takes a nuanced approach. When deciding on the fate of the contract, French courts will usually take into account the practical consequences of *force majeure* (partial *versus* total non-performance) and the temporary nature of a supervening event (temporal *versus* permanent impossibility). In cases where the awarding of damages might be precluded by operation of Art. 1148 CC and termination could be a step too far, courts may reduce or vary the creditor's obligations in order to balance the reduced obligation of the debtor. For instance, in one case decided in 1943 a claimant rented advertising space on an illuminated pillar at a railway station. However, in 1939, due to the war, the pillar lighting had to be switched off during the night. The court accepted that this was a *force majeure* event which made contractual performance partially impossible. As a result, the court lowered the rent by 20%.⁹⁴

The flexibility of the French approach makes it rather similar to positions adopted by the Russian and German legal systems when it comes to the termination of

⁹¹ Under French law, a party is not released from its contractual obligations and the contract is not terminated, when the impossibility is temporal in nature. In general, temporary impossibility warrants suspension of performance, until the impossibility ceases. See: John Bell et al., *Principles of French Law* 348 (2nd ed., Oxford University Press 2008); Malaurie et al., *supra* n. 86, at 514. In each particular case in order to determine whether termination is justified, a court will analyze the seriousness the debtor's non-performance. As a result, the court may order the suspension of the obligation, reduction in price (or other intermediate solution) or termination.

⁹² Barry Nicholas, *Force Majeure in French Law*, in *Force Majeure and Frustration of Contract* 21, 26 (Ewan McKendrick, ed.) (2nd ed., Informa Law from Routledge 2013).

⁹³ Terré et al., *supra* n. 86, at 588.

⁹⁴ Nicholas, *supra* n. 92, at 27.

a contract due to *force majeure*. Although at a closer look, the legal reasoning may differ. In Russia, discussion will most probably relate to the issue of materiality, *i.e.* whether the breach of a contract effectively deprives the other party of what it could reasonably have expected when entering into the contract (Art. 450(2) RCC). German and French courts will look at the parties' legitimate interests, considering, *inter alia*, whether impossibility is temporary or permanent, total or partial. They consider the issue of *force majeure* to be a high-wire balancing act. When impossibility due to *force majeure* is total and permanent, it is almost certain that a French court would license termination of the contract.

To prove the existence of *force majeure* under French law, the debtor has to show that contractual performance has become impossible, physically or legally, and not just more onerous. However, French courts might be willing to give a rather broad interpretation to *force majeure* and apply it in cases of frustration of purpose.⁹⁵ Apart from the impossibility of performing, a *force majeure* defence requires such elements as: (i) the irresistibility of an event; (ii) its unforeseeability; and (iii) the external character.⁹⁶

Irresistibility highlights an unavoidable and insurmountable character of *force majeure*. As Le Tourneau described it, 'if the event was insurmountable, it can be imputed to no one. This is the application of common sense: no one can be obliged to perform what is impossible.'⁹⁷ Irresistibility is closely linked with another element, namely the external nature of the event, which shall not be attributed to the parties or their agents. Imposition of trade restrictions would likely satisfy these criteria, as commercial parties cannot affect state policy, at least not directly.

If a party foresaw or should have foreseen an event preventing performance, it is assumed that such a party should have prepared itself for all the related negative consequences. The awareness should result in the terms of a contract, through, *e.g.*, price adjustment mechanisms. Failure to do so falls under the commercial risk title. As we saw from the previous analysis, the notion of foreseeability is the most problematic one. Unfortunately, there is not much more clarity under the French system when

⁹⁵ The case *Dispot Merlin v. Robillard* (Comm. Rouen, August 28, 1843, upheld on appeal Rouen, February 9, 1844, D. 1845, 4) is a good example of that. The case concerned a contract regulating an express service by road between Rouen and Paris. A couple of years after the conclusion of the contract, a railway connection was established between the above cities and the contract lost its original purpose. The judge in this case allowed the contract to be terminated by applying the doctrine of *force majeure*. See Denis Philippe, *France and Belgium*, in Foreseen and Unforeseen Circumstances (= 27 BW-krant jaarboek) 156, 163 (Alex G. Castermans et al., eds.) (Kluwer 2012), available at <<http://www.philippelaw.eu/UploadDirectory/UserFiles/files/France%20and%20Belgium.pdf>> (accessed Jul. 25, 2015).

