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THE IMPACT OF U.S. TARIFFS ON INTERNATIONAL SALES CONTRACTS

INTRODUCTION

The U.S. government's recent announcement of substantial tariffs affecting all trading partners, including Switzerland, has rocked the global economy and threatens to severely affect the stability of major international markets, including global stock markets.

The U.S. President defended the sweeping tariffs to be imposed on imports into the U.S. market with a remark that "sometimes you have to take medicine to fix something". These tariffs will be a bitter pill to swallow for the consumers, major corporations and entire economies.

Aside from a plethora of issues that arise from the wave of tariffs launched by the U.S. government on a political and macro-economic level, the question arises what consequences such tariffs have on the supply chains and – for the purposes of this article – on international sales contracts. Who bears the risk and financial burden of these import tariffs?

Further, could the unexpected nature of these tariffs provide grounds for modifying or excusing performance under international contracts (e.g. on the basis of force majeure or hardship)?

We will provide a brief overview on those questions from a Swiss law perspective, as well as from the angle of the United Nations Convention on Contracts for the International Sale of Goods (CISG), and the Incoterms 2020.

WHO BEARS THE RISK (AND COST) OF TARIFFS IN INTERNATIONAL SALES CONTRACTS?

Incoterms

The question of who bears the risk for paying tariffs in international sales contracts will primarily depend on the terms agreed upon between the buyer and seller. Thereby the Incoterms play a central role.[1]

Incoterms are standardized trade terms that clarify the obligations of both parties involved in contracts for the sale and purchase of goods.[2] The choice of a specific Incoterm depends on the specific trade requirements, mode of transport, and other aspects of the transaction negotiated between the parties. In international trade (particularly for marine traffic), the Incoterms FOB (Free on Board), CIF (Cost, Insurance, Freight), FAS (Free Alongside Ship), CFR (Cost and Freight), EXW (Ex Works) and DAP (Delivered at Place) are among the most commonly used, with FOB leading the statistics.[3]

How does the use of the Incoterms affect the risk allocation in terms of newly imposed tariffs? For instance:

- Under FOB (Free on Board), the buyer assumes responsibility for all import duties once the goods depart from the seller's country.[4]

- Similarly, if the contract provides for a CIF (Cost, Insurance, Freight) Incoterm, the buyer must cover any expenses that arise after the goods reach the destination port, including import taxes.[5]

- Differently, under DDP (Delivered Duty Paid), the seller is responsible for all duties and taxes, including the import tariffs.[6]

Therefore, the allocation of tariff costs can vary significantly, depending on the negotiated terms of the contract.

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1 Available at : https://incodocs.com/blog/who-pays-tariffs/#:~:text=Who%20pays%20the%20tariff%20can,Incoterm%20used%20in%20the%20transaction

2 Available at: https://iccwbo.org/business-solutions/incoterms-rules/

3 See e.g. here: https://www.agflow.com/wp-content/uploads/2021/05/Incoterms-Share-from-AgFlow-data-between-2010-01-01-and-now.jpeg.

4 Available at: https://incodocs.com/blog/who-pays-tariffs/; https://www.incotermsexplained.com/the-incoterms-rules/the-eleven-rules-in-brief/free-board/.

5 Available at : https://cargox.io/content-hub/cif-incoterms-your-guide-to-cost-insurance-and-freight-2024; https://www.incotermsexplained.com/the-incoterms-rules/the-eleven-rules-in-brief/delivered-duty-paid/.

6 Available at: https://incodocs.com/blog/who-pays-tariffs/.

Swiss code of obligations

Where the parties to an international sales contract have not made use of an Incoterm (and have not otherwise negotiated and agreed on the allocation of risk), from a purely Swiss substantive law perspective the following applies:

Absent any agreement or established trade custom between the parties, Articles 188 and 189 of the Swiss Code of Obligations (SCO) provide that: in principle, "the seller bears the costs of delivery, while the buyer bears the costs of acceptance."[7] Thereby, under Article 189(1) SCO, costs of acceptance include all expenses associated with the buyer taking possession of the goods in a distance sale, including transport, customs duties, taxes, fees, and transport insurance.[8]

However, Article 189(3) SCO provides that where delivery is agreed to be free of shipping costs and duties, the seller assumes export, transit, and import duties (though not the consumer taxes charged upon receipt of the goods).[9]

CISG

In international trade practice the above provisions of the Swiss Code of Obligations are of minor relevance. First, sophisticated parties will often have allocated the risks in their contract, e.g. by choosing an Incoterm. Second, in our experience, very often the parties choose the application of a law, without excluding the application of the CISG.

