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Possible future work in the area of international contract law

Proposal by Switzerland on possible future work by UNCITRAL in the area of international contract law

Note by the Secretariat*

I. Introduction

1. In preparation for the forty-fifth session of the Commission, the Government of Switzerland submitted to the Secretariat a proposal in support of future work in the area of international contract law. The English version of that note was submitted to the Secretariat on 2 May 2012. The text received by the Secretariat is reproduced as an annex to this note in the form in which it was received.

* This document transmits a proposal by a Member State. It was submitted less than ten weeks before the opening of the session, upon receipt of the proposal.

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Annex

I. Executive Summary

The global aggregate volume of trade of goods has again significantly increased over the last decade. Although modern means of communication facilitate access to foreign law, differences in domestic law of contracts remain a burden on international trade. International endeavours such as the 1980 Convention on Contracts for the international Sale of Goods (CISG) have greatly improved the level of legal certainty for many parties to international sale of goods contracts. However, that Convention leaves important areas to applicable domestic law. Over the last 30 years, numerous endeavours have been undertaken to elaborate sets of uniform contract law on a regional scale. Yet, where successful, those efforts may have made international contracting even more complex. Having said this, they have evidenced the need for harmonization and may have cast ground work for further thought.

Today, Switzerland believes that time has come for UNCITRAL (i) to undertake an assessment of the operation of the 1980 Convention on Contracts for the international Sale of Goods and related UNCITRAL instruments in light of practical needs of international business parties today and tomorrow, and (ii) to discuss whether further work both in these areas and in the broader context of general contract law is desirable and feasible on a global level to meet those needs.

II. Introduction

Due to globalization, the overall development of international trade over the last half century is startling. Without having regard to the dramatic decrease of world merchandise exports in 2009, which however was basically equalized in 2010, it may be useful to have a look at the demonstrated trend up to 2008. World Trade Organization figures (WTO) for 2008 indicate that worldwide merchandise export trade amounted to USD 15’717 billion and worldwide merchandise import trade to USD 16’127 billion. These figures are approximately 100 times more than 50 years ago and more than 10 times the level at the time of the signing of the United Nations Convention on Contracts for the International Sale of Goods (CISG) in 1980. The average annual growth from 2000 to 2008 was more than 5 per cent for both exports and imports worldwide. No longer is the highest growth found in North America, Europe and Japan, but instead it is the transition economies from different points of the globe — particularly China, Brazil, Russia, and some African countries.

It goes without saying that different domestic laws form an obstacle for international trade as they considerably increase transaction costs for market participants. Different surveys conducted during the last years revealed that traders themselves conceive differences in contract law as one of the main obstacles for cross-border transactions. They include the difficulty in ascertaining the content of an applicable contract law, obtaining legal advice, negotiating the applicable law as well as adapting standard terms to different domestic laws. Unsurprisingly, trade has always been the motor for harmonization and unification of contract law in

particular since the 19th century starting on a domestic level and turning to the international level in the 20th century. Notably, in the area of sales law, in the 1960s the Uniform Law on the Formation of Contracts for the International Sale of Goods (ULF) and the Uniform Law on the International Sale of Goods (ULIS) were the first endeavours in unifying sales law at an international level.

Today's international sales practice shows that contracts — by the choice of the parties — tend to be governed by a closed circle of domestic laws, even though those laws may not necessarily be suitable to adequately govern international contracts. In Switzerland's view, this is evidence that UNCITRAL ought to discuss and assess whether the practical needs of today's and tomorrow's international business communities might not be better served by uniform rules covering the full array of legal issues that arise in a contractual business to business (b2b) relationship.

III. United Nations Convention on Contracts for the International Sale of Goods (CISG)

It was exactly against this background that UNCITRAL started working on the unification of sales law in 1968, culminating in the Convention on Contracts for the International Sale of Goods (CISG) which entered into force on 1 January 1988. The CISG proved to be the most successful international private law convention worldwide. Today there are 78 contracting States with the number continuously increasing. According to WTO trade statistics, nine of the ten largest export and import nations are contracting States, with the United Kingdom of Great Britain and Northern Ireland being the only exception. It can be assumed that approximately 80 per cent of international sales contracts are potentially governed by the CISG.

Moreover, a truly great success is the strong influence the CISG has exerted at both the domestic and international level. The Uniform Act on General Commercial Law by the Organization for the Harmonization of Business Law in Africa (OHADA) in its sales part is in many respects practically a transcript of the CISG. The UNIDROIT Principles of International Commercial Contracts, the Principles of European Contract Law, the Draft Common Frame of Reference and now the Draft Common European Sales Law are all modelled on the CISG. Furthermore, the EC Consumer Sales Directive heavily draws on the CISG. Similarly, the Sale of Goods Act in the Nordic Countries, the modernized German Law of Obligations, the Contract Law of the People's Republic of China and other East Asian Codifications, and the majority of the recent post-Soviet codifications in Eastern Europe, Central Asia, and in two of the Baltic States build on the CISG. Likewise, the draft for a new Civil Code in Japan follows the CISG. It is reported that in developing countries the CISG is used to teach traders the structures of contract law so as to improve their level of sophistication.