⁹⁶ Malaurie et al., *supra* n. 86, at 509; Terré et al., *supra* n. 86, at 585.

⁹⁷ Philippe le Tourneau, *La responsabilité civile* 239 (3rd ed., Dalloz 1982) (quoted in David R. Rivkin, *Lex Mercatoria and Force Majeure*, in *Transnational Rules in International Commercial Arbitration* (= ICC Publication No. 480/4) 161, 176 (Emmanuel Gaillard, ed.) (ICC Pub. 1993), available at <<http://www.trans-lex.org/116100>> (accessed Jul. 26, 2015).

it comes to this indispensable element of *force majeure*. Despite the prevailing view that the requirement of foreseeability shall be scrutinized objectively, there is a trend (at least in academic circles) to take into account an element of relativity. Thus, it is argued, the 'courts must . . . base themselves on the average man and a standard of *bon père de famille*, as adapted to the defendant's activities and to their level of specialization'.⁹⁸ Therefore, reasonable foreseeability may be overtaken by the specific foreseeability, enhanced in view of a party's experience and specialization. It is more likely, that the subjectivity will play a role only when a party's qualifications are above the average standard, not below it, at least in B2B transactions.

In practice, it might be immaterial which type of standard is applied. A lot more will depend on the way the courts define an 'average' or 'reasonable' man. Should the foreseeability be absolute (so as 'to escape the bounds of all human foresight'⁹⁹), or is it enough for it to be relative (normally foreseeable)? For instance, in the decision of April 9, 1962, the French *Conseil d'État* (Council of State) found that since a previous flood had occurred 69 years before the one at issue, the flood was foreseeable.¹⁰⁰ In another case, the court refused to consider an avalanche which struck Val-d'Isère in 1970 a *force majeure* event, due to the fact that another one was recorded around 50 years before.¹⁰¹ In the famous case concerning the robbery of a hotel,¹⁰² the court emphasized that unpredictability was a relative concept. The court found that an armed robbery was not unpredictable for a luxurious Saint-Tropez hotel full of wealthy clients, even though it had never had any experience of being robbed. These examples show that the standard of an 'average man' in the eyes of the French judiciary is extremely high, making such a man almost a prophet, who knows the past and sees the future. The rigidity of the French stance makes it more like a Russian approach than a German one. It seems that the mere possibility of a future event (e.g., an embargo) derived from the past occurrences, however remote and inconsiderable in number, might imply foreseeability. As the arbitral tribunal in one of the cases suggested, if a party 'has or must have the *slightest* doubt about his ability to perform at the given time, he must make all necessary verifications before promising performance'¹⁰³ (emphasis added).

⁹⁸ Geneviève Viney, 5 *Traité de droit civil. Les obligations. La responsabilité* 398 (Jacques Ghestin, ed.) (Librairie générale de droit et de jurisprudence 1988) (quoted in Rivkin, *supra* n. 97, at 176–77).

⁹⁹ Bell et al., *supra* n. 91, at 344.

¹⁰⁰ Conseil d'État, 4 avril 1962, *Ministre des Travaux publics c/ Société des Chais d'Armagnac*, A.J.D.A. 1962, II, 592, concl. G. Braibant.

¹⁰¹ Trib. adm. Grenoble, 19 juin 1974, *Dame Bosvy et autres c/ Ministre de l'Equipement et Commune de Val d'Isère*, A.J.D.A. 1975, 194, note F. Servoin, J.C.P. 1975, II, 17956, note Moderne.

