PRACTICAL
GUIDELINES

DRAFTING CONTRACTS IN LEBANON DURING HYPERINFLATION: PREVENTIVE CLAUSES

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"An excellent paper, which is both practical and scholarly, on this crucial topic"

Philip Wood, CBE, KC hon, author of the *Law and Practice of International Finance* series, formerly visiting professor and distinguished visiting fellow at Oxford, Cambridge, the London School of Economics & Political Science, Queen Mary, and London.

I dedicate this paper to the memory of my Mentor honorable Judge Antoine BRIDI. I am indebted to my wife Judge Samar Bouhairi for the helpful comments she provided on the final draft of this piece.

ABSTRACT

The current financial crisis put Lebanon in second place for the highest inflation rates in 2022 after Sudan. The Lebanese currency i.e., LBP lost more than 95% of its purchasing power and depreciated to the extent where the Exchange Rate reached LBP 40,000 per US dollar after remaining equal to LBP 1507.5 per US dollar between December 1997 and October 2019.

The collapse of the Lebanese currency i.e., LBP had catastrophic impact on creditors whose contractual obligations are denominated in LBP and on debtors (especially whose income is in LBP) whose contractual monetary obligations are denominated in US dollar. As for the creditor whose debt is 15 million LBP for instance, he suffered a fall in the value of that debt which is worth now 375 US dollar while it was worth 10,000 US dollar before 2019. The same applies to the debtor whose debt is 1000 US dollar for example, who found the value of his debt increasing from 1,5 million LBP before 2019 to 40 million LBP nowadays.

The main concern of contractual creditors in Lebanon currently is to be reimbursed in cash US dollar by undertaking fast dispute settlement proceedings. Taking into consideration the current legal and jurisprudential context, creditors are advised to insert foreign currency clauses in addition to some or all of the following clauses: jurisdiction clauses, arbitration clauses, governing law clauses, cross-border payment clauses, contractual exchange rate clauses, lollar clauses and bira clauses. In certain circumstances, gold clauses and indexation clauses could provide the minimum level of protection.

▪ Introduction

1. In October 2019, Lebanon plunged into an unprecedented fiscal and economic crisis that put him "in 4th place for the highest inflation rates in 2020 preceded by Venezuela, Zimbabwe and Sudan; and in 3rd place in 2021, after Venezuela and Sudan"[1] and "in second place in 2022 after Sudan"[2]. This crisis cannot be attributed to any of the conventional causes of hyperinflation i.e., social unrest, foreign military invasion or money oversupply and it is not clear yet what first triggered the sharp fall of the Lebanese pound (henceforth "LBP")[3]. However, it is obvious that the collapse of the banking[4] system which was affected by an unbalanced -still ongoing- outflow of foreign currency deposits led to a severe shortage of US dollar banknotes in circulation and to the loss of trust in LBP.

2. So far LBP lost more than 95% of its purchasing power and got depreciated to the extent where the Exchange Rate (henceforth "ER") exceeded LBP 39,000 per US dollar after remaining equal to LBP 1507.5 per US dollar between December 1997 and October 2019. This collapse had catastrophic impact on creditors whose contractual[5] and legal[6] monetary obligations are denominated in LBP and on debtors (especially whose income is in LBP) whose contractual[7] and legal[8] monetary obligations are denominated in US dollar. As for the creditor whose debt is 15 million LBP

[1]World Bank. 2022. Lebanon Economic Monitor, Fall 2021: The Great Denial. World Bank, Washington, DC. © World Bank. https://openknowledge.worldbank.org/handle/10986/36862 License: CC BY 3.0 IGO, page 15.

[2]https://www.fitchsolutions.com/country-risk.

[3]The legal name of the Lebanese currency is "the Lebanese Lira".

[4]This collapse has not been crystallized yet by an official declaration of bankruptcy of banks.

[5]The creditors are mainly -among others- the banks that provided subsidized loans (mortgages).

[6]The creditors are mainly the Government (taxation and public utility rates) and the public servants (wages and pensions).

[7]In the highly dollarized Lebanese economy, inserting foreign currency clauses was a common practice in drafting contracts.

[8]Law No. 302 dated on 8 August 2022 states that airport fees and port tariffs are collected exclusively in cash US dollar; Law No. 57/2017 indicates that all companies that have petroleum rights should pay taxes in US dollars or in Euros or in LBP according to "highest exchange rate" issued by the central bank; Basic circular of the Lebanese Central Bank No. 86 of 20 September 2001 entitled "compulsory banks' investments" obliges banks to deposit at the central bank a specific percentage of their foreign currency deposits. It is worth mentioning that the Governor of the Central Bank sent on 11 May 2022 letter No. 1399/1 to the president of the Association of Banks in Lebanon and informed him that the Central bank is entitled to pay back "the compulsory investments" to banks "in LBP according to the exchange rate of LBP to US dollar" and not in US dollar.

for instance, he suffered a fall in the value of that debt which is worth now 375 US dollar while it was worth 10,000 US dollar before 2019. The same applies to the debtor whose debt is 1000 US dollar for example and who found the value of his debt increasing from 1,5 million LBP before 2019 to 40 million LBP nowadays.

3. This piece does not tackle legislative and judicial solutions directed to the problem of drastic impact of hyperinflation on contractual monetary obligations; however its scope is limited to the preventive measures that parties should take when they enter into contracts during hyperinflation. The following discussions are useful to advise the parties and draft their contracts in such manner that will protect them where possible from the adverse effects of inflation. Taking into consideration the current legal and jurisprudential context, creditors are advised to denominate their obligations in US dollar[9] and therefore to insert foreign currency clauses in addition to some or all of the following clauses: jurisdiction clauses, arbitration clauses, governing law clauses, cross-border payment clauses, contractual exchange rate clauses, lollar clauses and bira clauses. In certain circumstances, gold clauses might be useful. Finally, if the parties denominate their obligations in LBP, they are advised to insert indexation clauses[10].

▪ Legal and jurisprudential context

4. As it will be discussed, the classic scenario in Lebanon nowadays concerns two categories of contractual parties: debtors whose contractual monetary obligations are denominated in US dollar (henceforth "the US dollar debtors") and creditors whose contractual monetary obligations are denominated in LBP (henceforth "the LBP creditors").

1- The US dollar debtors offer to discharge their devalued debts by paying in LBP at the lowest ER i.e. the Average ER (henceforth "AER") while their creditors (henceforth "the US dollar creditors")

[9]The US dollar is selected for example purposes. Having in mind the constant depreciation of the US dollar, the author considers that a basket of foreign currencies (US dollar, Canadian dollar, Swiss franc, Euro …) is a better option for several reasons that are outside the scope of this paper.

[10]Often in this paper there will be recommendations to insert those clauses in order to enable the creditor to receive eventually the payment in cash US dollar, based on an assumption that the judgment/arbitral award is rendered in favor of the creditor.

insist on getting paid in US dollars and contest the validity of payment in LBP and, by extension, demand a payment at the highest ER. In internal contracts, courts give the US dollar debtors the option of paying either in US dollar or in LBP. However in international contracts, courts exonerate US dollar debtors only when they pay in US dollar.

2- The LBP creditors insist on receiving their debts after being revalorized, while their debtors (henceforth "the LBP debtors") offer to pay the amount as determined in the contracts. In this case, courts apply the principle of nominalism and render judgments in favor of the LBP debtors.

- **Internal contracts**

5. While certain authors[11] consider foreign currency clauses void in internal contracts, others[12] find them not only valid but binding to the debtors who are obliged therefore to pay in foreign currency and not in LBP. Jurisprudence[13] has always considered those clauses valid and since 17 October 2019 the US dollar creditors have been incurring huge losses due to judgments[14] that allowed -in their vast majority- US dollar debtors to exonerate themselves by paying in LBP at AER in a defacto chaotic multiple exchange rate system.

- **Multiple Exchange Rates** [15]

[11]Bechara Karam, "Le paiment des obligations monétaires en monnaie étrangère en droit libanais: Une relécture de l'alinéa 2 de l'article 301 COC", Revue juridique de l'USEK 2020, n. 20, p. 7-41; Available on https://www.usek.edu.lb/Content/Assets/20201228BecharaKaram.pdf. Dr. Karam explains that article 301 (paragraph 2) of the Code of Obligations and Contracts does not allow foreign currency clauses and this in the light of the judgment of the French Court of Cassation (17 may 1927). See also مرسال سيوفي، "التعاقد بالعملة الاجنبية"، مجلة العدل 1993، صفحة 25 وما يليها. See also سامي منصور، عنصر الثبات وعامل التغيير في العقد المدني، دار الفكر اللبناني، 1987، صفحة 197 وما يليها. In those publications, Lights are shed on the Lebanese jurisprudence that does not void foreign currency clauses and allows the US dollar debtor to pay either in US dollar or in LBP.

