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Principles for International Contracts
Chapter 5 (Contents) and 6 (Performance)
Comments

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UNIDROIT

INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

PRINCIPLES FOR INTERNATIONAL COMMERCIAL CONTRACTS

CHAPTER 5

CONTENT

Article 5.1

(Express and implied obligations)

The contractual obligations of the parties may be express or implied.

COMMENTS

This provision states the widely accepted principle according to which the parties' obligations are not necessarily limited to what has been expressly stipulated in the contract. Some other obligations may be implicit (see below, comments and illustrations on article 5.2.)

Close links exist between this rule and some other provisions of these Principles. This Article 5.1 is a direct corollary of the rule according to which "Each party must act in accordance with good faith and fair dealing in international trade" (art. 1.8). Insofar as the rules on interpretation (Chapter 4) provide for criteria for filling lacunæ (besides criteria for solving ambiguities), those rules can contribute to determine the precise content of the contract and therefore to establish which terms have to be considered as implied.

Article 5.2

(Implied obligations)

Implied obligations stem from :

(a) the nature and purpose of the contract;

(b) practices established between the parties and usages;

(c) good faith and reasonableness.

COMMENTS

Article 5.2 explains where implied obligations may originate from. Different reasons can account for the fact that they have not been expressed. They may have been so obvious, from the nature or the purpose of the obligation, that the parties felt these obligations "went without saying". Orh they were already included in the practices established between the parties or prescribed by the usages of the trade, according to article 1.9. Or they are the consequences of the requirement of observing good faith and reasonableness in contractual relations, as stated in article 1.8

Illustration 1

Firm A rents a full computer network to Firm B., and installs it. The contract fails to provide anything about A's possible obligation to give the lessee at least some basic information concerning the way to operate the system. But it can be considered to be an implied obligation. It is obvious, and necessary for the accomplishment of the purpose of such a contract, that the provider of sophisticated goods has to supply the other party with a minimum of information.

Illustration 2

A broker has negotiated a charter-party and he now claims for his commission. The brokage contract is silent about the moment when that commission is due. The usages of the sector can provide an implied term according to which the commission is due e.g.

only when the hire is earned, or, on the contrary, on signing the charter-party, regardless whether the hire will effectively be paid or not.

Illustration 3

Two companies have entered into the negotiation of a cooperation agreement. They make an agreement concerning a complex feasability study, which will be very time-consuming for one of the parties. Much before the study is completed, the other party decides it will not pursue the negotiation of the cooperation agreement. Even though nothing has been stipulated for such a situation, good faith obliges that party to notify its decision without delay to the other party.

Article 5. 3

(Cooperation between parties)

Each party shall cooperate with the other party, when such cooperation may reasonably be expected for the performance of that party's obligations.

COMMENTS

A contract is not the mere meeting point of conflicting interests; it must also, to some extent, be considered as a common project to which each party has to cooperate. This view also has definite links with the principle of good faith that dominates the law of contract, as well as with the obligation to mitigate damages in case of breach.

This duty to cooperate must of course be contained within certain limits (the provision refers to reasonable expectations), so as not to upset the allocation of duties in the performance of the contract. The duty not to hinder the other party's performance is the main concern of the provision. But there may also be instances requiring a more active cooperation.

Illustration 1

Party A, after contracting with B for the immediate delivery of a certain quantity of oil, buys from another source all the available oil on the spot market. This behavior, which will hinder B from performing, is contrary to the obligation of cooperation.

Illustration 2

An art gallery of country B has bought an ancient painting from a private collector of country A. The work of art may not be exported without a special authorization, and the contract obliges the seller to apply for that permission. The seller, who has no experience with such formalities, encounters serious difficulties with his application. The art gallery, on the other hand, is familiar with such procedures. Under those circumstances, and in spite of the contractual provision, the buyer can be expected to give at least some help to the seller.

Article 5.4

(Duty to achieve a specific result

Duty of best efforts)

(1) To the extent that an obligation of a party involves a duty to achieve a specific result, that party is bound to achieve that result.

(2) To the extent that an obligation of a party involves a duty of best efforts in the performance of an activity, that party is bound to make those efforts that would be made by a reasonable person of the same kind under similar circumstances.

COMMENTS

The degree of diligence required from a party in the performance of an obligation may vary considerably according to the kind of obligation incurred. Sometimes a party is only bound by a duty of best efforts; he then has to exercise such best efforts to perform, but does not guarantee the achievement of a specific result. In other cases, on the contrary, the obligation is more intense, and such a result is promised.

The distinction between a "duty to achieve a specific result" and a "duty of best efforts" corresponds to two frequent and typical degrees of intensity in assuming a contractual obligation., though it does not encompass all possible situations.

Obligations of both types can coexist in the same contract. For instance, the firm that repairs a defective machine may be considered to be under a duty of best efforts concerning the quality of the repair work in general, and under a duty to achieve a specific result relatively to the replacement of certain spare parts.

The two paragraphs respectively provide judges and arbitrators with criteria by which correct performance can be evaluated. In the case on an obligation to achieve a specific result, the obliged party is simply bound to achieve the promised result; failure to achieve it amounts in itself to non-performance, subject to the application of the force majeure provision of article 7.1.6. On the other hand, assessing non-performance of an obligation of best efforts implies a more qualified judgement, based on the comparison with the efforts a reasonable person of the same kind under similar circumstances would have made. This criterium means that more will be expected from a very specialized firm selected for its expertise that from a less sophisticated partner.

Illustration 1

A distributor promises he will reach a quota of 15.000 sales within a year in the contract zone. If he has sold only 13.000 items at the end of the period, he has clearly failed to perform his obligation.