¹⁰² Cass. 1^e civ., 9 mars 1994, 1994 Bull. civ. I, No. 91, 70, at <<http://www.legifrance.gouv.fr/affichJuriJudi.do?idTexte=JURITEXT000007031881>> (accessed Jul. 26, 2015).

¹⁰³ ICC Case No. 12112, 34 Y.B. Comm. Arb. 77 (2009).

As we have pointed out above, when dealing with the Russian approach, such strictness is morally unfounded and economically unjustified. It is wrong to punish someone for not doing the impossible, provided that a party could not have reasonably predicted a supervening event and acted in good faith. It also imposes a heavy burden on all parties in commercial transactions to negotiate and redistribute risks, whether probable or not, otherwise facing the negative consequences in the form of liability. This state of affairs may contravene the purpose of contract law, if we view it as a method of maximizing economic efficiency. It is true that each case is unique and there could be valid arguments to impute the blame on a non-performing party, e.g., when the party is a superior risk bearer. Such is, for instance, a situation whenever the subjective factors (professional knowledge or particular awareness) indicate the subjective foreseeability of the event in question. In the words of Guenter Treitel, '[t]he making of a contract in the face of an imminent prohibition and in the belief that performance will be affected by the prohibition comes very close to entering into the contract after the prohibition has already taken effect.'¹⁰⁴ As it follows, trade prohibitions should be imminent, and not merely hypothetical.

4.2. Doctrine of *imprévision*: Dual Approach

The sternness of the French legal system is especially evident from the treatment of unforeseen change of circumstances, whenever private contracts are concerned. Under French law there is a fine line drawn between physical or legal impossibility to perform (*force majeure*) and situations where performance is technically possible, but extremely difficult or onerous (*imprévision*). It is well known, and remains so up to this date, that the traditional French doctrine rejects the application of *imprévision* to private matters. Article 1134 CC states that the '[a]greements lawfully entered into take the place of the law for those who have made them.' It is appealing to compare private agreements with laws binding the parties, as both create certainty and are supportive of the idea of economic freedom. Thus, the judge amending the contract is considered to be 'a source of instability and arbitrariness, particularly if it is related to an economic evaluation of the counter-obligations or contractual equilibrium.'¹⁰⁵ Mirroring this image, French courts persistently refused to amend contracts whose performance was affected by extraordinary inflation or depreciation in the value of national currency.¹⁰⁶

The unwillingness of the French system to adopt the doctrine of *imprévision* could be explained by its historical and political background. The abuses of the *ancien*

¹⁰⁴ Guenter H. Treitel, *Frustration and Force Majeure* 508 (2nd ed., Thomson; Sweet & Maxwell 2004).

¹⁰⁵ Rodrigo M. Uribe, *The Effect of a Change of Circumstances on the Binding Force of Contracts: Comparative Perspectives* (= 94 Ius Commune Europaeum) 45 (Intersentia 2011), available at <<http://dspace.library.uu.nl/handle/1874/204792>> (accessed Jul. 26, 2015).

¹⁰⁶ Depreciation of the pound in the thirties, depreciation of the ruble after 1971 (reported in *Unexpected Circumstances in European Contract Law*, *supra* n. 23, at 249).

régime and distrust of the courts have contributed to the vision of the revolutionaries that limited the courts' role in the enforcement of statutes. Even the original function of the French *Tribunal de cassation* (now *Cour de cassation*) was to assist the legislature rather than to act as a court: '[I]ts task was to see that the courts did not deviate from the text of the laws and so encroach on the powers of the legislature.'¹⁰⁷ Besides, in the aftermath of the paper money (*assignats*) crisis at the time of the French Revolution, the CC introduced the principle of monetary nominalism in relation to loans. As is evident from the wording of Art. 1895 CC, French law of obligations operates with the category of nominal value, and not the real value, which takes into account depreciation and purchasing power. The principle of monetary nominalism is now considered to be applicable to all monetary claims.¹⁰⁸