Despite its worldwide success, the CISG is merely a sales law convention that nevertheless covers core areas of general contract law. In addition to the obligations of the parties and typical sales law issues (e.g. conformity of the goods, passing of risk etc.), it contains provisions on the formation of contracts and remedies for breach of contract. Still it remains a piecemeal work, leaving important areas to the applicable domestic law.

IV. Other UNCITRAL endeavours

In addition to the CISG, UNCITRAL has embarked upon the unification in many other areas of international trade. Some of these instruments again touch upon various questions of general contract law,[1] especially the 1974 Convention on the Limitation Period in the International Sale of Goods, the 1983 Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance, the 1992 UNCITRAL Legal Guide on International Countertrade Transactions, and the 2005 United Nations Convention on the Use of Electronic Communications in International Contracts. However, this still leaves important areas to domestic law.

V. International initiatives in the area of general contract law

During the last 30 years, there have been numerous endeavours around the globe to elaborate sets of uniform contract law.

1. UNIDROIT

On a global scale, the UNIDROIT Principles of International Commercial Contracts (PICC) are probably the best-known example of an international venture to harmonize general contract law. Their 1994 version mostly covered areas already dealt with under the CISG, and included validity issues. The 2004 version added issues such as the authority of agents, contracts for the benefit of third parties, set-off, limitation periods, assignment of rights and contracts, and transfer of obligations. Most recently, the 2010 version contains a chapter on illegality and a section on conditions as well as detailed rules on the plurality of obligors and obligees and on the unwinding of contracts. In short, the PICC 2010 now cover all areas that are perceived as contract law in most legal systems.

There is no doubt that the substantive qualities of the PICC will constitute an important source of inspiration for any future work of UNCITRAL on the assessment of its own instruments as well as in the broader context of related issues of general contract law. Beyond this, future UNCITRAL work will greatly benefit

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[1] 1974 Convention on the Limitation Period in the International Sale of Goods; 1978 United Nations Convention on the Carriage of Goods by Sea — the "Hamburg Rules"; 1980 United Nations Convention on International Multimodal Transport of Goods; 1983 Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance; 1988 United Nations Convention on International Bills of Exchange and International Promissory Notes; 1991 United Nations Convention on the Liability of Operators of Transport Terminals in International Trade; 1992 UNCITRAL Legal Guide on International Countertrade Transactions; 1992 UNCITRAL Model Law on International Credit Transfers; 1995 United Nations Convention on Independent Guarantees and Stand-by Letters of Credit; 1996 UNCITRAL Model Law on Electronic Commerce with Guide to Enactment, with additional article 5 bis as adopted in 1998; 2001 UNCITRAL Model Law on Electronic Signatures with Guide to Enactment; 2001 United Nations Convention on the Assignment of Receivables in International Trade; 2005 United Nations Convention on the Use of Electronic Communications in International Contracts; 2007 UNCITRAL Legislative Guide on Secured Transactions; 2007 Promoting confidence in electronic commerce: legal issues on international use of electronic authentication and signature methods; 2008 United Nations Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea — the "Rotterdam Rules"; 2010 UNCITRAL Legislative Guide on Secured Transactions: Supplement on Security Rights in Intellectual Property.

from the PICC's experience in permeating legal practice. In particular, UNCITRAL may wish to remain conscious that many courts will decline to give effect to a choice of law in favour of a soft law instrument. Also UNCITRAL may wish to discuss early on whether a mere opt-in scheme would be desirable in light of the problems described above.

2. Regional endeavours

On a regional level, a number of initiatives can be discerned.

Several approaches can be found in Europe which all aimed at a European Civil Code or at least a European Contract Law. First and foremost, the Principles of European Contract Law (PECL) shall be mentioned here. Starting with preparatory work in the 1980s, PECL were published in three parts (1995, 1999, 2003), Part I covering performance, non-performance and remedies, Part II covering formation, agency, validity, interpretation, content and effects of contracts, and Part III covering plurality of parties, assignment of claims, substitution of the debtor, set-off, limitation, illegality, conditions, and capitalization of interest. The PECL have a clear European focus, but also take into account the US-American Uniform Commercial Code as well as the Restatements on Contracts and Restitution. Like the PICC, the PECL are so-called soft law. Although the parties at least in arbitration may choose the PECL, there are no reported cases where this has happened.