Illustration 2

Another distributor promises "to use his best efforts to expand the sales of the product" in the contract zone, without any stipulation to reach minimum quantities. This provision creates an obligation of best efforts; it obliges the distributor to take all the steps that a reasonable person, placed under similar circumstances (nature of the product, characteristics of the market, importance and experience of his firm, presence of competitors, etc...) would take to promote the sales (advertising, visits to customers, good service, etc...). He does not promise the specific result of selling a certain amount of items per year, but he undertakes to do all that can be expected from him when acting as a reasonable person.

Article 5.5

(Determination of kind of duty involved)

In determining the extent to which an obligation of a party involves a duty of best efforts in the performance of an activity or a duty to achieve a specific result, regard shall be had to the following circumstances, among others :

a) the way in which the obligation is expressed in the contract ;

b) the contractual price and other terms of the contract ;

c) the degree of risk normally involved in achieving the expected result ;

d) the other party's ability to influence the performance of the obligation.

COMMENTS

It is important to determine whether an obligation involves a duty to achieve a specific result or a mere duty of best efforts, as the obligation is more intense in the former case. Sometimes that determination can be difficult. This provision offers criteria that can guide parties, judges and arbitrators, though the list given is not limitative. The problems involved are often matters of interpretation.

a) The way in which the obligation is expressed in the contract can often contribute to determine whether the parties have meant to stipulate a duty to achieve a specific result or a duty of best efforts.

Illustrations 1 and 2

Contractor A will build a storage facility for his client B, who badly wants the work to be finished in an unusually short time. If Contractor A accepts to promise that "the work will be completed before December 31", he assumes the obligation to achieve the specific result of meeting that deadline. If he merely undertakes "to try to complete the work before December 31", his obligation involves a duty of best efforts to attempt to meet the deadline, but no guarantee it will certainly be met.

b) The contractual price or other terms of the contract can also offer clues for the qualification of an obligation. An unusually high price, or another particular non-monetary reciprocal obligation, can be indicative of a duty to achieve a specific result where one normally assumes a mere duty of best efforts. Clauses linking payment of the price to the successful outcome of the operation, penalty clauses applicable if the result is not achieved, hardship clauses enabling a party to adapt the contract if circumstances make it too hard to perform as initially agreed, are other examples of contractual terms which can - in either way - help in the qualification of the concerned obligation.

c) When performance of an obligation normally involves a great degree of risk, one can generally expect that the obliged party will not want to guarantee a result, and the other party will not expect so much either. The opposite conclusion will be drawn when the desired result is normally reachable without any special difficulty.

Illustration 1

A space agency promises to put a telecommunication satellite into orbit. The rate of failure of the past launchings has been 22 %. One cannot expect the space agency to guarantee that the orbiting will be successful. The obligation is merely to observe the degree of diligence required for such launchings, considering the present state of technology.

Illustration 2.

Firm A promises to deliver 20 tons of steel to Firm B, on June 30. Such a relatively simple operation is subject to no special risk. Firm A is committed to the specific result of delivering the required quantity of steel on the required date, not merely to try to do it.

d) Sometimes the other party has some influence on the performance of the obligation. That circumstance can transform into duties of best efforts obligations which otherwise could involve duties to achieve specific results.

Illustration 3.

Company A will give Company B the technical assistance necessary to apply a newly discovered chemical process, and it is agreed that B will send some of its engineers to attend training sessions organized by A. Company A cannot promise the new process will be mastered by the other party, since that result partly depends on B's effectively sending its engineers to the sessions, on those engineers's competence and on their assiduity to the sessions.

Article 5.6

(Determination of quality of performance)

If the quality of performance is not fixed by nor determinable from the contract, a party is bound to render a performance of a quality that is reasonable and not less than average in the circumstances.

COMMENTS

Standards have been set in article 5.4. about exerting one's "best efforts", but quality of performance is a wider problem, which article 5.6 addresses. If goods have to be supplied, or services rendered, it is not sufficient to supply those goods or to render those services; they also have to be of a certain quality.

Often the contract will be explicit concerning the quality due ("grade 1 oil"), or it will provide elements to make that quality determinable. In other cases, the rule set by article 5.6 is that the quality must be "reasonable and not less than average in the circumstances". Two criteria are thus combined.

The minimum requirement is to provide goods of an average quality. The obliged party is not bound to provide superior quality in case it is not required by the contract, but it may not deliver goods or services of inferior quality. This average quality is determined according to the circumstances, which normally refers to what is available on the relevant market at the time of performance (there may have been a recent technological advance). Some other factors may also intervene, such as the specific qualifications for which the performing party was chosen.

The additional reference to reasonableness intends to prevent a party from claiming it has performed adequately if it has rendered an "average" performance in a market where the average quality is very unsatisfactory. This will give the judge or the arbitrator an opportunity to raise those insufficient standards.

Illustration

Contractor A undertakes to build a hotel next to a busy train station. The contract provides for adequate sound isolation", the quality of which is not more precisely determied. However, it is determinable from the contract that the sound isolation must meet the high standards needed due to the proximity of a busy train station.

Illustration 2

Firm A buys 500 kgs. of "oranges" from Firm B. If the contract says nothing more precise, and no other circumstances call for another solution, these oranges may not be of less than average quality. However, average quality will suffice, unless it is unreasonably defective.