In addition, the readiness of the legislative branch to give a helping hand to those suffering injustice due to exceptional circumstances, has made a judicial response less needful.¹⁰⁹ As German courts were taking up an active corrective role after the outbreak of the World Wars, the French legislature provided for the termination of contracts if their performance were to cause hardship or loss greatly in excess of what could reasonably be expected at the time of the contract.¹¹⁰ During the time of war and post-war inflation, at least 9 statutes were passed 'ameliorating the position of contracting parties severely affected by inflation'.¹¹¹ It could be argued that the difference between the French and German approaches has its origins in the economic sphere, namely in the fact that the French economy has never seen such a dramatic and steep increase in inflation and currency depreciation as did the German economy. This of course is a valid argument. However, we believe that the divergence is primarily driven by unique French attitudes, political (strict adherence to the ideas of separation of powers), historical (vigilance towards the judicial authority) and cultural.

According to the Hofstede's index, France scores fairly high in power distance (68) and individualism (71). This explains that, on the one hand, one is only supposed to take care of oneself and one's family; but on the other hand, people are still dependent on the central government, an impersonal power centre. Therefore,

¹⁰⁷ James Gordley & Arthur T. von Mehren, *An Introduction to the Comparative Study of Private Law: Readings, Cases, Materials* 99 (Cambridge University Press 2009).

¹⁰⁸ Hugh Beale et al., *Cases, Materials and Text on Contract Law* 1158 (2nd ed., Hart Pub. 2010).

¹⁰⁹ It is possible to argue that inefficiency of the judiciary's response was the cause of the legislator's response. However, as pointed out by Posner & Rosenfield, 'there is no presumption that legislator seeks to enhance efficiency' (Posner & Rosenfield, *supra* n. 11, at 101).

¹¹⁰ See, e.g., Loi du 21 janvier 1918 dite failliot relative aux marchés commerciaux conclus avant la 1^{re} guerre mondiale (Loi Failliot) (J.O., January 23, 1918, p. 837), which allowed termination of contracts concluded before August 1, 1918, if performance under such contracts became excessively onerous for one of the parties.

¹¹¹ Shirley Renner, *Inflation and the Enforcement of Contracts* 15 (Edward Elgar Pub. 1999).

under normal circumstances people shall take care of themselves, acting in self-interested individualistic manner. They shall be responsible for future events, even if those are unforeseen. However, when the crisis strikes, the French might be expecting the central authority to intervene, as happened many times before, during and after the World Wars. Just like Russia with the score of 95, France ranks high in uncertainty avoidance (86). Therefore, stability and a strong desire for laws, rules and regulations to structure life are highly valued in French society. This may seem to be in contradiction with the general negative attitude of the judiciary to establishing boundaries in cases where the performance of a contract is no longer viable or just. However, at a closer look, a strict rule of non-intervention by courts in the universe of privately agreed terms is the zenith of predictability and legal certainty, so cherished by the French people.

Since the landmark decision in *Canal de Craponne*,¹¹² the *Cour de cassation* has been steadfast in refusing the adaptation of contracts due to significant change of circumstances, including the steep rise of prices and currency devaluation. Even the World Wars were not able to change this. For instance, in one of the cases the court dealt with a stock-rearing contract, entered into in 1910.¹¹³ Under this contract, the farmer was required to return to the proprietor the herd of equal value, that value being fixed in the contract. As a result of the post-war monetary depreciation, the real value of the herd increased when compared to the fixed contractual amount. The attempt by the proprietor to attain a proportion of the added value was abruptly cut off by the *Cour de cassation*, which held that no equitable consideration allows courts to amend contract. The arguments, based on Arts. 1134 and 1135 CC, which provide that contracts have to be performed in good faith and in accordance with equity, were rejected as referring to the interpretation of contracts and a duty of loyalty in the execution of contracts, rather than to their readjustment by the judiciary. In a more recent case, the *Cour de cassation* clearly stated that even when the rule of Art. 1134 allows the judge to sanction abuse of contractual rights, the provision does not grant him the right to 'alter the substance of the terms validly agreed upon by the parties'.¹¹⁴

