Applicability of the force majeure principle to the termination of a contract rendered unlawful

The subsequent adoption of binding regulatory measures that render unlawful either the existence or the performance of a previously valid contract constitutes a paradigm scenario for the application of *force majeure* under the general principles of commercial law.

This analysis has been conducted in the context of a pro bono legal advice provided for the NGO B4Ukraine and constitutes a formed legal opinion on the applicability of the regulation proposed by the EU Commission for the prohibition of all supply contracts for natural gas –or similar products– by any Russian or Russia related company in the EU.

A. Introduction and objectives of the regulation.

1 Over recent years, the European Union has taken steps to phase out the purchase of Russian natural gas, most recently under the REPowerEU programme. In this spirit, the proposed amendment to Regulation (EU) 2017/1938 aims at ending European imports of Russian natural gas by forcing European undertakings to terminate short and long-term contracts with Gazprom. Specifically, the amendments seek to introduce a legal prohibition of imports of natural gas as of 1 January 2026, which rends the performance of natural gas contracts with Russian unlawful for the proximate future.

2 Implicitly, the Regulation relies on the concept of *force majeure* to justify the termination of contractual obligations binding European undertakings, which would be rendered unlawful by its entry into force.

3 This analysis focuses primarily on the implications arising under European Union law and Spanish law -the areas of specialization of our firm- while also briefly considering relevant aspects under other jurisdictions. The authors of this post are qualified to advise on matters of Spanish and European Union law, and therefore any references to non-EU or non-Spanish legal frameworks are intended merely as informed observations for contextual purposes.

B. Force majeure and its applicability to the case.

a. Relevance of the applicability of international sales law principles and customary law to gas supply contracts.

4 The definition of *force majeure* is, in some cases, only found in soft law instruments of international trade (particularly under Common law systems) and some goods may be excluded from its application.

5 First, regarding the applicability of the UN Convention on Contracts for the International Sale of Goods (CISG), we can conclude that natural gas supply contracts are not expressly excluded from the scope of application of the Convention (art. 2 CISG), but that the parties

may exclude contractually the application of the Convention (art. 6 CISG). Furthermore, natural gas supply contracts constitute a contract of goods within the meaning of art. 3 of the Convention.[1]

6 On the other hand, the applicability of both the UNIDROIT Principles of International Commercial Contracts and the Principles of European Contract Law (PECL's) is contingent upon the parties' express intention as set out in the contract, notwithstanding its possible tangential application as reflecting "general principles of law" or "lex mercatoria". In the case of the UNIDROIT principles, where the parties have not designated an applicable law, the arbitral tribunal may apply these principles.[2]

b. Force majeure according to the general principles of commercial law

i. Interpretation of force majeure in the relevant soft law.

7 *Force majeure* operates as an external and unforeseeable event, beyond the control and sphere of influence of the party invoking it, and against which no reasonable resistance could be expected. Grounded in risk allocation and the preservation of contractual equilibrium, these principles emphasize the need to assess unforeseeability and impossibility by reference to a standard of diligent conduct typical in commercial practice.

8 The CISG, the PECL's and the UNIDROIT principles regulate *force majeure*, emphasizing the notions of "unforeseeability" and "insurmountability" as constitutive elements for force majeure to operate as a ground for exemption of performance, and to excuse the non-performing party from liability in damages.

9 Under most national regulations, an event of *force majeure* fully exonerates a party from performing the obligation of the contract, provided that the event is autonomous and not

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[1] This conclusion is reached in:

- Paras. 180-181 of case Gasum Oy v. Gazprom Export LLC, Final Award, Ad hoc Arbitral Tribunal, Stockholm (Sweden), 14 November 2022, CISG-online No. 7151 (Arbitrators: Prof. Dr. Juan Fernández-Armesto (Presiding Arbitrator), Prof. Dr. Klaus Peter Berger, Yves Derains); see <https://cisg-online.org/search-for-cases?caseId=15065>, and

- Paras. 59-71 of case Italia Ukraina Gas S.P.A v. National Joint-Stock Company "Naftogaz of Ukraine" (I), SCC Case No. V007/2008, SCC Arbitration Institute, Stockholm (Sweden), 17 January 2008, (Arbitrators: Staffan Magnusson (Chairman), Ms. Charlotta Sundman (Secretary), Mr. Lars Edlund, G Grönberg Advokatbyrå AB); see < https://jusmundi.com/en/document/decision/en-italia-ukraina-gas-s-p-a-v-national-joint-stock-company-naftogaz-of-ukraine-separate-arbitral-award-tuesday-19th-october-2010>.

[2] This conclusion is reached in pages 87-88, of case Petrobart Limited v. The Kyrgyz Republic, SCC Case No. 126/2003, SCC Arbitration Institute, Stockholm (Sweden), 29 March 2005 (Arbitrators: Justice Hans Danelius, Professor Ove Bring and Mr. Jeroen Smets); see: <https://www.italaw.com/cases/825>.

attributable to its own fault or sphere of risk. Additionally, most regulations rely on good faith of the contractual party and refer to the express notification of the circumstance preventing performance as soon as the relevant information is available to the invoking undertaking.

ii. Concrete application to the examined case.

10 The subsequent adoption of binding regulatory measures that render unlawful either the existence or the performance of a previously valid contract constitutes a paradigm scenario for the application of *force majeure* under the general principles of commercial law. The Regulation proposed by the EU Commission aims to end all existing short and long-term supply contracts with Russian companies and prohibit the adoption of similar contracts in the foreseeable future.

