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Some Thoughts at the Launch of a European Contract Law

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Chapter 1
Introduction

Currently, the only tailor made international commercial law is non-state law, such as CISG,[1] the UPICC[2] or even the UCC[3] and standard contract forms. At the same time, the current work on the DCFR[4] focusses on both consumer and business law. The current recommendations tend to make this new instrument 'optional' (an Optional Instrument, OI), backed by Europe's Justice Commissioner Viviane Reding[5] while some only wish to go as far as to treat it as a 'toolbox' within private international law,[6] and a third suggestion is even to combine the two.[7] In any case, the outcome will be non-state or soft law or indeed some hitherto unknown form of optional state-endorsed law.[8] The European Parliament has expressed a preference for the Optional Instrument in a vote of 8 June 2011.[9]

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[1] United Nations Convention on Contracts for the International Sale of Goods, done at Vienna, 1980, therefore often referred to as the 'Vienna Convention on the International Sale of Goods', short CISG. It is non-state law in those countries who have not ratified it such as the UK.

[2] UNIDROIT Principles on International Commercial Contracts, 1994/2004.

[3] Uniform Commercial Code (US American Law Institute).

[4] Draft Common Frame of Reference.

[5] Speech of 3 June 2011 in Leuven, see press release under link http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/11/411&format=HTML&aged=0&language=EN&guiLanguage=en [14 Oct 2011].

[6] As for instance the German Federal Justice Minister expressed adamantly in her recent contribution, Leutheuser-Schnarrenberger (2011), pp. 454–456.

[7] This is the suggestion contained in a report by Diana Wallis MEP adopted by the Legal Affairs' Commission on 12 April 2011 (MEMO11/236).

[8] Answering the question of the legal nature of the new instrument would exceed the scope of this paper. The consultation following the Green Paper from the Commission on policy options for progress towards a European Contract Law for Consumers and Businesses, COM(2010)348 final (2010) closed January 2011. 320 responses were received. Some respondents rightly remarked that it would be premature to comment on an instrument the contents of which were unpublished and undetermined at the time of the consultation.

[9] http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/683&format=HTML&aged=0&language=EN&guiLanguage=en [15 Oct 2011].

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The Commission has now formally issued the Proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law on 11th October 2011.[10] The draft blueprint of this proposal which is the outcome of the Expert Group's work is currently available in the form of a 'feasibility study'.[11]

So far, European law has concentrated on consumer law and touched on commercial matters in the form of financial regulation and competition law. So, both the questions of whether the issues covered by traditional commercial contract law will be covered by the new OI, whether the OI will make traditional commercial contract law redundant and how the application of such a potential new Optional Instrument will work in practice will have to be answered.

When Ole Lando set about drafting the European Principles of Contract Law he was expecting to draft a 'European Uniform Commercial Code'.[12] Meanwhile, the expert group that may be called a successor gremium to Lando's first project met almost once a month to draft the 'Common Frame of Reference' (CFR).[13] These experts were aiming not only at reformulating and consolidating the 'consumer acquis' following the Green Paper of 2007[14] but at providing more generally a European contract law including contracts between businesses.

The terminology denominating the respective constellations to be considered in the drafting of these rules is normally 'business to consumer', 'business to business' or even 'Business to business' indicating large to small business or SME,[15] short forms in use are B2B, B2C, B2b.[16]

Surveying the protocols of these meetings[17] one finds that despite the clear focus on consumer aspects in contract law, individual rules of the 'classic' uniform commercial contract law codified in the CISG and UPICC have been suggested to be preferred over the rules of the DCFR in order to suit both consumer and business contracts. The content of these rules can be said to be traditionally typical for commercial contracts such as notification rules, the order of payment and passing of risk Articles 6.1.3, 6.1.4, and 6.1.7 UPICC apart from the wording taken

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[10] COM(2011) 635 final.

[11] http://ec.europa.eu/justice/contract/files/feasibility-study_en.pdf [15 Oct 2011].

[12] Lando and Beale (2000), p. xi.

[13] See the current website http://ec.europa.eu/justice/policies/consumer/policies_consumer_intro_en.htm from where a list of members and also the individual protocols can be accessed.

[14] Green Paper on the Review of the Consumer Acquis, 8 Feb 2007, COM(2006) 744 final.

[15] Small and medium sized business.