Under the CISG, there is no specific provision that explicitly assigns responsibility for import taxes to either the seller or the buyer. In the absence of any agreement between the parties, the starting point under the CISG – in line with the general principles underlying it as per Article 7(2) CISG – is that each party bears the costs of its own performance.[10] Accordingly, the seller bears the costs to the place of delivery, while the buyer bears the costs that arise thereafter, with the acceptance of the goods.[11]

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7 BSK OR I-Koller, Art. 188/189 N 1.

8 *Ibid.*

9 Available at: https://www.fedlex.admin.ch/eli/cc/27/317_321_377/en

10 Schlechtriem/Schwenzer/Schroeter, Commentary on the UN Convention on the International Sale of Goods (CISG), 2022, Commentary on Article 31, p. 548, para. 79; C. Brunner, M. Dimsey, Article 31 [Place of Delivery]', in Christoph Brunner and Benjamin Gottlieb (eds), Commentary on the UN Sales Law (CISG), Kluwer Law International, 2019, para. 13.

11 Schlechtriem/Schwenzer/Schroeter, Commentary on the UN Convention on the International Sale of Goods (CISG), 2022, Commentary on Article 31, p. 548, para. 79; C. Brunner, M. Dimsey, Article 31 [Place of Delivery]', in Christoph Brunner and Benjamin Gottlieb (eds), Commentary on the UN Sales Law (CISG), Kluwer Law International, 2019, para. 13.

This principle generally applies to taxes, customs and other charges that are incurred by import and export of the goods concerned.[12] Consequently, the general rule is that the seller bears the costs of export, while the buyer bears the costs of import.[13]

Having said that, as Article 9 CISG mandates that the parties are bound by any usage in international trade they agreed to or which they knew (or ought to have known) of, the Incoterms are likely to find application through the backdoor.[14]

Once it is established which party bears the risk of newly imposed tariffs, the question arises whether the party bearing the contractual risk may nevertheless raise a defense, including one of hardship or force majeure to escape its liability.

DO TARIFFS CONSTITUTE FORCE MAJEURE OR HARDSHIP?

Introduction

Whether the imposition of tariffs constitutes an event of force majeure (or hardship) will depend on the terms of the contract. International sales contracts and long-term supply agreements often include a force majeure clause defining the term and including a non-exhaustive list of potential events, which may or may not cover economic sanctions, changes in law or changes in trade regulations.

Similarly, M&A related agreements, joint venture agreements or supply and procurement agreements may contain a MAC (material adverse change) clause that provides for a mechanism to address significant changes in circumstances that could negatively impact a party's ability to perform its contractual obligations.

The two doctrines of force majeure or hardship should be distinguished:

- Force majeure generally refers to an extraordinary event or circumstances that prevent a party from fulfilling one or more of its contractual obligations under the agreement.[15]

[12] Schlechtriem/Schwenzer/Schroeter, Commentary on the UN Convention on the International Sale of Goods (CISG), 2022, Commentary on Article 31, p. 548, para. 80; C. Brunner, M. Dimsey, Article 31 [Place of Delivery]', in Christoph Brunner and Benjamin Gottlieb (eds), Commentary on the UN Sales Law (CISG), Kluwer Law International, 2019, para. 13.

[13] Schlechtriem/Schwenzer/Schroeter, Commentary on the UN Convention on the International Sale of Goods (CISG), 2022, Commentary on Article 31, p. 548, para. 80.

[14] W.P. Johnson, Analysis of Incoterms as Usage Under Article 9 CISG, p. 403 (available at: https://scholarship.law.slu.edu/cgi/viewcontent.cgi?params=/context/faculty/article/1343/&path_info=Analysis_of_Incoterms_as_Usage_Under_Article_9_of_the_CISG.pdf).