[12]Available on ; نجيب الحاج شاهين، "إيفاء الديون المحررة بالعملة الأجنبية في العقود الداخلية"، المجلة القضائية/دراسات وآراء https://lebanon.saderlex.com/category/. Professor Hage-Chahine considers that foreign currency clauses are valid and binding to the creditor who cannot exonerate herself by paying in LBP. The analysis is focused on restrictive interpretations of article 301of the Code of Obligations and Contracts and articles 6 and 7 of the Code of Money and Credit.

[13]Judgment No.38/1989 rendered on 16 October 1989 and Judgment rendered on 26 November 1993 by the Court of Appeal of Beirut, published in137 صفحة ،1993 مجلة العدل; Judgment rendered on 29 January 1973 by the Court of Cassation (first chamber), published in 150 صفحة 1973 باز; Judgment No.4 rendered on 10 January 1951 by the Court of Cassation, published in 369 صفحة 1951 النشرة القضائية (In this judgment, the court considers the foreign currency a commodity).

[14]Courts have not so far voided any foreign currency clause.

[15] An analysis of the different ERs applicable in Lebanon is made by the author in his article "Hyperinflation in Lebanon: the exchange rate dilemma", Lexis Nexis / MENA Business Law Review, N. 02/2021; Available on www.linkedin.com/in/mohamad-fawaz-15099320. The Civil District Judge in Beirut (commercial affairs) expressly refers to this article in her Judgment No.62/2021 rendered on 26 October 2021). See also Bechara Karam, "A la recherche du taux perdu: Réflexions sur le taux de change dans le paiement des dettes monétaires libellées en devises", Revue juridique de l'USEK 2020, No 21, p. 7-45; Nadine Najem, "Le paiement des dettes libellées en dollars devant les tribunaux libanais", Horizons du droit - Revue de l'Association Francaise des Docteurs en Droit, Bulletin No. 35 – avril 2022, p. 18-39. See also, ندیم رعد، "انخفاض النقد، ومصير الالتزام النقدي في القانون اللبناني"، مجلة العدل سنة 1992 صفحة 59 وما يليه (in this paper, Mr. Raad considers that since 1973 there is no fixed legal ER for LBP against the US dollar).

6. The Lebanese Central Bank (*Banque du Liban*) (henceforth "BDL") through its circulars plays a major role in setting most of the ERs that are being applied in the everyday life of the Lebanese people. The current crisis led to the proliferation of seven ERs, namely:

(i) the AER of 1507.50 LBP per US dollar[16],

(ii) the Electronic Platform ER of LBP 8,000 per US dollar (henceforth "E-platform ER")[17],

(iii) the ER of LBP 12,000 per US dollar[18],

(iv) the "SAYRAFA" electronic application fluctuating Exchange Rate (henceforth "SAYRAFA ER"), that exceeds currently LBP 29,000 per US dollar[19].

(v) the "student dollar" ER 1500 LBP per US dollar (henceforth "Student Dollar ER")[20],

(vi) the Emergency Crisis and COVID-19 response Social Safety Net project ER(henceforth "ESSN ER"),[21] and

(vii) the black market fluctuating ER that is currently LBP 40,000[22] per US dollar.

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[16]It used to be the equilibrium price of a one dollar US bank note in LBP at the closure of the daily trading session of foreign currencies between BDL and commercial banks during the period of 1997-2019. Although BDL is not entitled to set an ER and is allowed only to declare and publish the AER resulting from its daily trading of US dollars with commercial banks, It nevertheless issued circulars and set the AER as a fixed ER to be applied in its operations with commercial banks and in the operations undertaken by those banks with their clients (basic circular No. 148 dated on 3 April 2020).

[17]Intermediary Circular No. 13277 dated on 9 December 2021.

[18]Basic circular No. 158 of 8 June 2021 and intermediate circular No. 626 of 21 June 2022. According to these circulars, the depositor is allowed to receive on a monthly basis 400 cash US dollar and the equivalent of this amount in LBP at the ER of 12,000 LBP per US dollar.

[19]Basic Circular No.5 of 10 April 2020, Intermediary Circular No. 583 of 10 May 2021 and Basic Circular No. 157 of 10 May 2021. BDL has required the most influential stakeholders in the foreign currency exchange market (commercial banks and exchange bureaus) to trade US dollars and foreign currencies on a platform that is supposed to be more transparent than the black market i.e., the SAYRAFA application. BDL publishes SAYRAFA ER on a daily basis.

[20]Law No. 283/2022 issued on 12 August 2022 (the previous student dollar law is Law n.193 issued on 16/10/2020).

[21]Law No. 219 of 8 April 2021. Paragraph C – schedule 2 – of the agreement stipulates that "as long as there is an official peg between the US dollar and LBP, the beneficiaries will receive cash transfers in LBP at the higher of: (a) the constant real exchange rate, and (b) the highest regulated exchange rate vis-à-vis the US dollar, plus sixty percent, such rate being determined in consultation with BDL and adjusted on a regular basis."

[22]According to the current speculations it will reach LBP 50,000 per US dollar before the end of 2022.

7. In all the judicial proceedings pending before Lebanese courts where the main demand is the payment of a contractual monetary obligation denominated in US dollar in internal contracts, the two key questions are the following:

(i) under Lebanese law, can contractual monetary obligations denominated in US dollars be paid in LBP; and
(ii) if yes, at which ER?

Since October 17th 2019, the Court of Cassation has rendered only one decision relevant to the ER matter where it applied "the market rate" without specifying it and with no legal justification[23]. Most of the cases are still pending before first and second instance courts. So far, almost all[24] of the judgments rendered[25] have considered payment in LBP of a contractual monetary obligation denominated in US dollar[26] to be valid. The reasoning in these judgments is mainly based on Article 30 [27] of the Code of Obligations and Contracts,[28] Articles 7[29] and 192[30] of the Code of Money and Credit,[31] and Article 767[32] of the Penal Code.[33] However, courts have

[23] Judgment No.14/2022 rendered on 12 April 2022 by the Court of Cassation, 2nd Chamber.
[24] One judgment considered that obligations denominated in US dollar (in an internal contract) should be paid in this currency and not in LBP: judgment No. 199/2019 rendered on 25/11/2019 by the judge of urgent affairs in Nabatyeh.
[25]Judgment No.17/2021 rendered on 15 April 2021 by the Civil District Judge in Beirut (commercial affairs); Judgment No.7/2019 rendered on 26 October 2020 by the President of the Court of Appeal of Beirut, 12th Chamber; Judgment rendered on 15 April 2021 by the Civil District Judge of Tripoli (Commercial and Financial Affairs); Judgment No.289/2020 rendered on 1 December 2020 by the Civil Court of First Instance of Beirut, 5th Chamber (Commercial and Financial Affairs); Judgment rendered on 12 November 2020 by the Execution Judge of Beirut; Judgments No.160/2020 rendered on 14 October 2020 and No.167/2020 rendered on 28 October 2020 by the Execution Judge of Beirut.
[26]Courts would probably take a different position in cases where Articles 432 and 356 of the Code of Commerce are to be applied. Those articles allow respectively the drawer of a banker's check and of a bill of exchange to ask the drawee to pay either only in a foreign currency or only in LBP according to a determined ER. If this condition is not mentioned, the payment will be made in LBP according to the market ER as determined by the Lebanese custom.
[27]"When the debt is an amount of money, it should be paid in the currency of the country. In normal time, and when inconvertibility has not been established for fiduciary money, the contracting parties remain free to agree that payment could be made in a specific metallic currency or a foreign currency." The original French version of the article is to be taken into consideration because its Arabic translation is inaccurate.
[28]Law dated on 9 mars 1932 .
[29]"Banknotes of a value of 500 pounds and over shall be unlimited legal tender throughout the Lebanese territory."
[30]"Refusal to accept Lebanese money within the framework of conditions laid down in articles 7 and 8 is subject to penalties listed in article 319 of the Penal Code."
[31]Decree No. 13513 of 8 January 1961.
[32]"The person who refuses to accept national currency shall be liable to a fine that ranges between 1000 and 10000 LBP."

not shared the same view on the ER matter; while most of them applied AER, several others[34] have applied the SAYRAFA ER.