Illustration 3

A company based in Rataland organizes a banquet to celebrate its 5Oth anniversary. Since Rataland cooking is rather mediocre, that company orders the meal from a renowned Parisian restaurant. Under the circumstances, the quality of the food provided must not be less than the average standards of the Parisian restaurant; it would clearly not be sufficient to meet average Rataland standards.

Article 5.7

(Price determination)

(1) If a contract does not fix or make provision for determining the price, the parties are considered, in the absence of any indication to the contrary, to have made reference to the price generally charged at the time of the conclusion of the contract for such performances under comparable circumstances in the trade concerned, or if no such price is available, to a reasonable price.

(2) Where the price is to be determined by one party whose determination is manifestly unreasonable, then notwithstanding any provision to the contrary, a reasonable price shall be substituted.

(3) Where the price is to be fixed by a third person, and he cannot or will not do so, the price shall be a reasonable price.

(4) Where the price is to be fixed by reference to factors which do not exist or have ceased to exist or to be accessible, the nearest equivalent factor shall be treated as a substitute.

COMMENTS

(1) A contract usually fixes the price to be paid, or makes provision for its determination. If however this is not the case, this article presumes that the parties have made reference to the price generally charged at the time of the conclusion of the contract for such performances under comparable conditions in the trade concerned. All these qualifications are of course significant. The provision also permits to reverse the presumption if there is any indication to the contrary.

This article is inspired by article 55 of C.I.S.G. The rule has the necessary flexibility to fit the needs of international trade.

It is true that in some cases, the price generally charged on the market may not satisfy the reasonableness test present elsewhere in this article. One would then have to appeal to the general provision on good faith and fair dealing (article 1.8), or possibly to some of the provisions on mistake, fraud and gross disparity (Chapter 3).

Some international contracts concern operations which are unique or at least very specific, for which one cannot refer to the price charged for similar performances under comparable circumstances. The parties are then deemed to have made reference to a reasonable price. The concerned party will fix his price at a reasonable level, under the control of judges or arbitrators.

Illustration 1

Firm A, specialized in express mailing all over the world, receives from Firm B a parcel to be delivered as soon as possible from France to the United States. Nothing is said about the price. Firm A is supposed to bill B with the price that is usually charged in the sector for such a service.

Illustration 2

The next order that same Firm A gets from Firm B is now to deliver another parcel as soon as possible to ... Antarctica, where an exploratory mission needs some urgent supplies. Again, nothing is said about the price, but there is really no possible comparison on the market. Firm A will have to be reasonable when fixing the price.

(2) In some cases the contract expressly provides that the price will be determined by one of the parties. This is a frequent

occurrence in several sectors, e.g. for services. The price cannot easily be determined in advance, and the performing party is in the best position to evaluate what it has done.

In those instances where the parties have made such a provision for determining the price, it will be enforced. But, against possible abuses, paragraph (2) enables judges or arbitrators to replace a manifestly unreasonable price by a reasonable one. This provision is mandatory.

(3) The provision that the price will be determined by a third person can lead to a serious difficulty if that third person is not able to accomplish his mission (he is not the expert one thought he was), or refuses to do it. Paragraph (3) provides that the price, possibly then determined by judges or arbitrators, shall be reasonable. If the third party determines the price under circumstances that may involve fraud, gross disparity or mistake, article 3. 11 may apply.

(4) In other cases, the price is to be fixed by reference to some outside factors, typically a published index, or quotations at a commodities exchange. What shall be done if the reference factor ceases to exist or to be accessible ? This paragraph provides that the nearest equivalent factor shall be treated as a substitute.

Illustration 3

The price of a construction contract is linked to several indexes, including the "official index of salaries in the construction sector", regularly published by the local government. Several installments of the price still have to be calculated when that index ceases to be published. But the Federation of Construction, a private trade association, decides to start publishing a similar index to replace the former one. This new index will serve as a substitute.

CHAPTER 6

PERFORMANCE

SECTION I : Performance in General

Article 6.1.1.

(Time of performance)

A party must perform its obligations :

a) if a time is fixed by or determinable from the contract, at that time;

b) if a period of time is fixed by or determinable from the contract, at any time within that period unless circumstances indicate that the other party is to choose a time; or

c) in any other case, within a reasonable time after the conclusion of the contract.

COMMENTS

When is a contractual obligation to be performed ? This article distinguishes between three situations. First, the answer will be found in the contract if it stipulates the precise time for performance or makes it determinable. If the contract does not provide a precise moment, but a period of time for performing, any time during that period chosen by the performing party will be adequate, unless circumstances indicate the other party is to choose the time. Finally, in any other case, performance is due within a reasonable time.

This article is inspired by article 33 of C.I.S.G.

Illustration 1

Firm A offers to counsel firm B in the latter's plans to buy computer equipment and software, and it is agreed A's experts will visit B "in May". It is in principle up to A to announce when precisely in May that visit will take place. But the opposite solution could derive from the circumstances, clearly if the contract explicitly gives B the choice of the precise dates, but also, for example, if it is understood that some of B's staff members, who are often away on business trips, have to be present when A's experts come.

Illustration 2

Building Contractor A encounters unusual difficulties when excavating a site, and needs special equipment he does not have to continue the work. Contractor A immediately telephones to Contractor B, who has the equipment and agrees to lend it to A. But nothing is said about the moment those tools should be delivered to A. Performance is then to take place "within a reasonable time", under the circumstances. Since the work has been interrupted because of the difficulties mentioned above, A needs to receive the borrowed tools urgently. In this case, "within a reasonable time" probably means that performance is due almost immediately.

Article 6.1.2.

(Contracts for an indefinite period)

A contract for an indefinite period may be ended by either party by giving notice of reasonable length.