¹¹² The decision dates back to 1876 and concerns a dispute between the owners of the canal built in the 16th century and the farmers who were the beneficiaries of the agreement, which allowed them to use water from the canal for irrigation purposes. By the 19th century the fixed fee paid by the farmers has become inadequate, with management costs exceeding such an amount. Despite this fact, the *Cour de Cassation* refused to revise the contract price, arguing that 'it was not open to the courts, however equitable their decision might like to be, to take into consideration the lapse of time and circumstances in order to modify an agreement, thereby substituting new terms for those which had been freely agreed upon by the parties' (quoted in Eva Steiner, *French Law: A Comparative Approach* 335 (Oxford University Press 2010)).

¹¹³ Cass. civ., 6 juin 1921, D. 1921, I, 73, S. 1921, I, 193. The case is discussed in Beale et al., *supra* n. 108, at 1132–33.

¹¹⁴ Uribe, *supra* n. 105, at 45 (describing the case Cass. com., 10 juillet 2007, R.D.C. 2007, 1107, note D. Mazeaud).

Interestingly, the approach of the French judiciary to unforeseen change of circumstances has never been unified. In the 1920^s, in order to alleviate the hardships caused by inflation, the lower courts began manipulating the remedy of damages, since it would usually be outside the scope of the revision by the *Cour de cassation*. They considered that '[w]here a change in the value of goods or services could be attributed to a change in the value of money, a buyer was supposed not to have suffered substantial damage.'¹¹⁵ The unease with which French courts were applying an unqualified one-size-fits-all vision is also evident from the numerous judgments allowing for contract revision and later reversed by the *Cour de cassation*.

As opposed to the area of private law and jurisprudence of the *Cour de cassation*, the *Conseil d'État*, the highest administrative court, embraced the doctrine of *imprévision* as early as in the 1910^s.¹¹⁶ In the famous *Gaz de Bourdeaux* case, the *Conseil d'État* allowed the renegotiation of the contract for the gas and electricity supply, entered into between a private contractor and the city of Bourdeaux. The court considered the fact that, due to an unexpected rise in coal prices during the war time, contractual performance under the original conditions would be disastrous for the supplier. In reaching its decision, the *Conseil d'État* was guided by the general interest of the public, which required the continuation of the company services.¹¹⁷ To address the injustice arising out of an unexpected change of circumstances, a judge would invite the parties to renegotiate the agreement. Failure to do so might result in a compensation (*indemnité d'imprévision*), awarded for the purpose of restoring the economic equilibrium. Thus, a contract itself remains unaltered and in force, unless the economic imbalance becomes permanent, in which case it can be terminated on the ground of *force majeure*.

For the purposes of this article we are not going to discuss the legal nature of *indemnité d'imprévision* or the limited scope of its application by the administrative courts. Instead, we would agree with those scholars who believe that the divergent approach of French administrative and private law has no compelling reasoning.¹¹⁸ Some authors believe that *imprévision* is characteristically an administrative law doctrine, which cannot be understood in the light of private law theories.¹¹⁹ This is

¹¹⁵ Janwillem Oosterhuis, *Unexpected Circumstances Arising from World War I and Its Aftermath: 'Open' versus 'Closed' Legal Systems*, 7(2) Erasmus L. Rev. 73 (2014), available at <http://www.elevenjournals.com/tijdschrift/ELR/2014/2/ELR_2210-2671_2014_007_002_003.pdf> (accessed Jul. 26, 2015). doi:10.5553/ELR.000018

¹¹⁶ French law is to a certain extent exceptional for having two distinct legal systems, one of private and one of public law.

¹¹⁷ Conseil d'État, 30 mars 1916, *Compagnie générale d'éclairage de Bordeaux c/ Ville de Bordeaux*, D. 1916, III, 25, concl. Chardenet.