Unless the Parliament enacts a law that expressly sets a legal ER that should be applied on all different types of contractual monetary obligations, it is unlikely that courts will settle the disputes relevant to internal contracts pending before them according to an ER different from AER. But in all cases, most of the courts will always consider the payment in LBP of a contractual monetary obligation denominated in US dollar to be valid: a creditor whose debt is 1000 US dollar will receive the amount of 1,500,000 LBP instead of an amount that could exceed 40 million LBP because courts will apply AER i.e. LBP 1500 per US dollar instead of the black market ER that is around LBP 40,000 per US dollar.

- **International contracts**

8. In international contracts, courts implement foreign currency clauses and allow the creditor to receive her debt in foreign currency. *"This rule [the payment in foreign currency cannot be imposed and the payment in national currency cannot be refused] is only applicable in internal contracts"* [35]. "*The [French] court of cassation allowed the creditor to ask the debtor to pay his debt in foreign currency as long as this was their will expressed in an international contract within the meaning of monetary theory".*[36]

9. International Private Law sets out two necessary criteria for the characterization of an international contract. The legal criterion takes into account subjective factors (nationality of the parties and place of residence) and objective factors (the language of the contract, currency of payment,

[33]Decree-Law No. 340/1943.

[34]Judgment No.62/2021 rendered on 26 October 2021 by the Civil District Judge in Beirut (commercial affairs); Judgment No.611/2021 rendered on 26 October 2021 by the Court of Appeal of Beirut, 9th chamber; Judgment No.24/2022 rendered on 22 February 2022 by the Court of First Instance of Beirut (financial affairs); Judgment rendered on 28 April 2022 by the president of the Court of Appeal of Beirut, 12th chamber (this judgment refutes the opinion of professor Hage-Chahine previously referred to in footnote No. 12), Judgment No.427/2022 rendered on the 6th of September 2022 by the Court of Appeal of Beirut, 11th chamber (rent affairs).

[35]Judgment No.180/2020 rendered on 30 December 2020 by the Execution Judge in Beirut, page 7.

[36]Yvon Loussouarn et Pierre Bourel, Droit international privé, Dalloz, 7ème édition, 2001, page 476.

place of performance of the obligations and the place of conclusion of the contract). As for the economic criterion, the main decisive element would be the correlation between the contract and international trade[37]. Whenever the economic criterion is satisfied, it is assumed that the contract is international; however the same cannot be said about the legal criterion. Therefore, once a contract involves "international payments" it is considered an international contract[38]. Along this same line of thoughts, it is of interest to see that the legislator himself considers that arbitration is international if it satisfies the economic criterion. Hence, Article 809 of the Code of Civil Procedures (Henceforth "CCP") reads "The arbitration is considered international when it involves the interests of international trade".

▪ Nominalism

10. When parties enter into contracts payable in LBP, it is logical to presume that a party has assumed the risk of inflation. In the current circumstance where LBP collapsed, judges have to rule in cases where LBP creditors demand the payment of revalorized depreciated contractual monetary obligations. While English law[39] adopts nominalism in the Case de Mixt Moneys (Gilbert v Brett)[40] and prohibits the intrusion of the judge to readjust the balance in contracts affected by inflation, French law[41] and laws

[37] سامي منصور، مرجع سبق ذكره، صفحة 153 وما يليها.

[38] Judgment rendered on 11 May 1955 by the State Council published in النشرة القضائية سنة 1955 صفحة 639; see also Yvon Loussouarn et Pierre Bourel, op cit page 477 "...pour qu'un payment puisse bénéficier de clauses de guaranties de change, il faut qu'il soit lié à un contrat international impliquant une circulation internationale de valeur, un "flux et reflux au-dessus des frontières". Il en est ainsi par exemple dans un emprunt, lorsqu'un Etat, une société ou un particulier, emprunte à l'étranger des fonds qu'il utilisera dans son pays de telle sorte que le prêteur devra normalement recevoir son remboursement de l'étranger ou aller l'y chercher, ou bien lorsque l'emprunteur qui émet le prêt dans le pays de son siège social à son centre d'exploitation dans un autre, de telle sorte que la somme empruntée est affectée naturellement à un emploi à l'étranger … En vertu du critère économique retenu, le caractère de contrat ou de règlement international est en effet reconnu à des contrats qui pourtant, parce qu'ils ne présentent pas d'élément d'extraneité, doivent *être* du point de vue du conflit de lois, considérés comme des contrats internes et soumis à ce titre à la loi francaise ".

[39] Mohamad Fawaz, Hyperinflation in England: The Aftermath, Sweet & Maxwell Ltd, 2016. The book explains the four different Legal techniques that can be used by English Courts to avoid the catastrophic effect of nominalism on contracts governed by English Law in case of collapse of sterling pound.

[40] (1604) Davies 18; 2 State Trials 114. The verdict reads "although at the time of the contract and obligation made…pure money of gold and silver was current within this Kingdom…yet the mixed money being established in this Kingdom before the date of payment may well be tendered in discharge of the said obligation and the obligee is bound to accept it."

[41] Article 1195 of the French civil code reads "In case a change in circumstances, unforeseeable at the time of conclusion of the contract, makes performance excessively onerous for a party who had not agreed to bear the risk, that party may request the other party to renegotiate the contract. It shall continue to perform its obligations during the renegotiation. If the renegotiation is rejected or fails, the parties may agree to

of other States[42] expressly adopt valorism and hence entitle the courts to implement the necessary change to those contracts.

11. Under Lebanese law**,** nominalism is still the applicable rule. Although there is no article which expressly states that the debtor must repay only the numerical sum lent in the lawful currency at the time of payment, however the two founding principles of the Lebanese contract law i.e. freedom of contract[43] and binding character of contracts[44] led the courts to adopt nominalism[45] and not to run the risk of undermining transactional security.

12. Nevertheless, legislative intervention with respect to inflation is not entirely absent. These rare interventions have, however, only a subsidiary character. For instance, non residential rents [46] are adjusted periodically in accordance with coefficients derived from price indexes. Hence, Article 1 (paragraph 2) of Law No. 111/2018 reads "During this period and starting from the date this law becomes effective, [non residential] rents will be indexed and increased on a yearly basis in a proportion equal to the yearly inflation rate as determined by the official index issued by the Central Administration of Statistics for the previous year on condition that the increase does not exceed 5%".

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terminate the contract, on the date and on the conditions they determine, or may request the court to adapt it by mutual agreement. If no agreement is reached within a reasonable time, the court may, at the request of one of the parties, revise or terminate the contract, on the date and under the conditions it shall determine.*"*

[42]Article 147 para.2 of the Egyptian civil code; Article 148 para.2 of the Syrian civil code; Article 147 para.2 of the Libyan civil code; Article 146 para.2 of the Iraqi civil code; Articles 249 and 147 of the civil transactions law of the United Arab Emirates State, Article 358-1 para.3 of the Polish civil code.

[43]Article 166 of the Code of Obligations and Contracts states: "The law of contracts obeys the principles of the freedom of contract: individuals are allowed to organize their legal relationships, provided that they do not violate *ordre public*, public morals and mandatory legal provisions."

[44]Article 221 of the Code of Obligations and Contracts provides: "Contracts that are legally formed are binding upon the contracting parties, and should be interpreted, read and performed in accordance with good faith, equity and customs."

[45]Judgment rendered on 29 August 1940 by the Court of Cassation (chamber of civil affairs) published in مجلة المحامي سنة 13 القسم الاول ص 19, Judgment No. 93 rendered on 26 September 1940 by the Court of Cassation (chamber of civil affairs) published in مجلة المحامي سنة 13 القسم الاول ص 33, Judgment No. 93 rendered on 14 January 1983 by the Court of Appeal of Beirut (third chamber) published in مجلة العدل سنة 1958 عدد 1 ص 80, Judgment No. 11 rendered on 27 January 1987 by the Court of Appeal of Mount of Lebanon (first civil chamber) published in.مجلة حاتم جزء 190 ص 887.

