

In previous alerts, we have dealt with the interplay between *force majeure* and frustration, five situations of *force majeure* and frustration, *force majeure* and change in law clauses, and what happens when *force majeure* ends – or does not. To complete the picture, we now add material adverse change (MAC) clauses to the mix and provide a decision tree to navigate the labyrinth.

## Material Adverse Change

MAC clauses, sometimes called hardship clauses, are highly dependent on text and context. We speak here of “usual clauses”; however, few MAC clauses are the same and our comments have to be read in that light. MAC clauses generally provide that if a party claims hardship or material adverse change in circumstances, notice may be given and the parties will negotiate a solution in good faith. Some provide for termination if a solution cannot be found, others allow for expert determination, while still others trigger the dispute resolution provisions.

These clauses usually have two parts – a definition of MAC or hardship and a provision for renegotiation to adapt the contract to the new situation. The definition usually limits entitling events to those occurring after the execution of the contract, which were unforeseeable at that time. Some definitions exclude changes in the global economy or the parties’ industry. In a situation such as the current pandemic, those definitions may require arguments that the adverse change came about from government action or the physical effects of the pandemic rather than from any global economic difficulty.

The second part of the clause provides a mechanism to evaluate the degree of the MAC or hardship, usually negotiation followed by dispute resolution or termination.

## Examples

### 1. International Chamber of Commerce model hardship clause

- [2] Notwithstanding paragraph 1 of this Clause, where a party to a contract proves that:
- (a) The continued performance of its contractual duties has become excessively onerous due to an event beyond its reasonable control, which it could not reasonably have been expected to have taken into account at the time of the conclusion of the contract
  - (b) It could not reasonably have avoided or overcome the event or its consequences, the parties are bound, within a reasonable time of the invocation of this Clause, to negotiate alternative contractual terms that reasonably allow for the consequences of the event

- [3] Where paragraph 2 of this Clause applies, but where alternative contractual terms that reasonably allow for the consequences of the event are not agreed by the other party to the contract as provided in that paragraph, the party invoking this Clause is entitled to termination of the contract.

### 2. UNIDROIT Principles of International Commercial Contracts 1994 model hardship clause

- “(1) In case of hardship the disadvantaged party is entitled to request renegotiations. The request shall be made without undue delay and shall indicate the grounds on which it is based.
- (2) The request for renegotiation does not in itself entitle the disadvantaged party to withhold performance.
- (3) Upon failure to reach agreement within a reasonable time either party may resort to the court.
- (4) If the court finds hardship it may, if reasonable,
- (a) terminate the contract at a date and on terms to be fixed, or
  - (b) adapt the contract with a view to restoring its equilibrium.”

“Hardship” in those principles is defined as:

“There is hardship where the occurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party’s performance has increased or because the value of the performance a party receives has diminished, and

- (a) the events occur or become known to the disadvantaged party after the conclusion of the contract;
- (b) the events could not reasonably have been taken into account by the disadvantaged party at the time of the conclusion of the contract;
- (c) the events are beyond the control of the disadvantaged party; and
- (d) the risk of the events was not assumed by the disadvantaged party.”

### 3. From a contract

In the event an inequitable condition occurs, which adversely affects one party, it shall be the joint and equal responsibility of both parties to act promptly to determine the action required to cure the inequity and effectively to implement such action. Upon written claim of inequity served by one party upon the other, the parties shall act jointly to reach an agreement concerning the claimed inequity within 60 days of the date of such written claim. The party claiming inequity shall include in its claim such information and data as may be reasonably necessary to substantiate the claim and shall freely and without delay furnish such other information and data as the other party reasonably may deem relevant and necessary.

## Key Differences

In this table, MAC means material adverse change or hardship, FM means *force majeure*, CIL means change in law and FCL means frustration at common law. The table compares the usual response of those clauses to the stated effect on performance. Answers in particular cases will depend on the reason for the effect on performance and, of course, the wording of the clauses in their context.

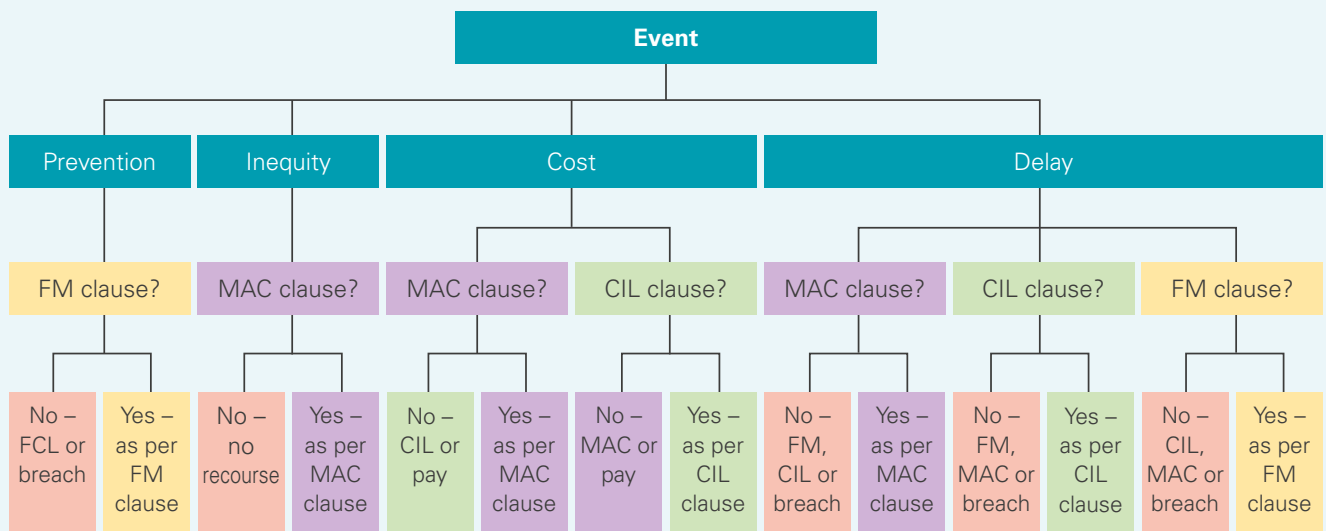
Effect on Performance	FM	CIL	MAC	FCL
Delay	Yes	No	No	No
Increased cost	No	Yes	Yes	No
Prevention	Yes	No	No	Yes
Inequity	No	No	No	Yes
Ability to pay	No	Yes	Yes	No
Effect on contract	Performance temporarily excused	Price increased or decreased	Contract renegotiated	Contract terminated

## Decision Tree for Affected Contract Performance

This decision tree shows the clauses that might respond to the four usual effects on performance – delay, cost, inequity and prevention. It is necessarily a summary and depends heavily on the text and context of clauses, which can vary widely.

### In this tree:

- CIL means change in law
- FM means force majeure
- Breach means breach of the term
- FCL means frustration at common law
- MAC means material adverse change or hardship
- Pay means pay the reasonable, foreseeable cost



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