...

(comments to be completed after determination of the final location of this article)

Article 6.1.3.

(Performance at one time or in installments)

In cases under Article 6.1.1. (b) or (c), a party must perform its obligations at one time, if that performance can be rendered at one time and the circumstances do not indicate otherwise.

COMMENTS

A party's performance is sometimes necessarily rendered at one time (e.g. delivery of a single object), or, on the contrary, necessarily takes places over a period of time (e.g. construction). But there are also cases when it can be rendered either at one time or in installments (e.g. delivery of quantities of goods). Article 6.1.3. addresses this last situation, in the absence of any contractual provision as to how such performance should then be rendered, or if it is not determinable from the contract. The principle stated is that performance is due at one time, unless the circumstances indicate otherwise.

Illustration 1

Firm A has promised to deliver 100 tons of coal to firm B "in March". It would materially be possible for A, and perhaps convenient for that party, to deliver those 100 tons in installments; for instance, 25 tons every week of the month. But in principle, according to the rule of article 6.1.3., A has to deliver the 100 tons at one time.

Illustration 2

The case is the same as in Illustration 1, but Firm B needs the coal gradually, to meet the needs of its operations; it also has limited storage facilities and could not adequately cope with a delivery of 100 tons at one time. Here are circumstances that indicate that Firm A should instead deliver in installments, during the month of March.

Article 6.1.4.

(Partial performance)

(1) The obligee may reject an offer to perform in part at the time performance is due, whether or not coupled with assurance as to the balance of the performance, unless he has no legitimate interest in doing so.

(2) Additional expenses caused to the obligee by partial performance are to be borne by the obligor, without prejudiuce to any other remedy.

COMMENTS

(1) When performance is due at maturity (whether it is the whole performance or an installment), what is due has to be performed completely. In principle, the obligee may reject an offer of partial partial performance, whether or not coupled with assurance as to the balance of the performance . He is entitled to receive the whole of what was stipulated. Subject to what will be said below, partial performance normally constitutes a breach of contract. The party who does not get a full performance at maturity can make use of the available remedies. As a rule, the obligee has a legitimate interest in demanding full performance of what was promised, at the time that performance is due.

The obligee may of course also abstain from rejecting the offer to perform in part while reserving his rights as to the breach. He may even find it acceptable without any reservation, in which case partial performance can no longer be treated as a breach.

There may be situations when the obligee's legitimate interest to receive full performance is not apparent, when temporarily accepting partial performance will not cause any significant harm to the obligee. If the party tendering partial performance proves that it is the case, the obligee cannot then refuse such partial performance (subject to the following paragraph (2)), and there is also no breach of contract in such a situation. This can be considered as a consequence of the general principle of good faith and fair dealing expressed in article 1.8.

Illustration 1

Firm A wants to open a subsidiary in Brussels and it rents the necessary office space in a building under construction, due to be finished by the time of the move, on September 1. On that date, only 4 of the 10 offices are offered to Firm A, with an assurance that the remaining six will be ready in one month. In principle, Firm A may refuse to accept moving into those 4 offices only.

Illustration 2

An airline has promised to transport 25 automobiles from Italy to Brasil, in one single delivery due to be made on a definite date. When performance is due, some circumstances make it difficult for the airline, though not impossible, to find sufficient place in a single aircraft. The airline suggests to make two successive deliveries within a week. It is established that this will not cause any inconvenience to the purchaser of the cars, which will actually not be used before the following month. Here the obligee has no legitimate interest in refusing partial performance.

(2) In case partial performance is accepted, it may entail additional expenses to the obligee. In all cases, these expenses are to be borne by the other party. If partial performance amounts to a breach (the normal case), these expenses will be part of the damages, without prejudice to any other available remedy. If partial performance does not amount to a breach (the obligee has been shown not to have any legitimate interest in rejecting the offer of partial performance, or he has found that offer acceptable without reservation), he will only be entitled to those expenses.

Illustration 3

If in the case of Illustration 2 above, the purchaser has to meet additional expenses because of having to make double arrangements for picking up the cars at the airport, these extra costs will be borne by the airline.

(3) The situation covered by article 6.1.4. should be distinguished from that of article 6.1.3.

The provision on "Performance at one time or in installments" attempts to solve a preliminary question, which concerns only certain special cases. If a party's performance can be rendered at one time or in installments and if the contract does not make it clear or determinable how that party has to perform, it has in principle to perform at one time.

Article 6.1.4. ("Partial performance") has a more general scope. It says that at the time performance is due, the obligee may in principle reject an offer of partial performance. This applies at maturity, and whether what is due then is a global performance or an installment of a larger obligation (which, in some cases, has been previously determined on the basis of article 6.1.3.).

Illustration 4.

Borrower A owes $ 1,000,000 to Bank B, and it has been agreed he will reimburse $ 100,000 on the 1st of every month, starting in January. On the 1st of April, A offers to reimburse only $ 50,000, and the balance two weeks later. In principle, Bank A is entitled to refuse.

Article 6.1.5.

(Order of performance)

(1) To the extent that the parties' performances can be rendered simultaneously, the parties are bound to render them simultaneously, unless the circumstances indicate otherwise.

(2) To the extent that performance of only one party requires a period of time, that party is bound to render its performance first, unless the circumstances indicate otherwise.

COMMENTS

In bilateral contracts, where both parties have obligations towards each oher, who is to perform first ? This is a basic, but complex question. In practice, if the parties have not made any specific arrangements, much depends on usages. One must also consider that there are often several obligations on each side, which may have to be performed at different times.