[46]Relevant to contracts that were entered into before 23 July 1992 and are being extended by enacted Laws on a regular basis.

- **Foreign currency clause**

13. The Lebanese who enter into contracts have always preferred to insert foreign currency clauses and that was a widespread practice due to the lack of trust in the national currency (construction contracts, leases, insurance policies, annuities, installment sales …). In practice as seen earlier, after 17 October 2019 the US dollar creditors incurred huge losses due to the judgments rendered by Lebanese courts that allowed -in their majority- US dollar debtors to exonerate themselves by paying in LBP at AER.

14. Assuming that courts will not in their majority change their standing in the near future which is high likely the case, what would be the preventive clauses that could enhance the efficiency of foreign currency clauses in order to enable US dollar creditors to get paid in US dollar or in the worst case scenario in LBP at the market ER?

- **jurisdiction and governing law clauses**

15. In the current catastrophic circumstances, inserting only a foreign currency clause does not provide the required protection to US dollar creditors. They should make sure to insert jurisdiction and governing law clauses for objective reasons.

16. As for the jurisdiction clause, it is recommended that foreign courts have the exclusive jurisdiction to settle any dispute which may arise in connection with the contract (creation, validity, interpretation, performance …). During the last 5 years, Lebanese judges went five times on strike to achieve two main demands, namely the adoption of the "judiciary independence law" and the enhancement of poor working conditions. In parallel, the judiciary assistants declared strikes several times and demanded improved financial conditions[47]. So far and because of the ongoing national economical crisis, the wheels of justice are only expected to grind even slower than ever before. This will prevent contractual parties from having fast judicial proceedings.

[47]In this regard, it is worth mentioning that only 0.5 percent of the annual spending of the Government is dedicated to the Ministry of Justice. Insufficient funds resulted in an infrastructure that is in a quasi total collapse (run-down courthouses, power cuts …).

17. Hence, contractual parties should be careful when they select the foreign court that will have the exclusive jurisdiction to hear disputes arising under the contract. The two most important things to bear in mind when a US dollar creditor agrees on a specific foreign court are related to the place where the foreign judgment will be enforced and the cost of judicial proceedings. The location of the US dollar debtor's assets will be decisive to choose the foreign court that once it renders a judgment will be able to enforce it directly on assets present on its soil. This choice will enable the US dollar creditor to avoid the procedure of recognition and enforcement of this judgment in the jurisdiction where the assets are located (unless an international treaty provides that exequatur is not necessary). As for the cost, the US dollar creditor should be aware of the fees that he will pay in the foreign jurisdiction, e.g. appointing lawyers, collecting evidence, consulting experts, transporting witnesses …

18. The foreign court chosen in the exclusive jurisdiction clause should therefore be the court of the country where the US dollar debtor's assets are located and where the judicial proceedings fees can be afforded by the US dollar creditor. Add to that, the US dollar creditor has to make sure that this clause is valid and enforceable in Lebanon. He needs to be certain that if the US dollar debtor starts judicial proceedings before a Lebanese court, the latter will decline to exercise jurisdiction in favor of the foreign court determined in the jurisdiction clause. The Lebanese jurisprudence considers a jurisdiction clause valid as long as it respects the rules of internal compulsory territorial jurisdiction [48] and "the principles related to the Lebanese *ordre public"* [49] . In principle, the Lebanese courts retain international jurisdiction according to the same rules applicable to the internal territorial jurisdiction (Articles 74 and 80 of CCP), therefore contractual parties are allowed to choose foreign courts as long as they respect internal territorial jurisdiction compulsory rules determined in articles 108 (bankruptcy), 109 (life insurance), 110 (accident insurance), 111 (fire insurance), and 112 of CCP (any court that has a statutory express exclusive jurisdiction[50]).

[48] Judgment rendered on 10 February 1987 by the Court of Cassation, published in حاتم page 172; Judgment No. 11/1994 rendered on 8 August 1994 by the Court of Cassation (first civil chamber), available on http://77.42.251.205/ViewRulePage.aspx?ID=67760&selection.

[49] Judgment No. 36/1992 rendered on 9 July 1992 by the Court of Cassation (second civil chamber), available on http://77.42.251.205/ViewRulePage.aspx?ID=68740&selection;

[50] Articles 98 (real estate), 77 (concession), 78 par 2 (interim and preventive measures) and 79 (civil marriages) of CCP.

19. Thereby, if the US dollar creditor can afford the cost of undertaking judicial proceedings abroad, it is recommended to insert a jurisdiction clause that enables exclusively a court of the country where the assets of the US dollar debtor are located to settle the disputes relevant to the contract. The Lebanese courts will decline to exercise their jurisdiction to settle those disputes as long as the clause does not infringe the rules that involve Lebanese internal compulsory territorial jurisdiction and express Lebanese exclusive jurisdiction.

20. As for the governing law clause, both parties have to be aware that the choice of a foreign law is allowed only in international contracts[51]. It is a common practice that the foreign governing law should be the law of the foreign court to enable the judge to apply the law that he is most familiar with. Hence, the exclusive jurisdiction and governing law clauses will lead to foreign judgments that will allow the US dollar creditors to execute them directly on US dollar debtors' assets located in the same jurisdiction and therefore to receive a payment in US dollar[52] without the intervention of the Lebanese judiciary.

21. However, if the assets of the US dollar debtor are located in Lebanon, the US dollar creditor will have to go through two phases to execute the foreign judgment on the Lebanese soil, the exequatur (a court declaration of enforceability) procedure and the execution procedure.

Unless an international treaty of mutual judicial assistance provides that the exequatur is not necessary, the recognition of foreign judgments in Lebanon requires a judicial decision delivered according to articles 1009-1024 CCP. The president of the court of appeal[53] grants the exequatur (article 1013 CCP) on condition of reciprocity (article 1014. Par. d) if the judgment is issued in the name of a foreign sovereignty (article 2009 CCP) by a court considered competent according to its State laws on condition that this jurisdiction is not determined only by the nationality of the plaintiff (article 1014 par. a CCP) and that the judgment is enforceable according to

[51]Batiffol, "Contrats et conventions", Repertoire Dalloz de Droit international, No. 9. See for the definition of an international contract footnotes No. 36, 37 and 38.

[52]The drafters should make sure that the foreign judge can render a judgment in the currency of the contract in case it is different from his national currency. For instance, the "local currency rule" in English law which obliges courts to render judgments exclusively in sterling pound has been abolished in the famous case Miliangos v. George Frank (Textiles) Ltd. Currently, the English courts (and other European courts) can deliver judgments in foreign currencies.

[53] … of the judgment debtor's place of residence or assets.

those same State laws (article 1014 par. b CCP)[54]. The judgment debtor should have been allowed to be present at the proceedings that resulted in the foreign judgment (article 1014 par. c CCP) which should not be contrary to the Lebanese *ordre public* (article 1014 par. e CCP).

22. Once the foreign judgments are granted the exequatur, they will reach the phase of execution where the Lebanese execution judge will be entitled to use means of enforcement on the assets of the judgment debtor. Two preliminary questions could be raised at this stage, is the judgment debtor (the US dollar debtor) allowed to execute the foreign judgment by paying in US dollar by check if the judgment creditor insists on receiving the payment in cash US dollar? Is the judgment debtor (the US dollar debtor) allowed to execute the foreign judgment by paying in cash LBP or by check instead of US dollar (if the judgment creditor refused the payment in LBP)?

23. As for the first question, the judgment debtor might pay the amount mentioned in the judgment in lollars instead of "fresh dollars"! Is this payment valid? After 17 October 2019, the Lebanese banks witnessed a shortage of US dollar banknotes which obliged them to implement a *de facto* capital control and therefore to restrict withdrawals and transfers of customers' US dollar . Those pre-crisis US dollar deposits known as Lebanese dollars or "Lollars'' (a term coined by the banker Dan Azzi) can now be withdrawn in LBP at an ER of 8000 LBP for every Lollar[55] and they can also be sold on the market by checks at 85% discount rate (the 100 lollars' check is sold currently for 15 US dollar bank notes known as "fresh dollars"). Hence, if the judgment debtor pays with a check and not in cash, he will be paying only 15% of the amount owed to the judgment creditor. So far, the court of cassation has not delivered any decision that obliges judgment creditors to pay in cash. Therefore, checks are still considered acceptable means of payments according to Article 425 of the Code of Commerce. Nevertheless, few judgments have been rendered lately which considered that checks are no more means of payments due to the fact that they do not in practice enable their holders to receive the relevant cash amounts from banks[56].