¹¹⁸ See, e.g.: Uribe, *supra* n. 105, at 52; Beale et al., *supra* n. 108, at 1130.

¹¹⁹ René David & Henry P. de Vries, *The French Legal System* 65 (Oceana Pub. 1958).

mainly explained by the nature and importance of public services, and the possible consequences of a failure to perform such services. However, in today's interdependent world, the private sector has no less effect on the economic stability and societal well-being, than the public one. A good example of that was given by the recent economic crises, which have shown, as clearly as they could, that the public and private interests are mixed and that the failure of the private 'too-big-to-fail' companies could have a significant economic impact, affecting a large number of people.

The artificial character of a private-public distinction, when it comes to contractual relations and unforeseen change of circumstances, and the need to embrace the doctrine of *imprévision* in private matters have led to various initiatives aimed at modernizing the French law of obligations. The most famous of the reform projects are the *Avant-projet Catala*, prepared by the group of scholars under the chairmanship of Professor Pierre Catala and presented to the French Ministry of Justice in 2005 and the *Projet Terré*, prepared by the working group led by Professor François Terré and published in 2009.

The most recent *Projet d'Ordonnance* related to the reform of French civil law was published by the Ministry of Justice on February 25, 2015.¹²⁰ Article 1196 of the *Projet* effectively introduces the notion of hardship / *imprévision* into French private law. It provides that in case the unforeseen change of circumstances has made the execution of a contract excessively onerous for a party which did not assume such a risk, the party can ask for a contract renegotiation. If the other party refuses to conduct negotiations or if negotiations fail, parties can jointly ask a judge to adapt the contract. If this does not work, one party may ask the judge to terminate the contract, on the date and conditions determined by him. Thus, as we see from the text of the article, a judge does not have the power to adapt the contract, unless both parties agree on that, which is hardly possible, taking into account the conflicting nature of their relations. This limited role given to the court is in line with the traditional caution of French society towards the judiciary, as noted above. Nevertheless, the power to terminate a contract 'at a date and on terms to be fixed' might, in theory, compensate for the lack of revision competence.

We agree with Alain Ghozi that contracts are by their nature judicial acts looking into the future and therefore, they shall themselves provide for answers to the difficulties arising in the future.¹²¹ In any case, mutually agreed compromises are always preferable to court-imposed solutions. French courts seem to have embraced

¹²⁰ Ministère de la justice, *Projet d'Ordonnance n° du portant réforme du droit des contrats, du régime général et de la preuve des obligations*, <http://www.justice.gouv.fr/publication/j21_projet_ord_reforme_contrats_2015.pdf> (accessed Jul. 26, 2015).

¹²¹ Alain Ghozi, *The Effects of Contracts; Contractual Interpretation and Contractual Classification (articles 1134 to 1143)*, in Reforming the French Law of Obligations. Comparative Reflections on the Avant-projet de réforme du droit obligations et de la prescription ('the Avant-projet Catala') 543, 547 (John Cartwright et al., eds.) (Hart Pub. 2009).

this vision like no other court. In comparison to the legal systems referred to above, the French approach to *force majeure* and unforeseen change of circumstances is the most rigorous one. Up to this date, the *Cour de cassation* has been persistent in refusing contract adaptation due to supervening events, making contractual performance excessively burdensome or even ruinous to one of the parties. It is very unlikely that steep inflation or currency fluctuations will ever be regarded as a reason for the revision or termination of a contract. They were not considered a good enough reason during, and in the aftermath of, the World Wars, accordingly they will not be accepted as such in times of peace. The same negative attitude to court intervention holds true for issues of *force majeure*, which under French law sets a high bar for the foreseeability requirement. It seems that any intrusion by the courts into the sanctity of private relations is viewed as a source of insecurity and economic instability. As opposed to the regimes found in Russian and German law, the French legal system is manifestly a 'closed' one.

