Gernandt & Danielsson

2022 Russian invasion of Ukraine

Potential contractual implications under Swedish law

Following a build-up of military forces along its border with Ukraine since the end of 2021, Russia began a full-scale invasion of Ukraine on 24 February 2022. The invasion is an escalation of Russia's war of aggression against Ukraine, which started in 2014 with the Russian invasion and temporary occupation of Crimea, and is the largest military attack on a European state since World War II.

Russia's invasion of Ukraine has caused tremendous human suffering in Ukraine, is in flagrant violation of Article 2(4) of the UN Charter, and should be condemned in the strongest possible terms. An overwhelming majority of 141 countries at the UN General Assembly have voted in favour of a resolution demanding that Russia "immediately, completely and unconditionally withdraw all of its military forces from the territory of Ukraine within its internationally recognized borders." The vote reflects the widely held view of the international community that Russia's invasion of Ukraine is unprovoked, unjustified, and illegal under international law.

Beyond its devastating humanitarian consequences, Russia's act of war may also have reverberations for businesses around the world, affecting their ability to perform contractual obligations. This may be a direct consequence of the on-going armed conflict on the ground, or indirectly because of the sanctions currently being imposed on Russian and Belarusian enterprises. In this article, we provide a brief overview of the available remedies under Swedish law in these circumstances.

Contractual regulation of the effects of an armed conflict

The main principle: the wording of the contract is governing

Introduction

Many international commercial contracts contain force majeure clauses, aimed at regulating the legal effects of unexpected events that may impede a party's performance. Other clauses, often referred to as hardship clauses, are aimed at regulating the effects of changed circumstances that may render the performance of a contract excessively onerous for one of the parties.

Swedish law recognises the principle that a party may be exempted from liability for non-performance if performance is impeded or rendered unreasonably burdensome due to unforeseeable circumstances beyond the party's control. However, the relevant statutory provisions – which we discuss in the next section – are non-mandatory, meaning that the contents of the parties' agreement take precedence. Indeed, under Swedish law, parties enjoy a broad freedom of contract, including the freedom to regulate the effects of particular events that may impede or render a party's performance more burdensome. Accordingly, if a contract includes a force majeure and/or a hardship clause, the parties' obligation to perform in situations of armed conflict will primarily be decided by interpreting such clauses and applying them to the relevant factual circumstances.

Force majeure clauses

A typical force majeure clause relieves the parties from performing their contractual obligations when certain unforeseeable circumstances beyond their control make performance impossible. The language of force majeure clauses vary. For example, the ICC Force Majeure Clause combines the predictability of listed force majeure events with a general force majeure formula that is intended to cover circumstances that fall outside the listed events.

In deciding whether a force majeure clause is applicable, a first issue is thus to determine whether a certain circumstance is beyond the invoking party's control. In the case of armed conflicts, this requirement would usually be fulfilled. The ICC model clause explicitly includes "war" and "invasion" among the situations that are presumed to fulfil this requirement.

A second issue is whether an armed conflict, or sanctions adopted because of such a conflict, falls within the categories of circumstances covered by the relevant clause. While there are virtually no Swedish statutes that provide guidance on how terms of a contract should be interpreted when the parties disagree about its contents, there is a tendency in case law to interpret clauses that discharge a party from liability narrowly. Hence, if a force majeure clause explicitly lists the situations that would trigger its application, then the list is generally regarded as exhaustive, unless the clause contains language to the contrary. That said, if events of war or sanctions are neither explicitly included nor excluded from the list, it may still be relevant to the construction and application of the contract, e.g. if the event is found to have rendered a contractual obligation unconscionable (see further below).

A third issue is whether the impediment due to the armed conflict was reasonably foreseeable. For instance, depending on the wording of the force majeure clause, contracts concluded at a time when the conflict was reasonably foreseeable may not permit a party to successfully invoke force majeure as a result of the foreseeable conflict.

If the requirements for successful invocation are fulfilled, one must determine the legal effects for the parties' respective obligations. Ultimately, the contractual implications vary and are inherently dependent on the wording of the force majeure clause. The consequences could include that a party may delay performance or be partially excused or entirely relived from performance. In some cases, the clause may allow a party to unilaterally terminate the agreement.

Hardship clauses

A typical hardship clause provides that a party is bound to perform its obligations even if events have rendered performance more onerous, except in cases where the relevant event fundamentally alters the equilibrium of the contract. Some of the requirements for hardship correspond with those often set out in force majeure clauses. For instance, it is often required that the event was beyond the invoking party's reasonable control and that the party could not reasonably have been expected to consider the event at the time of the conclusion of the contract.

Remedies available under a hardship clause vary considerably, ranging from the right to suspend performance or terminate the agreement, to the possibility of requesting a judge to modify the contract provisions with the purpose of restoring the equilibrium of the contract. As in the case with a force

majeure clause, the legal effects will ultimately depend on the wording of the hardship clause.

Tools available in extraordinary circumstances irrespective of the express regulation in the contract

The so called general clause in Section 36 of the Swedish Contracts Act, states that a contract term or condition may be modified or set aside if such term or condition is unconscionable having regard to, inter alia, subsequent circumstances and the circumstances in general.