[54]Provisional decisions and decisions issued in non-adversarial cases that are enforceable in the State of origin can also be enforceable in Lebanon.
[55]At 12000 LBP in certain cases (see footnote 18).
[56]Judgment No. 49 rendered on 5 October 2021 by the execution judge in Beirut and judgments rendered on 18 January 2022 and on 30 December 2022 by the execution judge in Beirut.

24. As for the second question, the jurisprudence is silent and provides no answer. On one hand, the Lebanese judge has to comply with Article 1022 CCP[57] and force the judgment debtor to pay the amount mentioned in the foreign judgment in US dollar, and on the other hand the judgment debtor might voluntarily execute the judgment and pay in LBP instead of US dollar based on Articles 30 of the Code of Obligations and Contracts, 7 and 192 of the Code of Money and Credit and Article 767 of the Penal Code. While the Lebanese judge who grants the exequatur is not allowed to make any amendments to the foreign judgment (article 1014 par. a CCP), it is not expected that any other judges including the execution judge would enable the judgment debtor to pay in LBP and not in US dollar if the judgment creditor insists on receiving the amount in US dollar. However, the probability that a judge accepts the payment in LBP at AER or at another ER should not be totally excluded. If the court accepts the payment in LBP, it could refuse that this payment be made by check. One court decision so far has refused the payment to be made in LBP by check[58]. The aforementioned *de facto* capital control imposed as well restrictions on the withdrawals of LBP deposits. Those restrictions started a trading market for the "bank LBP" known as "Bira" (a term coined by the banker Dan Azzi) where it was and still is being sold in exchange of cash LBP at 20% discount rate. Hence, if the judgment debtor pays the amount of 100 million LBP by a check, the creditor will sell the check for 80 million LBP in cash therefore incurring a loss of 20 million LBP.

25. In order to avoid this risk of receiving payments in lollar or in LBP, a cross-border payment clause (explained below in details) should be inserted in the contract. This clause will enable the foreign judge to order the payment in US dollar in a bank account outside Lebanon. During the execution phase of this foreign judgment, the Lebanese judges will not be allowed to accept a payment in lollar or in LBP. The judgment debtor will be forced to make a money transfer to a foreign bank account and the judgment creditor will be reimbursed in fresh dollar.

26. To sum up, the foreign currency clause will definitely enable the debtor to receive the payment in fresh dollars, without the intervention of the

[57] "The foreign judgment that has been granted an exequatur has the executive force of the Lebanese judgments and can be executed by the means of execution of those judgments".

[58] Judgment rendered on 26 May 2022 by the Court of Appeal of Beirut, 11th chamber (The judgment debtor (the client) had to pay to the judgment creditor (the lawyer) his fees worth 92000 US dollar or its equivalent in LBP at SAYRAFA ER "in cash and not with a check").

Lebanese judiciary, if a valid jurisdiction and a foreign governing law clauses are inserted and if the foreign judgment is executed on the debtor's assets located in the country of the chosen foreign jurisdiction. If the debtor's assets are located in Lebanon, the US dollar creditor should make sure to insert an additional cross-border payment clause according to which he will receive the payment in a bank account outside Lebanon. Hence, the foreign judgment will require that the payment takes place in a foreign bank account and the Lebanese judge will force its execution accordingly and will not allow the payment in cash LBP, in bira and in lollar.

- **Arbitration and governing law clauses**

27. In case the US dollar debtor's assets are located in a foreign country and the US dollar creditor is looking for confidential and relatively faster proceedings, the latter is advised to insert an arbitration clause instead of the jurisdiction clause. Arbitration proceedings are confidential and supposedly faster and less expensive[59] than judicial proceedings. If the governing law is a foreign law or a-national rules of law (rules applied in international trade, general principles of law …), he is advised to insert a foreign currency clause (US dollar)[60]. The arbitral award that requires an exequatur by the judiciary of the aforementioned country will be executed by it and eventually the US dollar creditor will receive the payment in fresh dollar. If the contractual parties choose the Lebanese law to govern the arbitration, it is recommended in the current scenario, to insert a cross-border payment clause. The arbitrator will not give the US dollar debtor the option to pay his debt in LBP.

28. In case the assets of the US dollar debtor are located in Lebanon and if the US dollar creditor is willing to avoid the Lebanese judiciary in the phase of settlement of dispute, it is recommended that the latter inserts an arbitration clause after he takes into consideration four main issues.

First, only commercial and civil disputes[61] that can be settled by transaction contracts are the ones that can be settled by arbitration. An

[59] Ad-hoc arbitration in general is less expensive than institutional arbitration.
[60] In all cases, it is better to make sure that the jurisdiction where the arbitral award is executed enables the creditor to receive the amount in the foreign currency of the award (US dollar).
[61] Articles 762 and 765 CCP and Article 1037 code of obligations and contracts.

arbitrator is not entitled to settle disputes[62] relevant to personal status, family status, succession, insolvency, *ordre public*, commercial representation[63] and labor contracts, banking disputes.

Second, it is recommended to insert (in addition to the arbitration clause) a cross-border payment[64] clause in order to make it an international contract which will make the arbitration itself an international arbitration. It shows from the practical experience that in comparison with internal arbitral awards[65], international arbitral awards[66] have a much higher chance to be granted exequatur by the Lebanese courts[67].

Third, if the applicable rules are a foreign law or a-national rules of law, the arbitral awards will require the payment of amounts denominated in US dollar according to the foreign currency clause. Once they are granted the exequatur, they will reach the phase of execution[68]. If the international arbitral award requires the payment of a specific amount of US dollar in a foreign bank according to a cross-border payment clause, the Lebanese judiciary will force the debtor to transfer the amount to the foreign bank account. It will not accept the payment in lollar or in LBP. If there is no cross-border payment clause and the arbitral award does not therefore require the payment of the amount (US dollar) in a foreign bank account, it is highly expected that the Lebanese execution judge will execute it the same way he executes foreign judgments with similar requirements and therefore might accept the unfortunate payment in lollar, in LBP or in bira.

Four, if the Lebanese law is the one applicable by the arbitrator, there should be a cross-border payment clause. The arbitrator will not give the US dollar debtor the undesirable option of paying in LBP and will order him to transfer the amount to the foreign bank account.

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[62] However, monetary rights deriving from all those disputes can be arbitrated.
[63] The exclusive commercial representations are abolished by the competition law No. 281 dated on 15/3/2022 (Article 5).
[64] See footnotes 34 and 35.
[65] Articles 767 till 808 CCP.
[66] Articles 809 till 821 CCP and *Lex Mercatoria.*
[67] In civil and commercial matters, exequaturs are granted by the president of the court of first instance, either at the place where the internal award was rendered or in Beirut if the award is international (Articles 770 (paragraph. 2), 775, 793 and 810 CCP).
[68] Article 835 CCP.

29. Hence, whether the assets of the debtor are located in Lebanon or in a foreign country, and whether the governing law is a foreign or a Lebanese law or a-national rules of law, the creditor is advised to insert a foreign currency clause, an arbitration clause, and a cross-border payment clause. The arbitral award will require the payment of an amount denominated in US dollar in a foreign bank account. The execution of the arbitral award whether in Lebanon or abroad will definitely lead to the payment in fresh dollar. The debtor will have to make the transfer of the amount to the specified bank account outside Lebanon.

- **Cross-border payment clause**

30. If the US dollar creditor inserts neither a foreign jurisdiction clause nor an arbitration clause, he should make sure to insert a foreign currency clause and a cross-border payment clause. The latter provides the required level of protection to US dollar creditors when the Lebanese judge is settling the dispute. This protection will enable the US dollar creditor to get paid in fresh dollar in a foreign bank account. Add to this that if for any reason the foreign exclusive jurisdiction clauses or the arbitration clauses are voided [if originally inserted] by the Lebanese courts, the cross-border payment clauses will be the decisive criterion that will enable those courts to characterize the contract as international contract and therefore to order a specific performance and force the US dollar debtor to pay in fresh dollar in a foreign bank account and not in lollar or in LBP, according to Article 249 of the Code of Obligations and Contracts[69].