Article 6.1.5. states two broad principles, while admitting in both cases that circumstances can indicate otherwise. Actually, the main purpose of this provision is to draw the parties' attention to the problem of order of performance, and to invite them to draft adequate contractual stipulations if necessary.

A distinction is made between situations where the parties' performances can be rendered simultaneously, and cases where the performance of only one party requires a period of time.

In the first hypothesis, the rule is that the parties are bound to render their performances simultaneously. A seller is entitled to be paid at delivery. But circumstances may indicate otherwise, and that covers all deviations originating from contractual terms or from usages, which may allow a party to perform a certain time after the other party has performed.

If performance of only one party's obligation, by its very nature, requires a period of time, e.g. in construction and most services, the rule set in paragraph (2) is that that party is bound to render its performance first. Here again, circumstances may indicate otherwise, and it will be frequent. Insurance premiums are normally paid in advance, so are rents and transportation freights. In construction contracts, payments are usually made in agreed installments along the progress of the works.

This article sets the rules which will condition the application of article 7.1.3. concerning withholding performance.

Illustration 1.

Firm A and Firm B agree to barter a certain quantity of oil and a certain quantity of cotton. Unless circumstances indicate otherwise, both commodities should be exchanged at the same time.

Illustration 2.

Consultant A promises to write a legal opinion to help Firm B in an arbitration case. If no arrangement is made as to when A should be paid for his services, he has to prepare his consultation before asking for his fees.

Article 6.1.6.

(Earlier performance)

(1) The obligee may reject an earlier performance unless he has no legitimate interest in doing so.

(2) A party's acceptance of an earlier performance does not affect the time for the performance of his own obligation if it has been fixed irrespective of the performance of the other party's obligations.

(3) Additional expenses caused to the other party by earlier performance are to be borne by the performing party, without prejudice to any other remedy.

COMMENTS

(1) When performance is due at a certain moment (determined according to article 6.1.1.), it has to take place at that moment. In principle, the obligee may reject an earlier performance. Usually the time for performance has been set to suit the obligee's activities, and earlier performance may cause him some inconvenience; therefore, the obligee has a legitimate interest to refuse it. Earlier performance, in principle, constitutes a breach of contract.

The obligee may of course also abstain from rejecting an earlier performance, but reserve his rights as to the breach. He may also find it acceptable without any reservation, in which case earlier performance can no longer be treated as a breach.

There may be situations when the obligee's legitimate interest to receive timely performance is not apparent, when accepting earlier performance will not cause significant harm to the obligee. If the party tendering earlier performance proves that this is the case, the other party cannot then reject earlier performance.

Illustration 1

Firm B is to do the yearly maintenance of all elevators in Firm A's office building on October 15. B's employees appear on October 14, a day when important meetings, with many visitors, are taking place in the building. Firm A is entitled to refuse such earlier performance that would cause obvious trouble.

Illustration 2

Same example as the preceding illustration, but October 14 is an ordinary day just as October 15. Firm B can probably prove A has no legitimate interest in refusing that earlier performance.

(2) If a party accepts earlier performance by the other party, does it affect the time for performing its own obligations ? Paragraph (2) deals with the case those obligations were due at a certain time, which was not linked to the performance of the other party's obligations; that time for performance remains unchanged.

However, this provision does not deal with the opposite case where the performances were linked in time. Several situations may then occur. This circumstance in itself may establish the obligee's legitimate interest in rejecting earlier performance. If earlier performance is thus rejected, nothing is changed as to the obligee's time of performance. If earlier performance is taken with all due reservations as to the breach involved, the obligee may also reserve his rights as to his time for performance. If earlier performance is agreeable to the obligee and he accepts it, he may or he may not at the same time also accept the consequences on his own obligations.

<u>Illustration 3</u>

Firm B has to deliver goods to Firm A on May 15, and A has to pay the price on June 30. Firm B wants to deliver the goods on May 10, and A has no legitimate interest in refusing such earlier performance. But this will have no effect on the time agreed upon for payment of the price, which was determined irrespective of the date of delivery.

<u>Illustration 4</u>

Firm B has to deliver goods to Firm A on May 15, and A has to pay the price "on delivery". If Firm B tenders the goods on May 10, Firm A, depending on the circumstances, may reject such earlier performance, pointing out it is not in a position to pay at that date, or it may take the goods subject to keeping the original deadline for payment of the price, or it may still decide to accept the goods and pay them directly.

(3) In case earlier performance is accepted, it may entail additional expenses to the obligee. In all cases, these expenses are to be borne by the other party. If earlier performance amounts to a breach (the normal case), these expenses will be part of the damages, without prejudice to any other available remedy. If earlier performance does not amount to a breach (the obligee has been shown not to have any legitimate interest in rejecting the offer of earlier performance, or he has found that offer acceptable without reservation), he will only be entitled to those expenses.

Illustration 5

Firm A has no legitimate interest to refuse delivery of the goods on May 10 instead of May 15, but there are some additional storage fees to pay for those five extra days. Those costs will be borne by Firm B.

Article 6.1.7.

(Place of performance)

(1) If the place of performance is not fixed by nor determinable from the contract, a party is to perform :

a) a monetary obligation, at the creditor's place of business;

b) any other obligation, at its own place of business ;

(2) A party must bear any increase in the expenses incidental to performance which is caused by a change in its place of business subsequent to the conclusion of the contract.

COMMENTS

(1) The place where an obligation must be performed is often determined by an express term of the contract, or it is determinable from it. It is obvious, for instance, that an obligation to build must be performed on the construction site, and that an obligation to transport goods must be performed along the route to be taken.