5. Conclusion

The purpose of law is always two-fold. On the one hand, it stimulates economic growth, insures stable societal development and the protection of human rights. On the other, it is often reactive to all sorts of instability. It so happens that modern times have been characterized by rising tensions, both political and economic. In such a situation, the role of legal norms and the judiciary obtains increased importance.

In the pages above, we have analysed how the legal systems of Russia, Germany and France have reacted to cases of trade restrictions and currency depreciation, when contractual performance becomes impossible (*force majeure*) or extremely burdensome (change of circumstances). To make the comparison more relatable, we referred to the recent events, including the trade restrictions imposed by the Russian Federation on certain food products coming from the USA, the EU, Japan, and some other countries. The imposition of the embargo coincided with the devaluation of the rouble, caused by various macroeconomic reasons. Whereas the former might have become an obstacle to international trade as delivery of various goods became illegal, the latter affected contracts concluded in foreign currency, making performance under such contracts more onerous, at least for one of the parties involved.

Our analysis has been necessarily broad. In order to give a better vision of the current state of affairs related to impossibility and impracticability, we reviewed historical and cultural backgrounds, and briefly touched upon the economic considerations. Ironically, despite the fact that the concepts discussed have been known in Russia, Germany and France for a reasonably long time, there still seems to be confusion among practicing lawyers when it comes to their application in

practice. The reason for that might naturally lie in the nature of *force majeure* and unforeseen change of circumstances. They both affect contractual equilibrium and distort a normal or foreseeable course of contract execution. Another explanation may stem from the poorly drafted legal provisions or contradictory case law. In this respect, we hope that our article sheds some light on the existing regulations of these distinct, but closely connected notions.

When it comes to *force majeure*, all three legal systems recognize that a party should not bear responsibility for non-performance, if performance became impossible (physically or legally) due to unforeseeable, insurmountable and external events. Despite the perceived similarity, practical application of force majeure may vary depending on the judicial interpretation of the terms 'foreseeability' and 'unavoidability'. This would be determined by historical, cultural and political considerations. Some scholars have divided all legal systems into two categories, the so called 'open' and 'closed' regimes.¹²² The former are characterized by the existence of a general doctrine addressing unexpected circumstances and the mechanism of contract adjustment as a remedy, while the latter lacks one of the two. This distinction is purely doctrinal and in practice 'open' systems might turn out to be rather 'closed'. We believe that the same division holds true for the application of the impossibility defence, at least when we consider Russian, German and French approaches to *force majeure*. Courts in Russia and France have set a rather high bar for the requirement of unforeseeability, so whenever a similar event happened in the past, it can be argued that all future incidents would in fact be foreseeable. Foreseeability also plays a central role in the treatment of an unforeseen change of circumstances.

Another important aspect of *force majeure* is the effect it has on the fate of the contract. Turning back to economic and moral considerations, we argue that impossibility shall not automatically lead to the termination of a contract and contractual obligations. In this respect, both French and German approaches support this view. The RCC (Arts. 416 and 417) does not provide a clear answer to the question whether temporal or partial impossibility terminates contractual relations. Moreover, recent amendments to Art. 417 have created additional complications, as contractual obligations terminated due to the adoption of a state act may well be restored when such an act is held void or is repealed later on. In our view, it is only when impossibility is permanent and total that the automatic termination may be justified. Temporal and partial impossibility, as is usually the case with trade restrictions, shall not lead to such grave consequences. Late performance causes default, not impossibility. In some situations, however, temporal impossibility can reasonably be equated to permanent, and partial impossibility – to total, of course not in a strict sense, but rather in the result achieved. This shall be determined from the position of the creditor, taking into account all relevant factors, such as urgency of performance,

¹²² Unexpected Circumstances in European Contract Law, *supra* n. 23.

potential losses for the creditor, etc. In our view a case-by-case approach to the issue of termination of contractual obligations is well justified.