[16] C2C for 'consumer to consumer', is also in use, see protocol of the third meeting of 22/23 July 2010, p. 2. It is not explained in much more detail in the protocol of that meeting why this constellation would need special attention. The protocols often use the capital and small letter spelling with no apparent intention to differentiate in the Above way, thereby deviating from established use in the literature. The protocols may of course have been drafted very speedily and not with a view to being published as academic papers, but nevertheless this use of inconsistent spelling is confusing.

[17] See in more detail below, 2.2. et seq.

from CISG 'could not have been unaware' to replace the wording in Articles IVA 2:307b, 301 and 302 of the DCFR for greater clarity.[18]

This begs the question of whether the reasons for the separate traditions of commercial or merchant and civil or private contracts have been analysed sufficiently before embarking on the redrafting project for the prospective CFR/OI. Are the rules in both spheres interchangeable or do they each serve a separate purpose? Should businesses and consumers have separate contract law codifications in order to enhance the Internal Market?

I will discuss this question in the first part of this paper and then move on to discuss the current role of transnational contract law within the setting of private international law in order to explain the prospects of the Optional Instrument (CFR) in current international law.

[18] Due to reference to the non-disclosed draft in the recorded discussions, now feasibility study, it is not straightforward to derive how the respective rules under discussion finally feature in the final product. It is however noteworthy and highly laudable that instructions were given early on by the EU drafters to effectively remove the longwinded counting method of the DCFR and create a simple structure with plain consecutive Article numbers.

Chapter 2
Review of Current Use of the Law Merchant in Domestic and International Law

"Commercial law occupies in some sense ground zero of the onslaught of globalization." This observation by Jane K. Winn[1] offers a strong metaphor for the significance and the traditional pioneering role of commercial law. Commercial contract law currently forms the only consistent body of transnational contract law and therefore plays an exemplary role in the formation of transnational legal methodology.

2.1 Uniform Commercial Law as Responding to a Need to Promote Uniformity on Behalf of International Trade by Purpose and Scope

Existing substantive legal instruments in the field of international commercial contracts include the 1980 Vienna Convention on the International Sale of Goods, CISG, the 2004 UNIDROIT Principles of Commercial Contracts, UPICC, the United Nations Commission for International Trade Law (UNCITRAL) Model Laws, a wealth of standard terms and arbitration rules. Within the EU,[2] but not originally arising from institutions, the Principles of European Contract Law (PECL) were drafted, also the so called CoPECL,[3] Insurance Law Principles and now the Draft Common Frame of Reference (DCFR) with an informal underlying mandate and official institutional funding, however from general research funds.

[1] Winn (2002), p. 445.
[2] European Union.
[3] The Common Core of European Contract Law.

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The starting point for all of these projects was to provide uniform law for international trade.[4] Based on this early foundation and at the end of international research activities stretching over nearly 30 years the DCFR has now taken on a more recent development within EU legislative procedures which allows a more expanded scope of legislation in the field of private law resulting in an extensive 'consumer acquis' and regulatory provisions in many areas of European trade and services.[5] The DCFR has incorporated the predecessor project, the PECL.[6] This symbolises a form of continuity which has often been lacking among the various uniform law projects over the years, starting with the ULIS[7] and continuing with CISG and the UPICC: the projects eventually existed in parallel to each other with no express reference to the chronologically preceding instrument, such as the ULIS, CISG and PECL and without express reference to the scope of other coexisting instruments covering a narrower or wider range of aspects of the same area of law, such as the CISG, UPICC and PECL. The relationship between PECL and the DCFR also reflects the expanded scope of legislative potential of the EU Institutions following the Treaty of Nice with the Title IV establishing among others the judicial co-operation in civil matters and other comprehensive areas of activity enabling them to pass directly applicable instruments in previously uncovered areas, such as private international law. As the editors of the DCFR explain, the scope of the DCFR had to be determined with a view to current and future demand.[8] This motivation has now allowed the drafters to cover a much broader range of aspects of contract law than those of previous uniform law instruments were able to. However, the question arises what the place of these previously drafted instruments is in relation to the DCFR and if there is still a need for specialised law addressing commercial contracts. Traditionally, national contract laws cover contracts in general and there is no distinction between commercial and other contracts as such. There is, however, in some European national laws a special law merchant usually codified in special commercial codes which deal with aspects of company law, registration and also aspects of contract law. Despite long standing academic debate about the necessity of a separate

[4] See preambles of those texts and Lando and Beale (2000), p. xi.

[5] See Study Group on a European Civil Code/Research Group on EC Private Law (Acquis Group), (2008), Introduction, para's 60–71 and see the overview over many relevant legal instruments in Twigg-Flessner (2008), at 3.3.