[15] See e.g., ICC force majeure clause: https://iccwbo.org/wp-content/uploads/sites/3/2020/03/icc-forcemajeure-hardship-clauses-march2020.pdf.

- The concept of hardship relates to extraordinary events that fundamentally alter the balance of the contract, rendering obligations excessively onerous, but not impossible to perform. Thus, a hardship situation typically exists when unforeseen events significantly disrupt the balance of the contract, either by increasing the cost of a party's performance or by reducing the value of the performance received by that party.[16]

Force majeure and hardship under the CISG

Article 79 CISG provides that a party is exempt from liability for non-performance only if three conditions are met: (i) the failure must result from an impediment beyond the party's control and risk; (ii) the impediment must have been objectively unforeseeable at the time of contracting; and (iii) it must have been impossible for the party to reasonably avoid or overcome the impediment or its consequences.[17]

It is suggested that the provision governs both concepts, cases of force majeure as well as scenarios of hardship.[18] The traditional doctrine of force majeure requires an impossibility of performance, typically including situations of physical (absolute) impossibility (e.g. where the specific goods are destroyed) or legal (subjective) impossibility (e.g. when the sale of goods is subject to embargoes, export or import restrictions).[19] The imposition of tariffs does not fall under these categories, but could theoretically constitute an economic impossibility, i.e., hardship.

Under Article 79 CISG, economic impossibility or hardship may justify an exemption from performance where unforeseeable and exceptional economic changes – such as a dramatic increase in costs – render contractual performance excessively burdensome.[20]

Thus, it is not sufficient for the performance to merely have become more burdensome. Ordinary commercial risks, including inflation or shifts in market value, generally fall within the performing party's sphere of risk. The party bearing that risk cannot, in principle, invoke such defenses of

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16 See e.g., Article 6.2.2 UPICC: https://www.unidroit.org/instruments/commercial-contracts/unidroit-principles-2010/chapter-6-section-2/#1623694323415-30641944-9988.

17 C. Brunner, Article 79 [Impediment Excusing a Party From Damages]', in Christoph Brunner and Benjamin Gottlieb (eds), Commentary on the UN Sales Law (CISG), Kluwer Law International, 2019, para. 4.

18 C. Brunner, 'Chapter 4: Force Majeure Excuse, Section 8: Individual Requirements of the Force Majeure Excuse under General Contract Principles, IV. Impediments', in Force Majeure and Hardship under General Contract Principles: Exemption for Non-performance in International Arbitration, International Arbitration Law Library, Volume 18, Kluwer Law International, 2008, p. 78-79.

19 C. Brunner, 'Chapter 4: Force Majeure Excuse, Section 7: The Force Majeure Excuse Under General Contract Principles, II. Recognition of the Force Majeure Excuse as a General Principle of Law', in Force Majeure and Hardship under General Contract Principles: Exemption for Non-performance in International Arbitration, International Arbitration Law Library, Volume 18, Kluwer Law International, 2008, p. 78-79.

20 C. Brunner, Article 79 [Impediment Excusing a Party From Damages]', in Christoph Brunner and Benjamin Gottlieb (eds), Commentary on the UN Sales Law (CISG), Kluwer Law International, 2019, para. 26.

hardship or force majeure, as the occurrence constitutes a manifestation of the very risk assumed under the contract.[21] Hence, only where performance has become "excessively burdensome" or "excessively onerous" the defense of the hardship exemption may apply.[22]

Whether this threshold is met must be determined on a case-by-case basis. Legal doctrine confirms that exemption under Article 79 CISG may be established if the "ultimate 'limit of sacrifice' has been exceeded".[23] In some cases, it has been found that "price fluctuations amounting to over 100 per cent do not yet constitute a ground for exemption".[24] Other cases indicate that a party may be exempt from liability under Article 79 CISG when unforeseeable events, such as a 70% increase in prices, render contract performance excessively burdensome. 25 Similarly, a case of hardship may be recognized where the burden of performance becomes so excessive that it borders on factual impossibility.[26] In light of the foregoing, case law and doctrine regarding the threshold of hardship are far from unified and vary depending on the specific facts of each case. Nevertheless, they indicate that a considerably high threshold must be met for the application of the hardship exemption under Article 79 CISG.