31. In the same line of thoughts, it is of great interest to emphasize the importance of article 5 of the "standard form US dollar denominated loan contract" between the Government and BDL which states that the borrower (the Government) is supposed to reimburse the loan in US dollar in the BDL's foreign accounts (the lender). According to the previous draft (article 6), "the borrower [the government] is bound to reimburse the loan and interests from its income in US dollar (…). The borrower is allowed with the approval of BDL to reimburse in LBP according to SAYRAFA ER" [70].

[69]"As much as it is possible, the obligations should be executed in specific as the creditor has a right acquired to obtain the subject matter of the obligation in particular".

[70]In a meeting held with key decision makers on 24 March 2022 to discuss the drafting of this contract, the author suggested –among many other proposals-to make the reimbursement in US dollar "in the BDL's

Being a cross-border payment clause, article 5 makes from the loan an international contract which will enable courts to render judgments that oblige the government to reimburse the loan in fresh dollar and not in LBP or in lollar. This contractual provision is crucial to preserve the foreign reserves in foreign currency of BDL.

Hence, in all the contracts that are governed by the Lebanese law, the US creditor is advised to insert a foreign currency clause and a cross-border payment clause in order to receive the payment in fresh dollar whether the debtor's assets are located abroad or in Lebanon.

- **Exchange rate clause**

32. In case the US dollar creditor does not have foreign bank accounts or for a reason or another is not capable to benefit from this service, he cannot therefore insert cross-border payment clauses. Hence, under Lebanese law the foreign currency clause will not alone secure the US dollar creditor who will most probably be reimbursed in LBP at AER, in lollar or in bira according to a judgment or an arbitral award[71].

33. As for the payment in LBP at AER, the exchange rate clauses address this risk. Are the parties allowed to insert such contractual clauses? Are Lebanese courts (and arbitrators) bound to apply the agreed ERs? This question raises issues concerning the freedom of contract and the obligatory force of contracts in Lebanese law.

The answers to the questions can be found in both Article 166 and Article 221 of the Code of Obligations and Contracts which respectively state:

"*The law of contracts obeys the principles of the freedom of contract: individuals are allowed to organize their legal relationships, provided*

foreign accounts" and to remove the option of payment in LBP. This suggestion was taken into consideration in the final draft adopted by BDL (Article 5). To the knowledge of the author, the draft has not yet been adopted by the Council of Ministers.

[71]If the arbitration is governed by the Lebanese law.

that they do not violate ordre public, public morals and mandatory legal provisions."

"*Contracts that are legally formed are binding upon the contracting parties, and should be interpreted, read and performed in accordance with good faith, equity and customs.*"

34. According to the aforementioned Articles, courts and arbitrators are bound to apply the ERs determined in the relevant contractual clauses. One might argue that this type of clauses violates *ordre public* or mandatory legal provisions, but this reasoning is not legally founded: the Lebanese jurisprudence shows that courts have never considered that parties are forbidden from determining specific ERs; add to this that many of the investment treaties ratified by Lebanon expressly state that certain foreign investors "are allowed to agree with their contracting parties on a specific ER, otherwise the market rate of exchange shall be applied" [72]. Lebanon would not have ratified those treaties if contractual ERs clauses violate *ordre pulic* or mandatory legal provisions.

35. As for the payment in lollar and in bira, it is useful to insert a lollar clause and a bira clause (explained below), so that the creditor avoids the risk of receiving the contractual amount in US dollar by check (lollar) which is equal to only 15% of its value in fresh dollar or in LBP by check (bira) which is equal to 80% of its value in fresh LBP.

- **Lollar clause and Bira clause**

36. It is always wise to insert a lollar clause and a bira clause in addition to the foreign currency clause and the exchange rate clause in all the contracts governed by the Lebanese law, whether the disputes relevant to it are settled by an arbitrator or by a national court.

[72]The investment treaties signed with Iceland, Hungary, United Kingdom and Canada.

37. As for the lollar clause, it will enable the creditor to compensate the losses incurred in receiving a lollar payment if it reads "if the US dollar debtor offers to pay his monetary obligation denominated in US dollar by a check and the drawee is a Lebanese bank, the amount of the check should be equal to 7 [8,9 …] times the amount of the contractual nominal value of the monetary obligation". For instance, if the contractual monetary obligation to be paid is equal to 100,000 US dollar then the check amount should be equal to 700,000 lollar. If the creditor sells this check in the black market at the 15% current discount rate, he would get 105,000 fresh dollar. The additional 5000 US dollar would be a sort of safety margin (the discount rate is continuously increasing!). The US dollar creditor can eventually therefore be reimbursed in fresh dollar.

38. As for the bira clause, it will enable the creditor to compensate the losses incurred in receiving a bira payment if it reads "if the US dollar debtor offers to pay his monetary obligation in LBP according to the contractual exchange rate by a check, the amount of the check should be equal to the amount of the debt due in LBP plus 20% [30%, 40% …][73]". For instance, in a contract where the amount to be paid is equal to 1,000 USD and the contractual exchange rate is 40,000 LBP per US dollar, the judge will (as seen before) enable the US debtor to pay his debt in LBP at the contractual exchange rate. If the US creditor wants to pay in LBP by check he will have to pay 48 million bira[74]. The 48 million bira check will be sold on the market on a 20% discount rate for 40 million cash LBP which is enough to purchase 1,000 fresh dollars at the current black market exchange rate i.e., 40,000 LBP per US dollar. Therefore, the bira clause will enable the US creditor to receive the payment in fresh dollar if the US dollar debtor decides to pay in bira and not in cash LBP.

39. In this context, contractual parties should be aware that Lebanon is undertaking negotiations with the International Monetary Fund (Henceforth "IMF") and other international organizations and once they reach an agreement, the Lebanese Parliament will enact a capital control law. The Lebanese banks will be legally forbidden from enabling depositors to withdraw cash in foreign currency from their account and from transferring

[73]The value of bira is in continuous decrease.
[74](35,000*1000) +20%.

funds to foreign bank accounts[75] (with very limited exceptions). This law will lead judges to consider that checks are no more legal means of payments since they do not allow their holder to withdraw cash from the bank. This law will therefore forbid judges from allowing debtors to pay their debts denominated in dollars with checks denominated in dollars. The debtor will have to pay in cash dollar. The same will apply to bira in case the capital control law puts restrictions on the withdrawal of LBP deposits: paying with bira will not be acceptable by judges anymore.

- **Gold clause**

40. The gold clause is a provision that enables the creditor to require the payment in gold coins or in a weight of gold. Under Lebanese law, this clause is valid: the law No. 105 dated on 22/6/1999 abolished the decision No. 18 (Article 1) issued by the French high commissioner on 26/1/1940 that "prohibited to denominate civil or commercial obligations whatever their nature is, in a currency of gold or in a weight of gold or in an amount of legal tender that represents its corresponding equal in gold tender or weight of gold, and every contract that breaches this prohibition is void." Gold can therefore be used as a unit of payment and as a unit of account.

41. It is of utmost importance to provide a detailed description of the gold clause content. The quantum of this clause should be clear since there are no gold coins minted by the government that could be referred to[76]. The specifications should cover the form (coins, ounces, bars …), quantity (in letters and not in numbers[77]), their type[78], their weight[79] and their purity[80]. A

[75]The Middle East & North Africa Financial Action Task Force (MENAFATF) is expected to publish an assessment of the implementation of anti-money laundering and counter-terrorist financing measures in Lebanon by the end of 2022. In the previous assessment, Lebanon was on the list of compliant countries, however the new assessment can place Lebanon on the gray or even on the black list which could push the correspondent banks to stop dealing with the Lebanese banks. It will become impossible to undertake a cross-border bank transfer.

[76]Zimbabwe declared that it will introduce gold coins in July 2022 in order to encourage investors to store value inside the country as the currency is constantly losing its value.

[77]One hundred coins instead of 100 coins.

[78]The gold coins that are traded on a wide range on the Lebanese market are the "English gold coin" ("Lira dahab Englizyya"). On a much smaller range the "Turkish gold coin" ("Lira dahab osmallyya") and the "lira dahab rachadyya" are traded. The gold ounces and the gold bars traded on the Lebanese market are the "Lebanese gold ounces", the "Swiss gold ounces", the "Lebanese gold bars" and the "Swiss gold bars" all stamped with the "9999" mark.