[6] For details refer to Study Group on a European Civil Code/Research Group on EC Private Law (Acquis Group) (2008), Introduction, para 50 et seq.

[7] Uniform Law of International Sales, The Hague Academy, 1964.

[8] Study Group on a European Civil Code/Research Group on EC Private Law (Acquis Group) (2008), Introduction, 60–76.

codification in this area,[9] this model is still followed even in recent law reform.[10] The applicability of those contract rules contained in the commercial codes depends on certain aspects and the size of the business activity of the contracting party and is closely intertwined with the domestic company law. Independently of this tradition of using the notion of merchant to unlock a separate legal regime, the European acquis has created a different approach by introducing the term entrepreneur as the counterpart of the consumer who is the focal point of a range of legislation affecting contract law. This introduces a new 'character' onto the scene and it also looks at the content and purpose of the contract itself. Existing uniform law instruments such as the CISG similarly determine their applicability by way of looking at the contract itself and its purpose rather than the qualities of the contracting parties.[11] Some European jurisdictions have taken this development as an incentive to adapt their commercial codes such as Austria where the commercial code has been reformed introducing the term entrepreneur ('Unternehmer') instead of the traditional 'Kaufmann'.[12] In other countries such as Germany, the traditional law now exists simultaneously with the new concept—if indeed it can be called a concept—where the notion of consumer has been introduced into the BGB[13] but without any explanation about the relationship of this new concept to the traditional dichotomy.[14] This is a gap in legislation and legal science which has yet to be bridged. However, the question arises what the practical significance of this newly arising concept of consumer law and even a wholesale 'European private law' is in the context of traditional commercial law and specifically international trade law which is certainly a central interest of European policies directed towards the creation of an internal market as well as to global trade. Much of the European *acquis* and the European uniform model rules on contract law are

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[9] See for instance Schmidt (1982), p. 837. Surely, proponents of an integrated solution who only see the law of obligations concerned by the *Handelsrecht* overlook the more wide ranging provisions that the commercial codes make such as register law, the name of the company, Firma, accountancy rules and much more which to my mind are not obvious candidates for an insertion into the special law of obligations, Besonderes Schuldrecht. Cf. Müller-Freienfels (1978), p. 618 or the remark of Wiethölter (1970), p. 37, that merchant law (Handelsrecht) existed only for a few lawyers, such as law students. In my view, this perception comes from the development of a considerable body of special law for the different areas of commercial law, such as public limited companies, take overs, mergers and so forth where the GmbH Gesetz (the German Limited Companies Act) stood only at the beginning. These special laws have developed an overwhelming significance in society. The traditional commercial codes still contain the general principles on which the special law is built and so those should continue to form the backbone of the highly fragmented special laws. An old law is not inevitably outdated.

[10] Cf. the discussion surrounding the recent reform of Turkish private law including the commercial code and consumer law as reported by Damar and Rösler (2011), p. 612.

[11] So-called objective approach, see below 2.4.1.2.

[12] See below 2.4.1.2.

[13] *Buergerliches Gesetzbuch*, the German civil code.

[14] §§13 and 14 of the BGB, *Buergerliches* Gesetzbuch, *and* cf. Alpa and Andenas (2010), pp. 138–139; Schmidt (2005), p. 837, and see below, 2.4.1.2.

international contract law in a broad sense as they are uniform sources of law made to apply across the Member States.

The practical significance of international contract law for international trade is threefold: consequences arise from the actual content of the substantive rules and also secondly from their application within domestic legal systems either directly or by way of international private law which forms the third aspect. I am therefore asking in this chapter if there is any content in international contract law which is specifically addressed to international trade.

2.2 Commercial Contract Law in the Discussions of the Expert Group on the Drafting of a European Contract Law

Commercial contract law is an expression which does not show up in the discussions of this gremium that has been meeting almost monthly to formulate a European contract law instrument. By way of contrast, it was decided not to provide an abstract definition of consumer contract. So the expression contract is modified only by the attributes business to consumer (B2C) and business to business (B2C).[15] It was expressly decided to cover both those constellations in the proposed instrument even though it is very clear from the transcripts that the emphasis is on the consumer's rights in contractual relationships. There are no separate sections for each type of contracts in the proposed instruments but items are regulated by subject matter. Those subject matters concerning B2B contracts are only few and those included particular the role of good faith and unfair contract terms (6th meeting). The latter were recommended to be based on the current rule of Article II-9:405 DCFR (7th meeting). Also in B2B contracts, the passing of risk was confirmed to be reflected as in 'current practice' by Article IV A 2:201 DCFR. Otherwise, businesses are addressed by way of B2C contract rules.