Rules are however needed for cases when the contract is silent and circumstances do not indicate where performance should take place. Article 6.1.7.(1) provides two solutions.

The general rule is that a party is to perform its obligations at its own place of business. The other rule is specific to monetary obligations, where the opposite solution applies : the debtor is to perform its obligations at the creditor's place of business (subject to the application of article 6.1.9. concerning payments by funds transfers).

These solutions may not be the most adequate in all cases, but they fill the need to find rules where parties have not made any other arrangement, or circumstances do not indicate otherwise.

Illustration 1

An engineering firm undertakes to do preparatory studies and research work for the construction of a plant, and to deliver all plans and documents at the end of its work. If nothing else is agreed, all of this is to be perfotmed at the engineeering firm's place of business. If the contractor or the client want the plans and documents to be delivered to their place, they should stipulate it in the contract.

Illustration 2

The engineering firm of Illustration 1 sends its bill to the client or the contractor. The fees, in principle, have to be paid at the engineeering firm's place of business.

(2) Considering the importance of the parties' respective places of business for the application of Paragraph (1), the case must be met when a party changes its location after the conclusion of the contract. This move may involve additional expenses for the performing party. The rule is that each party must bear any such increase of expenses caused by a change of its place of business.

On the other hand, it is also possible that a party's move entails other inconveniences to the other party. The obligation to act in good faith (art. 1.8.) and the duty to cooperate (art. 5.3.) will often impose to the moving party the obligation to inform the other party in due time, in order to enable that latter party to make adequate arrangements if necessary.

Illustration 3

Firm A enters into a technical assistance agreement with Firm B, by which A will train ten engineeers from B at A's own premices, for a period of two months. The engineers will be accomodated in a local hotel, which offers very reasonable rates due to A's location in a rural area. After the agreement is concluded but before B's engineers have arrived, A notifies B it has moved to the capital city, where hotel rates are much higher. Whether the initial costs of accomodation were to be paid by A or by B, additional costs will be borne by A.

Illustration 4

Every year on May 3, Firm A has to pay royalties to Firm B, i.e. at B's place of business. Firm B moves to another country, to which it takes some time (e.g. two months) to get a payment through. Firm A used to give its bank the transfer order around April 15, but from now on the order has to be given late March at the latest if A does not want to be in delay. Firm B has the duty to inform A of its new place of business in time to permit A to organize the process of payment, and B will bear the additional costs.

Article 6.1.8.

(Payment by cheque or other instruments)

(1) Payment can be made in any form used in the ordinary course of business at the place of payment.

(2) However, a creditor who accepts, either by virtue of paragraph (1) or voluntarily, a cheque, another order to pay or a promise to pay, is presumed to do so only on condition that it will be honoured.

COMMENTS

Payment of monetary obligations are very frequently made by cheques or similar instruments, or by transfers between financial institutions. Yet the problems involved have very seldom been the object of codifications. As a notable exception one will mention the UNCITRAL Model Law on International Credit Transfers. Without attempting to provide a detailed regulation, which would not be compatible with the very rapid evolution of techniques in this field, articles 6.1.8 and 6.1.9. establish a few basic principles which should be useful in international payments.

The provision or paragraph (1) allows for a payment to be made in any form that is usual at the place of payment. With the reservation expressed in paragraph (2), the debtor may for instance pay in cash, with a cheque, a banker's draft, a bill of exchange, a credit card, or with any other technique, like the newly developing electronic means of payment, provided he chooses a mode that is usual at the place of payment, i.e. normally at the creditor's place of business. In principle, the creditor should be satisfied to receive his payment in a form that is customary at his place.

Paragraph (2) states the generally recognized principle according to which the creditor's acceptance of an instrument of payment that has to be honoured by a financial institution or another third party can only be given on the condition that the instrument will effectively be honoured.

The presumption can sometimes be overturned by usages. There are for instance countries where delivery of instruments such as certified cheques, banker's drafts and cashier's cheques is considered as equivalent of a payment by the obliged party, with the consequence that the risk of the bank's insolvency is transfered to the obligee. In such countries, the rule in article 6.1.8. (2) would apply to so-called personal cheques only.

Illustration 1

Luxembourg Importer A receives a bill for the goods he has bought from a firm in Central America, and he sends an eurocheque in payment. The exporter may reject this mode of payment if the banks in his country are not familiar with eurocheques.

Illustration 2

Contractor Y has to pay Sub-contractor Z for the works he has completed on the building site, but Y is going through a liquidity crisis as Client X is late in paying him the first installment due. Client X, however, has given Y a set of promissory notes up to the amount of his debt. Contractor Y offers to pay Z by assigning the adequate number of promissory notes to the sub-contractor. If Z accepts them (in this case he probably does not have to, as it is not a usual form of payment), the effectiveness of the payment by Y to Z is conditional to X's honouring the promissory notes at maturity.

Article 6.1.9.

(Payment by funds transfer)

(1) Unless the creditor has indicated a particular account, payment can be made by a transfer to any of the financial institutions in which the creditor has made it known he has an account.

(2) In case of payment by a transfer the obligation of the debtor is discharged when the transfer to the creditor's financial institution becomes effective.

COMMENTS

Article 6.1.9. deals with payments by funds transfers between financial institutions.

Paragraph (1) concerns the admissibility of payments by funds transfers. Though the principle still stands, according to article

6.1.7., that payment of a monetary obligation should be made at the creditor's place of business, it can also be made to one of the financial institutions in which the creditor has made it known he has an account. If however the creditor has indicated a particular account, payment should then be made to that account. Naturally, the creditor can also make it known that he does not want his payment to be made by transfer.