[79]Usually the weight is in grams. The weight of a gold coin is 8 grams and the weight of a gold ounce is 5, 10, 20, 30, 50 or 100 grams. The weight of a gold bar is 250, 500, 750 and 1000 grams.

typical gold clause would read, “The price of the sold car is ten English gold coins “Lira dahab Englizyya”. Each coin is twenty one karats and weighs eight grams.” The detailed description is crucial for the courts to order the debtor to pay and deliver the contractually agreed number of gold coins, ounces or bars[81]. However, the gold price history[82] shows that “gold or gold-supported money, both in times of peace and in times of war, has proved unreliable as a standard of purchasing value”[83], and this is due to the unexpected and constant fluctuations in price. Therefore, receiving payments in fresh dollar is more secure than in gold. The creditor is encouraged to insert clauses that guarantee the payment in fresh dollar instead of gold.

42. In all cases, would the debtor be allowed to exonerate himself by paying the price of gold in dollars by a check instead of delivering physical gold? Would the execution judge exonerate the creditor if he pays by check the amount of 4000 US dollar instead of delivering the contractually agreed 10 gold coins where the market value of a coin is 400 US dollar? In other words, would the debtor exonerate himself by paying 4000 lollars instead of delivering 10 gold coins that are worth 4000 fresh dollars?

43. There are no judicial precedents that answer the aforementioned questions. There are no guarantees that the Lebanese judges, especially in the execution phase, will refuse the payment in lollar. There will always be a risk that the creditor will be judicially forced to accept the payment in lollar instead of receiving the contractually agreed physical gold, therefore incurring the risk of losing more than 85 % of his right. Nevertheless, one should not underestimate the very low risk to get paid in LBP at AER (very few judges might consider that if the price of a gold coin is 400 US dollar, the debtor will be exonerated if he pays only 600,000 LBP according to AER). All this been said, if the Lebanese judiciary is settling the dispute, the gold clause is a preemptive measure that will allow the creditor in the best case scenario to get paid in physical gold (bearing the risk of gold price fluctuations) and in the worst case scenario in LBP at AER.

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[80]The purity of gold is measured in karats (24 karat gold is pure gold with no other metals). The purity of the “English gold coin” is 21 karats and the purity of the gold ounce and the gold bar is 24 Karats.
[81]Articles 249 and 250 of the Code of Obligations and Contracts.
[82]https://goldprice.org/fr/node/216.
[83]George Nenobline, “The gold clause in private contracts”, Yale law journal, vol. 422, page 1058. The article is available on https://core.ac.uk/download/pdf/143656236.pdf.

44. If the foreign court is settling the dispute, the gold clause is an inefficient preemptive measure[84]. In case the judgment is meant to be executed in the country of the ruling foreign court, the gold clause will expose the judgment debtor to the risk of price fluctuations of gold which is by far more dangerous than the risk of depreciation of US dollar. If the foreign judgment is executed in Lebanon, it is probable that the execution judge will consider that the judgment debtor is allowed to exonerate himself by paying in lollar, in cash LBP or in bira instead of delivering the physical gold.

45. If the arbitrator is settling the dispute, the creditor should make sure that the governing law does not void gold clauses. As for the execution of the arbitral awards abroad or in Lebanon, it is doubtful that the creditor will address the risk of gold price fluctuations and the risk of receiving the payment in lollar, in LBP or in bira for the same aforementioned reasons that apply to the execution of foreign judgments on the debtor's assets located in Lebanon.

- **Indexation clause**

46. Since September 2019, the constant changes in the ER had a direct impact on inflation rate. The non-stop loss of value of LBP against US dollar led to the increase of the price of all the imported goods and therefore to the increase in inflation. If the contracting parties do not agree to insert a foreign currency clause or a gold clause, they will be obliged to denominate their obligations in LBP instead of US dollar or gold. Hence, the creditor should make sure to address the risk of the constant depreciation of LBP by inserting an indexation clause and a bira clause that would shift the inflation burden totally or partially onto the debtor. This indexation clause will adjust the amount of contractual monetary obligations to be paid according to the Consumer Price Index (Henceforth "CPI') which is the most used tool to gauge inflation that is calculated based on the change in the level of prices in a specific country according to a typical basket of goods and services. The bira clause will compensate the losses that will be incurred by the creditor in case the debtor decides to pay LBP by check and not in cash as explained earlier.

[84]The contract drafter should make sure that gold clauses are valid under the chosen governing foreign law.

47. The Lebanese law recognizes indexation clauses[85]. However, it is still crucial to choose among the three CPIs published in Lebanon, the one that reflects best the variation in inflation. First, the Central Administration of Statistics (henceforth "CAS") publishes a CPI since 1999[86]. The main advantage of this CPI is that it is published with the technical assistance of IMF on a monthly basis to all users in the private and public sectors on CAS webpage and in newspapers and magazines. Second, the Consultation and Research Institute[87] (henceforth "CRI") publishes a CPI on a monthly basis since 1977. The advantage of this CPI is that it is the result of an extended long history where it was in the 1977-1984 period the sole reference for formal wage adjustment[88] and was the sole CPI adopted by the government until 1999. However, the disadvantage of this CPI is that it is not available on the website and requires a subscription. Third, the association "Consumers Lebanon"[89] computes a CPI but does not publish it and does not provide any information that could enable to have access to it. It stands outside the scope of this paper to give a technical analysis of each of the three published CPIs in order to conclude which is the most accurate. However, since the CPI published by CAS is accessible to all on its website for free, it is recommended that creditors make reference to it in contracts.

48. Yet to make one final but important remark relevant to the correlation between ER and CPI on the Lebanese market. For example, The total inflation rate from December 2019 to October 2021 is 519%[90] while the increase in ER during this period is 900%[91] (in December 2019 it was around 2000 LBP for one US dollar and it spiked to around 20000 LBP for one US dollar in October 2021). It is advisable that the creditor, whose contractual debt is denominated in LBP, inserts an index clause which includes an indexation formula that is equal to the monthly CPI published by CAS multiplied by two and that in order to hedge against the depreciation of LBP. A sample of such clause would be as follows "the landlord shall receive from the tenant on a monthly basis a rent equal to six million LBP.

[85]The principle of freedom of contract (Article 166 of the Code of Obligations and Contracts).
[86]http://www.cas.gov.lb/index.php/economic-statistics-en/cpi-en.
[87]www.crilebanon.com
[88]An extensive explanation of the history of CPIs in Lebanon is given by the founder of CRI the economist Kamal Hamdan in his interview with Jad Ghosn. It is Available on https://www.youtube.com/watch?v=uGnKlFt2snU (24:00 till 36:00).
[89]www.consumerslebanon.org
[90]The figures are available on the website of CAS.
[91]((20 000-2000)/2000)*100=900%.

This rent shall be increased by the double of the CPI monthly published by CAS. For instance, if the CPI is 10%, the additional amount should be equal to 20% of the rent which is equal to 1,200,000 LBP, therefore the rent to be paid this particular month would be 6,000,000 LBP+1,200,000 LBP= 7,200,000 LBP. If for any reason CAS does not publish a CPI, the CPI published by CRI shall be adopted".

- **Conclusion**

49. The main concern of contractual creditors in Lebanon currently is to avoid the drastic effects of hyperinflation. An ultimate protection will be to insert "first-tier clauses" that will enable the creditor to receive payments in fresh dollar with no intervention of the Lebanese judiciary. If this ultimate protection is not available, "second-tier clauses" will enable the creditors to reach their goal with a partial intervention of the Lebanese judiciary. If the total intervention of the Lebanese judiciary is inevitable to get reimbursed in fresh dollar, "third-tier clauses" are recommended. Otherwise, the "fourth-tier clauses" will provide the least amount of protection which is to receive the payment primarily in lollar or in bira by shifting the depreciation risk onto the debtors.

As for the "first-tier clauses",

50. If the debtor's assets are located in a foreign country and the creditor can afford the expenses of foreign judicial proceedings, the latter is advised to insert foreign jurisdiction and governing law clauses and a foreign currency clause (US dollar). In this same scenario, he can insert an arbitration clause instead of the foreign jurisdiction clause if he prefers confidential and fast proceedings. The rules governing the arbitration should be a foreign law or a-national rules of law. Those clauses will lead to foreign judgments and to arbitral awards where the sum to be reimbursed is denominated in US dollars and not in LBP. Those foreign judgments and arbitral awards will be executed on the debtor's assets on the foreign soil without the intervention of the Lebanese judiciary. Hence, the creditor will receive the payment in fresh dollar.

