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**Conditional contracts: authorising potestative conditions**

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I. Conditional contracts are of high interest and importance for business relations since their aim is to protect entrepreneurs rights. Each businessman wishes to condition its obligations introducing a particular event or an act to be done in order to either be bound by a treaty only when it becomes beneficial upon occurrence of a condition (condition precedent); or release himself from inconvenient contract if the condition will or will not occur (condition subsequent).

A great variety of conditions could be found in present-day contracts. However, not all of them are permitted by law. Most legal systems tend to prohibit potestative conditions, *i.e.* those depending on the will of the parties, authorizing primarily only events of the physical world as a condition.

Such prohibition is not justified, since actions of the parties themselves are often needed to represent conditions in order to protect someone interest. All potestative conditions should be authorized for the best interest of the business world.

II. A conditional contract refers to a contract containing provisions on conditions. Depending on the legal system of a particular country one may refer to a conditional contract or to a conditional obligation. The idea remains the same: a particular obligation under the contract or a particular provision of a contract may be made conditional upon the occurrence of an uncertain event in future.

The dispute arises when it comes to the question what a "condition" may be? The notion "condition" should be defined as "act subsequent to acceptance and prior to discharge, a fact upon which the rights and duties of the parties depend" (Corbin, 1919).

It is generally accepted that such a fact may be an event of the physical world, which occurs accidentally and is independent on the will of parties. As to the actions of the parties themselves, it is highly arguable whether or not the parties may contribute to the occurrence of a "condition". That is one of the most controversial issues in Russian court practice, where there are both judgments in favor of such conditions and those against them.

Such inconsistent court practice leads to ambiguity in application of Article 157 of Russian Civil Code regulating conditional contracts. The Article only provides the definition of both condition precedent and subsequent and prohibits abusive contribution to the occurrence or non-occurrence of a condition. Accordingly, the law itself does not expressly prohibit or authorize actions of the parties to be a condition.

III. As was mentioned *supra*, potestative conditions refer to those depending on the will of parties. For instance, Tom and Jack have agreed that Tom would sell his shares only after Jack would get the credit. Tom's obligation to sell is conditioned upon Jack's performance, making this condition potestative. At first sight, this condition seems to protect interests of both parties: Tom is sure that he gets money for his shares since he won't sell it until Jack gets the credit; Jack is sure that he assumes the burden of loan in exchange of Tom's shares.

However, if their agreement provides that Jack is an exclusive buyer of Tom's shares, meaning that Tom may not offer these shares for a sale to a third party despite abnormal delays from the part of Jack in getting the loan, then Tom's rights are highly violated. Jack

may use this situation to prevent the sale of shares.

Here's another example of violation of Tom's interest. Tom's obligation to sell his shares becomes effective upon obtaining the credit. This means, that once Jack gets his loan, Tom is under obligation to sell the shares. Meanwhile Jack may return the credit, since it is not expressly said, that Jack shall pay for Tom's shares using this particular loan.

In other words, provision on conditions shall not infringe interests of the parties. For this reason, most legal systems, *inter alia* French Civil Code, the Civil Code of Louisiana, US and UK case law, expressly prohibit the so-called purely potestative conditions, *i.e.* conditions that are in sole discretion of one of the parties, especially of the obligor, providing that not only a provision containing such purely potestative condition is null, but the whole contract is so.

Prohibiting only purely potestative conditions those legal acts and case law thereby authorize other potestative conditions referred to as "simple" and face a new problem: how those types of potestative conditions shall be distinguished. Professor Vernon Palmer and Mr. Andrew Plauche in their article, *A review of the Louisiana Law on Potestative Conditions* suggest a "reasonable man" test to distinguish the purely from the simply potestative conditions.

"Under this test, the courts inquire into the intention behind a contract clause that on its face gives one party an arbitrary option to perform, to determine whether, in fact, the obligation is conditioned purely upon arbitrary will of one of the parties".

Accordingly, the parties may include any potestative conditions, either pure or simple, in their agreement, and only when a dispute between them arises the court will assess whether or not those particular conditions are under prohibition or not, declaring the treaty void or effective.

IV. It is reasonable to assume that if simply potestative conditions do not render the treaty or particular obligation void then, *a fortiori*, mixed conditions, containing elements of both purely and simply potestative conditions will not equally void an obligation or a treaty. This idea was stressed by Palmer and Plauche in their work mentioned *supra*.

The meaning of a mixed condition is revealed in the Civil Code of Louisiana which states that such a condition "depends at the same time on the will of one of the parties and on the will of a third person, or on the will of one of the parties and also on casual event".

Accordingly, the abovementioned agreement on sale of shares between Tom and Jack is not void, since obtaining of the loan in question depends not only on the will of Jack, but also on the will of a bank. It is for the parties, in such a case, to include in their agreement provisions for protections of Tom's interests or leave it on the discretion of the court in the case of conflict, assuming that parties, generally, are expected to act in good faith.

What is crucial is that potestative conditions, even those depending mainly on the will of one party, may exist if there is something to put on the other scale. This is also a case of a contract known as "option".

An option is always an offer, usually an offer to buy or to sell property, which creates a power in the option-holder. It is a contract containing potestative conditions that provides the right of the option-holder to unilaterally decide whether or not the final contract will be concluded. The effect of option is usually limited in time. Shall the option-holder decide not to conclude the contract, he or she has to pay an indemnity to the option-giver.

An option is a contract containing purely potestative condition, since it is always for one party to decide on the conclusion of final contract, the decision being a condition. However, this purely potestative condition is mixed with other provisions, namely time-limit and indemnity

for refusal, that balance position of the parties and their interests.

Therefore, it is not reasonable to prohibit all potestative conditions, even those of pure nature, since they may serve for the best interests of contracting parties. The best solution is to limit purely potestative conditions authorizing those of them that are balanced under the contract.

V. In the light of recent amendments to the Civil Code of the Russian Federation it should be noted that Russian legislator has generally authorized potestative conditions introducing new Article 327.1. The Article provides that performance of obligations as well as exercising, alteration or termination of particular rights under a treaty might be conditioned upon the action (or inaction) of one of the parties or upon the occurrence of other circumstances provided by the treaty, including those that are fully dependable upon the will of one of the parties.

First, Article 327.1 seems to be a directions for those judges who decide against potestative conditions, a direction that such conditions should exist and be authorized. Besides that, the need to introduce new Article codifying basically the same Article 157 does remains unclear.

Second, the new Article authorizes purely potestative conditions without any restrictions as to abusive actions. The famous formula of dangerous purely potestative condition that is in sole discretion of the obligor "I will pay when I wish" is therefore not limited. Whether para.3 of Article 157 would be applicable to such situations? It is difficult to say yet. In any case, an advice for the parties is to balance their rights and interest by introducing other terms, such as indemnity.

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