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21 C. Brunner, 'Chapter 4: Force Majeure Excuse, Section 8: Individual Requirements of the Force Majeure Excuse under General Contract Principles, II. Contractual Assumption or Limitation of the Risk of the Occurrence of Certain Impediments', in Christoph Brunner, Force Majeure and Hardship under General Contract Principles: Exemption for Non-performance in International Arbitration, International Arbitration Law Library, Volume 18, Kluwer Law International 2008, p. 117.

22 C. Brunner, 'Chapter 4: Force Majeure Excuse, Section 8: Individual Requirements of the Force Majeure Excuse under General Contract Principles, IV. Impediments', in Christoph Brunner, Force Majeure and Hardship under General Contract Principles: Exemption for Non-performance in International Arbitration, International Arbitration Law Library, Volume 18, Kluwer Law International 2008, p. 214.

23 Schlechtriem/Schwenzer/Schroeter, Commentary on the UN Convention on the International Sale of Goods (CISG), 2022, Commentary on Article 79, p. 1142 *et seq.,* para. 31.

24 Schlechtriem/Schwenzer/Schroeter, Commentary on the UN Convention on the International Sale of Goods (CISG), 2022, Commentary on Article 79, p. 1142 *et seq.,* para. 31 and references there (CIETAC, 2 May 1996, CISG-online 1067; Arbitration Court at the Bulgarian Chamber of Commerce and Industry, 12 February 1998, CISG-online 436; Commercial Court Hasselt, 2 May 1995, CISG-online 371; Cour d'appel de Colmar, 12 June 2001, CISG-online 694; Cour de Cassation, 30 June 2004, CISG-online 870).

25 Scafom International BV v. Lorraine Tubes S.A.S., Hof van Cassatie van België (Belgian Supreme Court), 19 June 2009, CISG-online No. 1963; Oberlandesgericht Hamburg, 28 February 1997, No 1 U 167/95, CISG-online 261 (despite the market price tripling since the original contract, the sale was not considered sacrificial because the deal was deemed highly speculative); C. Brunner, Chapter 5: Hardship (Change of Circumstances): Fundamental Change of the Equilibrium of the Contract, Section 12: Individual Requirements of the Hardship Defence', in Force Majeure and Hardship under General Contract Principles: Exemption for Non-performance in International Arbitration, International Arbitration Law Library, Volume 18, Kluwer Law International, 2008: an 80–100% loss in value or a 100–125% increase in cost (including profit margin) is generally seen as the threshold for hardship in common and civil law systems, "[h]*owever, it is again to be emphasized that the above thumbnail rule is only applicable to 'standard' situations, where the relevant risk has not wholly or partially been assumed by one of the parties*". Also, the author reminds that if performance would result in lasting financial ruin, a lower threshold may apply.

26 C. Brunner, Article 79 [Impediment Excusing a Party From Damages]', in Christoph Brunner and Benjamin Gottlieb (eds), Commentary on the UN Sales Law (CISG), Kluwer Law International, 2019, paras. 27-28.

In case of hardship, the aggrieved party is entitled to request the renegotiation or termination of the contract by its contractual counterpart.[27] However, such a request does not, in itself, exempt the aggrieved party from the performance of its obligations.[28] If the parties fail to reach an agreement, the aggrieved party may seek the adaptation or termination of the contract from the competent court or arbitral tribunal, provided this is permitted under the applicable law.

Force majeure and hardship under the Swiss Code of Obligations

Whilst Swiss substantive law does not contain an explicit provision governing force majeure, according to case law of the Swiss Federal Supreme Court the notion of force majeure (or "höhere Gewalt" in German) shall be understood as an event that is extraordinary, unforeseeable, unavoidable and that is not related to the operation of the liable party, against which the liable party was powerless, and which could not have been avoided even if it had taken all the precautions that could reasonably be required from it.[29]

An event will qualify as force majeure only under very restrictive circumstances. Similar considerations as mentioned above in relation to the high threshold under the CISG will apply.