As for the "second-tier clauses",

51. If the debtor's assets are located in Lebanon, the creditor is advised to insert an arbitration clause, a foreign currency clause, a cross-border clause, and a governing law clause (a foreign law or a-national rules of law or the Lebanese law). The arbitral award will require the payment to be made in US dollar in a foreign bank account. The execution of this award in Lebanon after being granted the exequatur will force the debtor to implement the transfer of the amount of fresh dollar to the foreign bank account. If the creditor does not have a foreign bank account, he should replace the cross-border payment clause with an exchange rate clause and a lollar clause that will allow him to receive a payment in fresh dollar. In case the creditor inserts a foreign jurisdiction clause instead of the arbitration clause, the foreign judgment will force the debtor to transfer an amount of money in US dollar to a bank account outside Lebanon. This foreign judgment will be executed in Lebanon in the same way as the aforementioned arbitral award and the creditor will receive fresh dollars in his foreign bank account.

As for the "third-tier clauses",

52. If the creditor cannot afford the expenses of arbitration and foreign judicial proceedings, he should insert a foreign currency clause and a cross-border payment clause. Those clauses will enable the Lebanese judiciary to render judgments that allow the creditor to be reimbursed by a transfer of the fresh dollar amount to a foreign bank account.

As for the "forth-tier clauses",

53. In case the creditor cannot afford the expenses of arbitration and foreign judicial proceedings and cannot insert a cross-border payment clause, he will have to insert a foreign currency clause, an exchange rate clause, a lollar clause and a bira clause. Those clauses will allow the creditor to get the payment either in fresh dollar or in cash LBP at a pre-determined ER e.g. SAYRAFA ER or by a check (lollar/bira) that has a market value equal to the contractual debt amount (fresh dollar). If there is no possibility to insert a foreign currency clause, the creditor will have to denominate the obligation in LBP. In this case, an indexation clause and a bira clause will

enable the Lebanese judge to adjust the contractual amount due in cash LBP according to the depreciation rate of the currency.

54. Drafting contracts in Lebanon during hyperinflation is not about defying gravity, it is mostly about being aware of the one basic rule to stay in orbit namely, “what is temporary in Lebanon remains permanent”. No legislations that tackle foreign currency bank deposits and exchange rates will be enacted. There will just be minor quick fixes with no crucial legal impact on how to draft contracts except for the fact that they will probably make it even more complex. It will become more like drawing graffiti than drafting a contact. Pity the lawyers!

Annex 1

The recommended four tiers of clauses

Requirements	First tier clauses	output
-The debtor has assets abroad. -The creditor can afford foreign judicial proceedings. -The creditor can afford arbitral proceedings.	-Foreign currency clause. -Foreign governing law clause. -Jurisdiction clause or arbitration clause.	-Fresh U.S. Dollar. -Fast dispute settlements proceedings.

Requirements	Second tier clauses "I"	output
-The debtor has assets only in Lebanon. -The creditor can afford foreign judicial proceedings. -The creditor can afford arbitral proceedings. -The creditor has a foreign bank account.	-Foreign currency clause. -Cross Border payment clause. -Foreign governing law clause. -Jurisdiction clause or arbitration clause.	-Fresh U.S. Dollar. -Relatively fast dispute settlement proceedings.

	Second tier clauses "II"	
-The debtor has assets only in Lebanon. -The creditor can afford arbitral proceedings. -The creditor doesn't have a foreign bank account.	-Foreign currency clause. -Lebanese governing law clause. -Arbitration clause. -Bira clause. -Lollar clause.	-Bira or Lollar. -Relatively fast dispute settlements proceedings.

Requirements	Third tier clauses	output
-The debtor has assets only in Lebanon. -The creditor cannot afford arbitral and foreign judicial proceedings. -The creditor has a foreign bank account.	-Foreign currency clause. -Cross Border payment clause.	-Fresh U.S. Dollar. -Slow dispute settlement proceedings.

Fourth tier clauses "I"

-The debtor has assets only in Lebanon. -The creditor cannot afford arbitral and foreign judicial proceedings. -The creditor does	-Foreign currency clause. -Exchange rate clause. -Bira clause. -Lollar clause.	-Lollar or Bira. -Slow dispute settlement proceedings.

not have a foreign bank account.		

Requirements	Fourth tier clauses "II"	output
-The debtor has assets only in Lebanon. -The creditor cannot afford arbitral and foreign judicial proceedings. -The creditor does not have a foreign bank account. -The monetary obligation cannot be denominated in a foreign currency.	-Indexation clause. -Bira clause.	-Bira or LBP. -Slow dispute settlement proceedings.

Annex 2

Commentary of Professor Philip Wood

"Dear Mohamad,

I very much enjoyed your excellent paper on drafting contracts in Lebanon during hyperinflation and I agree with your general approach.

The basic principle is correct that, in order to insulate the contract for foreign currency payment from Lebanese legislation or Lebanese law, including exchange controls, the contract must:

- expressly be governed by an external system of law
- select the exclusive jurisdiction of external courts, coinciding with the governing law if possible, and complying with the local jurisdictional rules, such as the appointment of a local agent for service of process. Arbitration is also possible, in which event the New York Arbitration Convention of 1958 will apply to enforcement if Lebanon is a party, which I expect it is. This does not usually help much in the case of mandatory local laws or other public policy obstacles in Lebanon.
- expressly state the currency of payment
- expressly state that the place of payment is outside Lebanon – this would normally be New York if the currency is US dollars
- minimise any contact connexions with Lebanon. The externalising of the location of the contract is necessary under New York law in expropriation cases involving exchange controls since the recognition of Lebanese exchange controls will not apply if the contract is located outside Lebanon. The reason for this is that in those cases The US courts apply the act of state doctrine which rules out local laws if the contract is external: it is not enough that the contract is governed by New York law. On the other hand the English courts will not apply foreign exchange controls if the contract is governed by English law,

regardless of its location. Note that in many jurisdictions you may have problems if all the contract connexions, except the governing law, are local, that is, the contract is entirely domestic, as you point out.

There are some important qualifications. As you rightly say, the above insulation may not be successful in practice if the debtor has no external assets. In that case enforcement proceedings might well have to be taken in Lebanon and in that case you can expect the Lebanese courts always to apply their own mandatory laws, which would usually include exchange controls and similar laws.

So far as I know, virtually all countries will convert a foreign currency debt into the currency where any insolvency proceedings are taking place, eg presumably into Lebanese currency if there is a judicial order for the insolvency of the debtor in Lebanon if Lebanon follows that general rule (as almost all Napoleonic countries do). The date of conversion is almost invariably the date of the commencement of the insolvency, so that if the insolvency carries on for a long time the claim of the creditor is depreciated. Insolvency laws typically render top-up clauses void. Top-up clauses are also typically void in the case of judgments outside insolvency proceedings which are converted into the local currency for enforcement over local assets.

Note also that article VIII 2b of the IMF Agreement provides that exchange controls contrary to the exchange controls of a member state are not enforceable in the courts of any member state. The courts of France, Germany (sometimes) and Luxembourg typically apply this to all kinds of contracts, such as loans and contracts of sale, but the courts of England and New York do not. This is one reason that English or New York law are commonly chosen as the governing law of wholesale financial contracts, as well as their relevant courts. I suggest you mention English law as well - both English and NY law are thought to have about 80 per cent of the market for wholesale financial deals. English law has a simpler and more predictable approach to the insulation achieved by an external governing law than NY law.

I agree with you that indexation clauses can be problematic and in any event are often resisted by debtors. Gold clauses, which were very common in the 1930s, are similarly problematic now since the abandonment of the gold standard.

I hope that the above remarks are helpful but do let me know if you would like to discuss further.

Best regards,

Philip Wood, CBE, KC Hon".

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Mohamad Fawaz is a:

1- Judge at the Legislation and Consultations Board at the Ministry of Justice, specialized in finance law and international law.
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He is the author of:

1- "Hyperinflation in England: The Aftermath", Sweet & Maxwell Ltd, 2016.
2- "Hyperinflation in Lebanon: The Exchange Rate Dilemma", Lexis Nexis/MENA Business Law Review, No. 2/2021.

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