Paragraph (2) deals with the difficult question of determining when a payment by funds transfer can be considered as completed, i.e. when the debtor's obligation is to be discharged. This matter is of importance, e.g. to decide whether the payment was made in time, or in the case one of the banks does not forward the funds it has received. But the choice of an adequate solution has been the center of much controversy in many countries and international forums. Different moments have been considered : debit to the account of the transferor, credit to the account of the transferee bank, notice of credit to that account, decision of the transferee bank to accept credit transfer, entry of credit to transferee's account, notice of credit to transferee, etc... The matter is further complicated by the changes of procedures for the transfer of funds brought about by new electronic transfer mechanisms, and bank practices can also differ from one case to another.

All of this makes it extremely hazardous to establish a very accurate rule providing when payment by a transfer is completed. Article 6.1.9.(2) still serves a useful purpose as it states the basic principle which will permit to find the more precise rule in each case. Such a payment will be effective when the transfer to the creditor's financial institution will become effective. The solution rests on the ground that that institution acts as the creditor's agent. It means no effective payment exists before that moment, even though the order has been given to the transferor's financial institution, and the tranferor's account has been debited. And payment is effective before the transferee is notified or credited of it by his financial institution. But the precise moment when payment to the creditor's financial institution can be considered as effective will depend on banking practices in the case concerned.

<u>Illustration 1</u>

Shipyard Y, a firm established in Helsinki, has repaired a ship belonging to a Swedish firm, and the bill is sent on a letter-head that mentions a bank account in Finland and another one in Sweden. Unless Y states that payment has to be made to the Finnish account, or by another means than a bank transfer, the Swedish firm is entitled to pay to the Swedish account.

Illustration 2

Licensee A gives his Bank Z a transfer order of $ 5,000, royalties due to Licensor B, who has an account with Bank W. Bank Z debits A's account, but fails to forward the funds to Bank W, and goes bankrupt. Licensee A has not effectively paid Licensor B.

Article 6.1.10

(Currency of payment)

(1) If a monetary obligation is expressed in a currency other than that of the place of payment, it may be paid by the debtor in the currency of the place of payment unless

(a) that currency is not freely convertible; or

(b) the parties have agreed that payment should be made only in the currency in which the monetary obligation is expressed.

(2) If it is impossible for the debtor to make payment in the currency in which the monetary obligation is expressed, the creditor may require payment in the currency of the place of payment, even in the case envisaged in paragraph (1)(b).

(3) Payment in the currency of the place of payment is to be made according to the applicable rate of exchange prevailing there when payment is due.

(4) However, if the debtor has not paid at the time when payment is due, the creditor may require payment according to the applicable rate of exchange prevailing either when payment is due or at the time of actual payment.

COMMENTS

Monetary obligations are usually expressed in a certain currency (currency of account), and payment normally has to occur in the same currency.

However, when the currency of the place of payment is different from the currency of account, paragraphs (1) and (2) of this article provide for cases when the debtor may or must pay in the former currency.

(1) As a general rule, the debtor is given the alternative possibility of paying in the currency of the place of payment. It may have definite practical advantages, and if that currency is freely convertible, it should cause no difficulty to the creditor.

Precisely, if the currency of the place of payment is not freely convertible, the rule does not apply. Parties may also exclude the application of the rule by agreeing that payment is to take place only in the currency in which the monetary obligation is expressed (effectivo clause). If the creditor has an interest in having the payment effectively made in the currency of account, he should specify it in the contract.

Illustration 1

A French firm receives an order for machinery from a Brazilian buyer, and the price is expressed in U.S. dollars. According to article 6.1.7. of the Principles, payment of that monetary obligation must in principle be made at the creditor's place of business, i.e. in France. If the Brazilian firm finds it more convenient, it may pay the price in French francs.

Illustration 2

The same French firm frequently needs to buy from U.S. sources some parts to be included in the machines, and it has stipulated that the Brazilian buyer should pay only in dollars. In the case, payment may only be made in dollars.

Illustration 3

The same French firm has a plant in Syldavia, where the machines will be assembled. The contract provides that the Brazilian Buyer had to pay the price to the Syldavian subsidiary. Since the Syldavian dinar is not convertible, payment may only be made in dollars.

(2) In some instances, the debtor may find it impossible to pay in the currency in which the obligation was expressed. It may be the result of the application of exchange regulations or other mandatory rules, or also of any other cause preventing the debtor from obtaining that currency in sufficient quantity. Paragraph (2) gives then the creditor the option to require payment in the currency of the place of payment, even if the contract contained an effectivo clause. This is an additional option open to the creditor, who may find it acceptable or even advantageous under the

circumstances. It does not preclude the exercise of any available remedy in case the debtor's inability to pay in the currency of account amounts to a breach of contract (e.g. damages).

Illustration 4

Swiss Bank B has loaned $ 1 million to Borrower Z, to be reimbursed in Zürich. At maturity, Z is unable to find the necessary dollars. Bank B, which knows Z owns deposits in Swiss francs with another local bank, may require payment in Swiss francs, even though the loan agreement stipulated that reimbursement was to be made only in U.S. dollars.

(3)(4) These two paragraphs cover the problem of the determination of the rate of exchange to be selected when payment is made in the currency of the place of payment instead of the different currency of the contract. This may happen when the debtor avails himself of paragraph (1), or when the creditor avails himself of paragraph (2).