11 However, for the European companies with existing long-term supply contracts that are rendered unlawful, this prohibition poses the question of how to correctly and lawfully terminate such contracts, to avoid legal and economic risks. Under this paradigmatic scenario, we examine the applicability of the *force majeure* principle to the case.

12 First, the requirement of <u>unforeseeability</u> at the time of contract formation is satisfied. Where a legal prohibition arises only after the parties have concluded the agreement, it is reasonable to infer that the contracting parties could not have anticipated the proscription; otherwise, the contract would not have been executed. This analysis is referenced to the level of diligence expected of an ordinarily prudent participant in the relevant commercial sector.

13 Secondly, the <u>irresistibility</u> requirement is equally satisfied. Parties to a private transaction lack the capacity to prevent the adoption, entry into force, and enforcement of binding laws or regulatory acts. A legal prohibition constitutes an obstacle against which resistance is not possible, and which does not depend on the party's personal capabilities or economic circumstances.

14 Moreover, where these elements concur, *force majeure* operates as a full exemption from liability, not a partial one. Since the non-performance is not attributable to fault and the external event does not concur with any culpable behaviour, no compensatory liability may be imposed on the affected party.

15 In light of the above, when a post-contract regulatory change directly prohibits the contractual conduct, the legal impossibility that ensues must be recognised as *force majeure*. This preserves the principle of risk allocation inherent in commercial law and prevents the award of damages for non-performance.

c. Considerations of force majeure in certain jurisdictions.

16 European Civil law systems generally recognise *force majeure* as an exception applicable to supervening events which rend contractual obligations impossible to perform.

17 The judgment in *First City Trading*[3] confirms that *force majeure* may encompass acts of public authority, provided the event is unforeseeable, beyond the operator's control and unavoidable despite all due care. Applied to contracts that become unlawful due to subsequent legislation, *First City Trading* offers a solid doctrinal basis to treat a regulatory change as a qualifying event.

18 Under Common law, courts have traditionally adopted a strictly textual and narrow interpretative approach of *force majeure*, allowing it to operate exclusively when terms such as "acts of government" or "change of law" are included in the contract. Catch-all wordings have been interpreted restrictively, as illustrated by *Tandrin Aviation Holdings Ltd v Aero Toy Store LLC*,[4] where a global financial downturn would not trigger the clause.

19 Finally, the interpretation of *force majeure* situations before arbitration tribunals support this note's interpretation. As a relevant example, the recent *Gasum Oy v. Gazprom Export LLC*[5] must be considered.

20 In this case, the parties discussed Gasum's obligation to purchase a minimum quantity of natural gas to Gazprom, a Russian national company, when such a company enacted a new payment regime for foreign buyers under a newly issued Decree n.172 259.

21 In 2022, Gazprom suspended deliveries of natural gas to Gasum, alleging that Gasum had failed to comply with its payment obligation under the terms set in the Decree and argued that the requirements of *force majeure* were met, rendering performance of the contract impossible.

22 The tribunal considered that such regulation constituted a *force majeure* circumstance: it was unforeseeable at the time of the signing of the contract and non-compliance with the terms of the Decree may give rise to severe legal consequences for Gazprom, as it constituted a norm of general application.

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[3] Case C-263/97, The Queen v. Intervention Board for Agricultural Produce, ex parte: First City Trading and Others, ECLI:EU:C:1998:444; see <https://eur-lex.europa.eu/legal-content/ES/TXT/PDF/?uri=CELEX:61997CJ0263_SUM>.

[4] Tandrin Aviation Holdings Ltd v. Aero Toy Store LLC [2010] EWHC (Comm), 19 January 2010; see <https://www.casemine.com/judgement/uk/5a8ff7d260d03e7f57eb2503>.

[5] Gasum Oy v. Gazprom Export LLC, Final Award, Ad hoc Arbitral Tribunal, Stockholm (Sweden), 14 November 2022, CISG-online No. 7151 (Arbitrators: Prof. Dr. Juan Fernández-Armesto (Presiding Arbitrator), Prof. Dr. Klaus Peter Berger, Yves Derains); see <https://cisg-online.org/search-for-cases?caseId=15065>.

C. Main takeaways of the analysis.

23 Following a review of the soft law principles shaping the concept of *force majeure*, it can be concluded that the ability to invoke such arguments in order to terminate performance rendered unlawful by supervening regulation depends on the extent to which those principles -or equivalent national provisions- apply. In particular, it turns on the contractual allocation of regulatory risk as reflected in the wording chosen by the parties, the nature of the impediment (legal impossibility versus economic hardship), and strict adherence to both the procedural and substantive requirements embedded in the relevant clause.

24 Under Civil law systems, we take the view that *force majeure* is generally present in national bodies of law, and what originated as a soft law principle has been further developed within each national legal system and should therefore be interpreted according to the respective domestic framework. Nevertheless, we consider that the *force majeure* principle remains generally applicable across jurisdictions, as they reflect the fundamental principles underlying those systems.

25 Under Common law, the enactment of legislation that renders contractual performance illegal may constitute a valid *force majeure* event. However, this applies only where the clause's wording clearly allocates regulatory risk as a ground for relief,-typically through explicit references to "acts of government", "change of law", "illegality", or compliance with binding legal measures. In such cases, courts require the affected party to demonstrate that the supervening regulation has rendered performance legally impossible (not merely more onerous or commercially undesirable), that the illegality directly prevents performance within the meaning of the clause, and that any contractual obligations regarding notice or mitigation have been duly observed. Where these cumulative requirements are met, the clause will generally operate to excuse non-performance without liability.

26 These considerations are potentially applicable to arbitration litigation, since they are dependent on the body of law governing the contract, not the dispute resolution mechanism.