Those are in particular: The role and meaning of 'intention', pre-contractual information duties, confirmation between businesses, Article 7:104 PECL, (4th meeting), rules on order of performance, partial performance and method of payment in Articles 6.1.3. 6.1.4 and 6.1.7 of the UPICC, the 'perfect tender rule' (6th meeting), adaptation rules in Article 6:111 (3)(b) PECL, notification rules with regard to defective performance where Article III-3:107 (4) DCFR is recommended to be maintained, all other rules declared redundant, i.e. the previous sections of the aforementioned article as well as Article IV A.-4-301 DCFR. In defective performance knowledge of the defect is identified as justifying different rules for B2B and B2C (7th meeting) with an interesting involvement of third parties. Another distinction was made between B2B and B2C with regard to the right to cure. This was stipulated to be a business right only, also for

[15] Cf. 1. above.

early delivery (9th meeting). The consumer on the other hand should have an 'unfettered' right to choose the remedy for defective performance. For B2B the notion of impossibility should not be recognised and the wording of the DCFR (Article II 3 203) was preferred over that of the respective UPICC provision.

Businesses should also benefit from a right to non-economic loss according to Article III 3:701 DCFR. (9th meeting).

Much of the discussion has to be read *cum grano salis* because of the way the transcripts are composed. They do not always allow a clear understanding of what was discussed as the meaning gets lost in hasty drafting.[16] So, I want to take up on some points which surfaced in these documents for the sake of a discussion and illustration of special requirements of commercial contract law in legal drafting.

2.3 Special Problems of International Trade

It may be asked whether international commercial contracts are so different from domestic or private international contracts that they need a separate regime.

2.3.1 ...Typically Addressed in Standard Contract Forms

The first point to be noted, looking at the contracts themselves, is that the trading communities address many of the typical problems arising in international contracts by way of standard contract forms issued by branch specific trade associations. These contain certain clauses that in addition to the special modalities of the transactions within different branches cover situations which are specific to international commerce. These typically include *force majeure*, currency fluctuations as well as special requirements regarding delivery, defective performance and termination. Covering long distances in transportation through many different countries makes these more difficult and facing more and different risks than purely domestic contracts. Natural desasters, political upheaval, embargoes, wars, economic crises and long sea voyages affect contracts much more frequently in international trade than in a domestic setting.[17] This is not new but has resulted in customs and usages as well as rules of a range of different legal nature developed over centuries and the entirety of those rules is sometimes called *lex mercatoria*.

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[16] Many of the inconsistencies were picked up by the 'stakeholder' expert group and may have led to a correction of the considerations (meeting on 17th April 2011), such as the passing of risk upon delivery to the first carrier, a typical rule in commerce, also to apply to certain consumer contracts, as suggested by the EG in the ninth meeting, p. 1. Also, the inappropriate use of the term 'specific performance' in the eighth meeting of the EG (p. 2) was pointed out.

[17] The latter aspect even gives rise to a whole special trade, so called string sales, see Bridge (1991).

This phenomenon denotes that international commercial contracts are different from domestic commercial contracts in that they encounter different causes of irregularities in contractual performance which cannot be addressed by national legislators due to the territorial restrictions of their jurisdiction.

2.3.2 *...Leading to Specialised Infrastructure in Arbitration and Public Law Initiatives*

The specific nature of international commercial contracts governing transactions which span several countries and are often even delocalised in nature such as string contracts also calls for special settlement procedures, and in the absence of international courts of commercial law this role is entrusted with arbitration tribunals by commercial contract parties. These are at the forefront nowadays of applying the aforementioned special substantive law of international trade which arises from customs and usage but also consists of model laws and uniform law rules sometimes in the form of conventions drafted by UNIDROIT and UNCITRAL or even European scholarship such as PECL. The reason why state courts are less often seen to apply these legal instruments can be found mainly in private international law, or the conflict of laws, which still favours the application of the domestic law of a country and does not give effect to transnational non-state international contract law.[18] State involvement in an infrastructure for international trade comes closest to the actual transactions perhaps by concluding investment treaties. As mentioned above most other state initiated activity in the form of public law is of a regulatory nature or concerns business organisation by way of developing international company law.