If the impediment to fulfilling the contractual obligations in question is permanent, Article 119(1) SCO applies, pursuant to which the obligations are deemed extinguished.[30]

Where the performance of a contractual obligation would become excessively burdensome for one party because of significantly changed circumstances, under Swiss substantive law the party may seek relief from the courts based on the doctrine of clausula rebus sic stantibus. Based on this doctrine the affected party may either request that the terms of the contract be amended by the court or that the contract be terminated.

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27 C. Brunner, 'Chapter 5: Hardship (Change of Circumstances): Fundamental Change of the Equilibrium of the Contract, Section 13: Legal Effects of Hardship', in Christoph Brunner, Force Majeure and Hardship under General Contract Principles: Exemption for Non-performance in International Arbitration, International Arbitration Law Library, Volume 18, Kluwer Law International; Kluwer Law International 2008, p. 479.

28 C. Brunner, 'Chapter 5: Hardship (Change of Circumstances): Fundamental Change of the Equilibrium of the Contract, Section 13: Legal Effects of Hardship', in Christoph Brunner, Force Majeure and Hardship under General Contract Principles: Exemption for Non-performance in International Arbitration, International Arbitration Law Library, Volume 18, Kluwer Law International; Kluwer Law International 2008, p. 487.

29 See e.g. DFSC 102 Ib 257, para. 5

30 Article 119 SCO states:

> ***1*** *An obligation is deemed extinguished where its performance is made impossible by circumstances not attributable to the obligor.*
> ***2*** *In a bilateral contract, the obligor thus released is liable for the consideration already received pursuant to the provisions on unjust enrichment and loses his counterclaim to the extent it has not yet been satisfied.*
> ***3*** *This does not apply to cases in which, by law or contractual agreement, the risk passes to the obligee prior to performance.*

Regarding the U.S. tariffs

The tariffs announced by the US government as well as the corresponding retaliatory tariffs of other countries raise difficult questions about whether such actions constitute force majeure or hardship. At the date of the issuance of this short article the exact level of the tariffs is not yet certain as the U.S. President has decided to suspend the tariffs for a 90-day period. It is yet to be seen at what level the import tariffs for each country will end up.

In general, unless specified in the agreement, increased performance costs, including those resulting from governmental actions, typically do not qualify as force majeure or hardship. This is because increased costs alone are generally not considered an insurmountable obstacle, and neither may they be sufficient to make performance excessively burdensome.

From a Swiss law perspective, the initially announced (yet uncertain) 31% to 32% increase in tariffs, would be unlikely to qualify as a force majeure event, as it does not render contractual performance objectively impossible.

However, if the increase in tariffs was entirely unforeseeable at the time of contracting and results in a substantial economic imbalance to make performance excessively burdensome, such an increase may arguably constitute a case of hardship. Depending on the applicable law, the affected party could potentially be entitled to invoke Article 79 CISG or rely on the doctrine of clausula rebus sic stantibus, seeking a modification of the contract terms in order to restore the contractual equilibrium (similar to a MAC clause, or price review clauses found in long-term supply agreements). In exceptional cases, a court may even decide to terminate the contract.[31]

Conclusion

In conclusion, the imposition of U.S. tariffs on Swiss imports raises complex issues regarding the allocation of financial risk and the potential for invoking force majeure or hardship defenses.

The contract terms agreed by the parties – which in international trade will often be the Incoterms – will determine which party essentially carries the risk of import tariffs.

While the tariffs may not meet the strict criteria for force majeure under either the Swiss Code of Obligations or the CISG – since they do not render performance impossible –, the imposition of new tariffs may lead to a significant disruption of the contractual balance of the parties' obligations. Depending on the extent of the increase, such disruption may qualify as hardship.

[31] This is very similar to the remedies available e.g. under Section 36 of the Swedish Contract Act.

The parties are well advised to carefully review their contract to determine whether it contains any provisions governing such disruptions, including force majeure, hardship, or a MAC clause.

Ultimately, the application of force majeure or hardship provisions will depend on the foreseeability of the tariffs and the severity of their impact on the specific contractual framework governing the trade relationship. Only where such tariffs render performance impossible or excessively burdensome may a party successfully raise a defense and seek relief from liability.

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