As a general matter, *unconscionability* is a high threshold, and the purpose of Section 36 is not to rewrite a contract because a contractual term has become more difficult to comply with. Instead, Section 36 is an instrument to remedy an unconscionable imbalance in a contractual relationship. For example, if acts of war fall outside the scope of a force majeure clause, depending on the actual circumstances of the case, the commercial balance of the contract may be fundamentally disrupted. The impeded party may thus be able to argue that certain contractual provisions – *e.g.*, provisions regarding the time of delivery or the purchase price – have become unconscionable due to the war and con-sequently should be adjusted. It should be noted that when invoking Section 36, the counterparty often asserts that Section 36 is rarely used in commercial contracts. Although this is correct per se, the applicability of Section 36 is not limited to consumer relations and there are examples in case law where it has been applied in commercial contexts. Notably, Section 36 was applied by the arbitral tribunal in the high profile commercial arbitration between Naftogaz of Ukraine and Russian gas supplier Gazprom, to invalidate clauses that were found unconscionable to Gazprom's advantage.

The position under Swedish law in the absence of force majeure or hardship clauses

In respect of changed circumstances, some legal systems take the view that it is not the task of the judge or arbitrator to rewrite the parties' contract. Swedish law is not so dogmatic, and it is possible for a decisionmaker to find legal justification for modifying or supplementing the contract provisions.

If the contract lacks a force majeure clause, or if the wording of the clause does not support the view that it is invokable, it is uncertain to what extent optional law may fill the gap. The Swedish Sales of Goods Act (SSGA) as well as the United Nations Convention on Contracts for the International Sale of Goods (CISG)[1] both contain provisions regarding grounds for relief similar to force majeure. Section 27 of the SSGA and Article 79(1) of the CISG provide that a party may be exempted from liability for non-performance, if the impediment was unforeseeable and beyond the party's control and the party shows that it could not have avoided the impediment. Further, under Section 23 second paragraph of the SSGA, exemption from the seller's obligation to perform due to impediments, which he is unable to overcome, ceases if the impediment abates within a reasonable time. CISG lacks such a limitation; Article 79(3) of the CISG merely states that the exemption has effect for the period during which the impediment exists.

In addition, there may be other remedies under Swedish law that could be relevant in the absence of force majeure or hardship clauses, such as the doctrine of assumptions (Sw. *förutsättningsläran*). This doctrine essentially provides that a legal act (e.g., committing to a contractual obligation) may be annulled if undertaken on a premise not in accordance with the facts as they existed or as they would

1 The substantive provisions of CISG have been incorporated into Swedish law by the Swedish International Sale of Goods Act (Sw. lag (1987:822) om internationella köp).

subsequently appear and as a result, the act did not confer on the party expected benefits or entailed unforeseen burdens.

Implications for parties further down the contractual chain

In the context of complex transactions – as is often the case, e.g., in the construction sector – a party's ability to perform its obligations under a contract may depend on a third party in the supply chain. In such situations, the question is whether a disruption in the performance of the latter – e.g., a subcontractor or supplier – due to a force majeure event may constitute a ground for relief for a party up the chain.

In the first instance, this will be an issue of coordination of the relevant contract provisions, if any.

When the contractual chain is set up as a series of back-to-back transactions, all parties along the chain may be subject to the same contractual regulation of force majeure. In this case, a force majeure event excusing a party further down the chain would likely constitute a ground for relief up the chain as well.

However, when the treatment of force majeure in the contractual regulation along the supply chain is asymmetrical, the issue will require a more close analysis of the specific terms of the applicable clauses, together with a detailed analysis of the facts on the ground that actually caused the impossibility to perform.

Depending on the circumstances, the main contractor may risk being liable for, *e.g.*, a delay vis-à-vis its counterparty, without remedies against the contractor's delayed supplier. Conversely, the specific terms of the individual contracts may lead to the subcontractor being liable even when the main contractor is exempted. In such situations, it is important to keep in mind that the regulation under the respective party's insurance contracts might not correspond to that under the main agreements.

To the extent that the issue cannot be resolved through contract interpretation, or is not regulated at all in the relevant contracts, the answer may be sought in default rules under Swedish law, which may apply directly or by analogy. In this respect, Section 27 second paragraph of the SSGA provides that a seller will not be liable for damages for a delay in delivery, if the delay depends on a third party that the seller engaged to perform the sale in whole or in part. This applies also if the delay depends on issues with the seller's general suppliers. The liability exception, however, applies only in cases where the sub-contractor would itself be exempted from liability under the general rule on impediments in the first paragraph of Section 27, discussed above.

Article 79(2) of the CISG sets out a similar rule. Under that provision, a party may be exempted from liability if its failure depends on a third person whom that party has engaged to perform the whole or a part of the contract. This, however, presupposes that the contracting party is exempt under the main rule on impediments in Article 79(1) and that the third party equally would be exempted if said provision were applicable to it.

Gernandt & Danielsson's dispute resolution team

The firm's dispute resolution team have longstanding experience in representing clients in some of the largest and most complex Swedish and international disputes that have taken place in Sweden. We offer a dedicated and hardworking team of experts with solid experience in resolving disputes in different sectors in an effective and goal-oriented way and with a strong focus on the strategic considerations required in high profile and complex disputes. We have a long and successful history of working with fully integrated teams of experts in both dispute resolution and financial services to provide a holistic approach covering sanctions, ESG matters and compliance advice.

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