Two widely-accepted solutions are given. In normal cases, the rate of exchange is the one prevailing when payment is due. However, if the debtor is in default, the creditior is given the option between the rate of exchange prevailing when payment was due or the rate at the time of actual payment

The double reference to the "applicable" rate is justified by the fact that there may be different rates of exchange depending on the nature of the operation.

Illustration 5

Bank B has chosen to be reimbursed in Swiss francs, under the circumstances described in Illustration 4, and payment, which was due on April 10, actually takes place on September 15. The rate of exchange on April 10 was Sfrs. 2 to $ 1; it has become Sfrs. 2,15 to $ 1 on September 15. Bank B is entitled to apply the latter rate. If the dollar had not gone up, but down, Bank B would have chosen the rate on April 10.

Article 6.1.11

(Currency not expressed)

If a monetary obligation is not expressed in a particular currency, payment must be made in the currency of the place where payment is to be made.

COMMENTS

Determining the currency of payment causes a special problem if the contract does not express the currency in which a monetary obligation is due. This may not be frequent, but instances can be found : a contract can state that the price will be the "current price", or that it will be determined by a third party, or that some expenses or costs will be reimbursed by one party to the other, without specifying in which currency these sums are due. The rule in article 6.1.11. states that in such cases, payment must be made in the currency of the place where payment is to be made.

Article 6.1.11. does not concern the currency in which damages are to be paid. This problem is covered by article 7.4.12. of the chapter on non-performance.

Illustration 1

Dutch Client A instructs his broker to buy shares on the Frankfurt stock exchange. The broker pays them in German marks; should he bill his client in marks, or in Dutch guilders ? If Client A is to pay his broker in Amsterdam, he will pay in guilders.

Article 6.1.12

(Costs of performance)

Each party shall bear the costs of performance of its obligations.

COMMENTS

Performing one's obligations often entail costs, which may be of different kinds : transportation costs in delivering goods, bank commissions in making a monetary transfer, fees to be paid when applying for a permission, etc...

In principle, such costs are to be borne by the performing party.

Of course, other arrangements can be made by the parties, and nothing prevents the performing party to include those costs in advance in its quoted price. The rule in article 6.1.12 applies by default.

The provision states who shall bear the costs, not who shall pay them. Most of the time it will be the same party, but there may be different situations, e.g. when tax regulations put the burden of paying on a specific party; in such cases, if the person who has to pay is different from the person who has to bear the costs under this article 6.1.12, the latter must reimburse the former.

Illustration 1

Consultant X agrees to send five experts to Client Y for an audit of the firm. Nothing had been said about the experts' travel expenses, and X had failed to take those costs into account when determining its fees. X may not add the travel expenses to the bill.

Article 6.1.13

(Imputation of payments)

(1) A debtor owing several monetary obligations to the same creditor may specify, at the time of payment, the debt to which he intends the payment to be applied. However, the payment discharges first any expenses, then interests due and finally the principal.

(2) If the debtor does not make such specification, the creditor may, within a reasonable time after payment, declare to the debtor the obligation to which he imputes the payment, provided that obligation is due and undisputed.

(3) In the absence of imputation under paragraphs (1) or (2), payment is imputed to that obligation which satisfies

one of the following criteria and in the sequence indicated :

a) an obligation which is due or which is the first to fall due;

b) an obligation for which the creditor has least security;

c) the obligation which is the most burdensome for the debtor;

d) the obligation which has arisen first.

If none of the preceding criteria applies, payment is imputed to all the obligations proportionally.

COMMENTS

Articles 6.1.13. and 6.1.14. deal with the classical problem of imputation of payments. If a debtor owes at the same time, to the same creditor, several monetary obligations, and he makes a payment the amount of which is not sufficient to extinguish all those debts, to which debts does that payment apply ?

Article 6.1.13, inspired by widely-recognized principles, gives the debtor a first possibility to impute his payment, provided expenses and interests due are discharged before the principal. In the absence of any imputation by the debtor, the provision enables the creditor to impute the payment received, though not to a disputed debt. Paragraph (3) gives criteria which will govern the imputation in the absence of any initiative by either party.

Illustration 1

Firm A has received three loans, each of $ 100,000, from Bank B, by separate contracts. All three loans are due on December 31. Bank B receives $ 100,000 from A on January 2, with the imprecise message : "Reimbursement of the loan". The bank pays little attention to the matter and does not react at first. Three months later, the bank sues Firm A for payment of the remaining $ 200,000, and the parties disagree as to which of the loans has been reimbursed by the January payment. The Bank had similar security in each case, but the interest rates were not the same : 8 % on Loan n° 1, 8,50 % on Loan n° 2 and 9 % on Loan n° 3. Article 6.1.13 (3)(c) applies : the January payment will be imputed on Loan n° 3.

Article 6.1.14

(Imputation of non-monetary obligations)

Article 6.1.13 applies with appropriate adaptations to the imputation of performance of non-monetary obligations.

COMMENTS:

The problem of imputation of payments normally concerns monetary obligations, but similar difficulties can sometimes occur about obligations of a different nature. Article 6.1.14. provides that the preceding rules will then apply, with appropriate adaptations.

Illustration 1

Company Z is performing construction work on several sites in an African country, and through five separate and successive contracts with Supplier W, purchases different quantities of cement, all to be delivered in Antwerp on the same date, to be loaded on the same ship. The contracts are similar, except that contracts n° 3 and 5 stipulate very high liquidated damages for late delivery. Due to some difficulties, W can only deliver part of what he was supposed to. Upon delivery, in accordance with article 6.1.13 (1), the Supplier is entitled to specify that the quantities delivered are to be imputed to contracts n° 3 and 5.