2.4 Choice of Law Issues and Need for Transnational Contractual Regime

As is the case in a domestic setting, international traders also need a general contract law to govern their contracts complementing the contractual terms that they develop either on a purely individual basis or collectively for use in different branches. In addition to the application of national contract laws by way of the rules of private international law the above mentioned 'soft law' or instruments of *lex mercatoria* are possible sources of contract law to resolve disputes arising out of international commercial contracts. The latter type of law is of particular interest in this context. What is the need for specialised domestic and transnational contract law (2.4.1.) and how can it be given effect in an international contractual dispute (2.4.2.)?

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[18] See in more detail 3. below.

2.4.1 Is There a Need for a Specialised Substantive Commercial Contract Law?

Just as we can show that international commercial contracts contain typical clauses addressing typical risks and problems occurring within the course of contractual formation and performance there might also be a corresponding need for specialised rules of contract law applying specifically to commercial contracts rather than to contracts in general or non-commercial contracts.

2.4.1.1 European *Acquis*

Does the European *acquis* make such a distinction?

To What Extent is There a Special 'Law Merchant' in that Commercial Contracts are Treated Different from Other Contracts?

There are currently no explicit substantive rules of contract law enacted on the level of European Union. The Union has however promoted work in this area as mentioned above with the drafting of the potential CFR and the predecessor, the PECL. The most recent discussion of the groups of experts does expressly focus on so called B2B constellations specifically for the first time. Whether this covers the matter comprehensively will be considered below (2.4.1.2).

The resulting new Common European Sales Law Proposal does combine rules on consumer and business contracts accordingly.

How Does the Acquis Influence Contract Law?

The European Union's *acquis communautaire* provides of course a great amount of rules directly impacting on the contractual content of contracts drafted under the scope of the directives and regulations regulating the different areas of the internal market in its famously fragmented way. This fragmentation has however led to a different and new phenomenon within the European private law—it focuses more on the contracting parties than on the nature of the contract and it has therefore created a range of identities of contracting parties according to which role the party plays in the different areas of Community trade. Those identities are that of consumer, entrepreneur, professional, service provider, insurer and so forth. While it is clear that there is a distinction between a commercial party and a consumer as a supposedly non-commercial party these identities do not correspond to the traditional notions of merchant and non-merchant in many domestic European contract laws (see below 2.4.1.2) and they do also not correspond to the technique used in international codifications like the CISG where the purpose of the contract

is defining the scope of the law, not the role of the acting parties in the contract. So, while traditional contract laws remain neutral as to the role of the parties except for the notion of merchant which is carefully defined, the new international instruments describe the contract rather than the role of the parties while the European *acquis* has developed a third method by creating various roles for the parties in a range of typical contracts regulated by the European legislature. The absence of an overarching concept clearly poses part of the problems that international commerce faces and which is a problem academia needs to tackle and provide suitable concepts for its solution in the longer term.

2.4.1.2 Substantive 'Law Merchant' in Domestic Laws and Uniform Instruments

Most 'continental' or 'civil law' domestic laws have a specialised set of rules applying to merchants. These are either organised in a separate commercial code or contained in the general civil code. The term merchant is thereby not used in an informal way but rather strictly defined. Whether or not a person is a merchant depends on the nature and size of his or her business—what the trade is and what level of organisation it requires. When someone qualifies as a merchant specific rules apply imposing for instance book keeping duties and accounting standards. Companies are also classed as merchant or non-merchant. In fact, this distinction is of substantial significance in the traditional civil law as a number of contract law, company law and taxation law consequences are dependent on this definition.

Typical Instances of Contractual 'Sonderrecht'

In terms of contract law there are a number of rules that differ from the general rules which apply to non-merchants. These rules required specific justification under German law according to the constitution, Article 3 GG[19] (equal treatment) and have been called 'Sonderprivatrecht der Kaufleute' (special law of merchants) justified with the special skills they have or must be deemed to have. As much as this may serve as a justification of special law merchant, it does not explain its existence.

The law merchant has a very long tradition in European jurisdictions. Its origins reach well back to the feudal systems. In those systems the monarchs conceded special privileges to the class of merchants as they depended on their financial support.[20] Many of these privileges were not given to other subjects which were organised in different classes and categories each having limited rights towards the sovereign. In Germany, Austria and Switzerland, this was particularly apparent in

[19] *Grundgesetz*, Basic Law, the German constitution.

[20] Cf. for example Grossi (2010), p. 119/123 and Schmoeckel (2008), p. 93 (No. 93).