We agree that, at least in business relations, it is the role of the parties to contractually allocate risks related to future events capable of changing the balance of loss and profit in line with the economics of the transaction. After all, the parties are usually in a better position to assess the probability that the risk will materialize and the magnitude of the loss thereof, which Richard Posner referred to as risk-appraisal costs.¹²³ However, it is not always possible for the parties to predict all future events, especially in case of long-term contracts. Inability to foresee the future is exacerbated by the lack of access to all the relevant information and the optimistic bias inherent in human behaviour.¹²⁴

Obligations have moral and economic parameters. In some situations, contractual adjustment could be economically justified, as the need to negotiate specific provisions dealing with such consequences might substantially increase transaction costs, when taken at the global or nationwide scale. There is also no empirical evidence to suggest that a narrowly construed judicial intervention in situations of drastic currency fluctuations or trade restrictions can destabilize the economy or undermine the stability of contracts. Besides, considerations of justice, fairness, good faith, public interest and others may require interference by the court. This is what happened in Germany in the 1920^s and 1930^s, when the country was suffering from extreme inflation and the national currency was heavily depreciated. German courts reacted by revising contracts and adjusting rental payments and purchase prices. To the contrary, neither Russian nor French judiciary was ready to interfere in contractual relations, when faced with steep currency fluctuations. These divergent approaches cannot be explained by reference to the liability regimes (*fault versus no-fault liability*), as one might expect. Instead, we believe that the main reasons are rather historical and cultural, as shown by Hofstede's cultural dimensions theory that we used in our analyses.

It took the unprecedented shocks of the World War I to make the German approach more lenient and willing to accept the hardship defence. It is also true that deductive thinking, deeply rooted in the German tradition, might have contributed to the willingness of the judiciary to interfere, without being afraid of creating imbalance and causing legal uncertainty. Russia and France have not encountered such unrivalled circumstances. Even if they had done, it is rather improbable that their approach would have dramatically changed. This is so because of political and cultural peculiarities. First, unlike *force majeure*, which always targets a limited number of contractual relations, acceptance of hardship to currency depreciation

¹²³ Posner & Rosenfield, *supra* n. 11, at 91.

¹²⁴ For more on cognitive biases, see Behavioral Law and Economics (Cass R. Sunstein, ed.) (Cambridge University Press 2000).

would likely have a broader, countrywide effect. The judiciary in France and Russia were simply not prepared to make this far-reaching and to a certain extent, political move, unlike in Germany. Second, due to historical reasons, French courts were considered to be a source of instability. This is not necessarily so nowadays. But the negative attitude to uncertainty, inherent in French and Russian culture still makes a reserved approach of their courts rather logical. After all, what can be more predictable and certain than the lack of any intervention whatsoever?

In any event, legal regimes of *force majeure* and unforeseen change of circumstances operate very restrictively in all jurisdictions studied. This is the result of the high value and importance attributed to the ancient doctrine of *pacta sunt servanda*. Therefore, whichever law is applicable to a particular transaction in question, especially for international contracts, it might be advisable to provide for specific contractual mechanisms addressing issues of liability and release therefrom, should performance become impossible, economically impractical or unfairly imbalanced. Such mechanisms could include renegotiation, hardship, indexation, *force majeure* and other clauses. Otherwise parties risk suffering harsh consequences, even in the absence of their fault.

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Information about the authors

Ilya Kokorin (St. Petersburg, Russia) – Attorney-at-Law, Partner at *Buzko Kokorin* Law Firm, LL.M. (Central European University, Leiden Law School) (9/2 Pulkovskaya str., St. Petersburg, 196158, Russia; e-mail: ilya.kokorin@buzkokokorin.com).

Jeroen van der Weide (Leiden, The Netherlands) – Associate Professor of Private Law at Institute for Private Law, Leiden Law School (Kamerlingh Onnes Gebouw, Steenschuur 25, Office No. C207, Leiden, 2311 ES, The Netherlands; e-mail: j.a.van.der.weide@law.leidenuniv.nl).