More recently, the Study Group on a European Civil Code and the Research Group on EC Private Law published the Draft Common Frame of Reference (DCFR) in 2009. In contrast to PICC and PECL, the DCFR not only addresses general contract law but virtually all matters typically addressed in civil codes except family law and law of inheritance. The DCFR was, however, met with severe criticism not only with regard to the general idea of the project but especially with regard to drafting and style as well as specific solutions in the area of general contract and sales law.

Building on the DCFR, the European Commission published a proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law (CESL) in October 2011. Thus, the idea of a general contract law on the European level was not pursued anymore but rather narrowed down to sales law. The content of CESL is almost identical to that of the CISG and the United Nations Limitation Convention with additional provisions on defects of consent, unfair contract terms, pre-contractual information duties, and contracts to be concluded by electronic means. Most notably, in contrast to the CISG, CESL not only applies to b2b contracts but is in fact primarily aimed at contracts with consumers. CESL, too, is an opting-in instrument. The future of this instrument is yet to be seen.

In Europe, a few more private initiatives undertook similar projects, among them the Academy of European Private Lawyers that issued the Preliminary Draft for a European Code (2001) and the Trento Common Core Project.

In Africa, first regard is to be given to the OHADA's Uniform Act on General Commercial Law (1998, amended 2011). As mentioned above, the sales part of this act strongly relies on the CISG, although it contains certain modifications. In addition to this act, OHADA initiated works on a Uniform Act on Contract Law. A draft was prepared in cooperation with UNIDROIT and published in 2004, heavily

drawing on PICC. At the time being, the future of this project is uncertain. Considerations for the harmonization of contract law based on the current international experience are also voiced in the framework of the East African Community.

Another recent private initiative aiming at the elaboration of Principles of Asian Contract Law (PACL) can be found in Asia since 2009. Among others, participants come from Cambodia, Viet Nam, Singapore, China, Japan, and South Korea. Until today, the chapters on formation, validity, interpretation, performance and non-performance of the contract have been finalized.

Likewise, in Latin America, general contract principles are being developed since 2009 within the framework of the Proyecto sobre Principios Latinoamericanos de Derecho de los Contratos hosted by a Chilean university. The countries covered up to now are Argentina, Uruguay, Chile, Colombia and Venezuela (Bolivarian Republic of). However, the European approach seems to be considered as well.[2]

3. International Chamber of Commerce

For decades, important contributions to the harmonization of international trade law have emanated from the International Chamber of Commerce (ICC). As far back as 1936, the ICC published the International Commercial Terms (Incoterms®). Their latest version, the 8th edition, dates from 2010. Although in many sales contracts they are agreed upon and thus being of utmost practical importance, Incoterms® cover only a small fraction of the parties' obligations in an international sales contract. With the Uniform Customs and Practice for Documentary Credits (UCP), the ICC has created another important instrument to facilitate international trade. Finally, the ICC provides innumerable model contracts and clauses for use in various types of international commercial transactions.

VI. Desirability: UNCITRAL to assess operation of CISG and desirability of further harmonization and unification of related issues of general contract law

Switzerland expects the number of CISG contracting states to keep rising. Despite this worldwide success in bringing about unification of sales law, the CISG cannot satisfy all the needs of the international commercial community in relation to contract law.

The shortcomings of the CISG firstly relate to the areas not at all covered by the Convention.[3] Furthermore, many issues that were still highly debated in the 1970s had to be left open in the CISG (e.g. the problem of battle of the forms, specific

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[2] Along these initiatives, a trend aiming at building common regional law by using global texts also exists, for instance in the framework of the North American Free Trade Agreement (NAFTA), and now also in the framework of the Dominican Republic — Central America Free Trade Agreement (DR-CAFTA).

[3] Especially, the CISG does not deal with agency, validity questions such as mistake, fraud, duress, gross disparity, illegality, and control of unfair terms, third party rights, conditions, set-off, assignment of rights, transfer of obligations, assignments of contracts, and plurality of obligors and obligees.

performance, and applicable interest rate). Some areas covered by the CISG have in the meantime proven to need more detailed attention, such as the rules on unwinding of contracts. Finally, conventions meant to supplement the CISG, such as the 1974 United Nations Convention on the Limitation Period in the International Sale of Goods and the 2005 United Nations Convention on the Use of Electronic Communications in International Contracts, have not attracted as many members as the CISG, thereby diminishing their unifying effect.

Switzerland is of the view that time has come for UNCITRAL to reflect on these issues of general contract law in the context of international sales — and possibly other types of — transactions from a global perspective. Regional endeavours to harmonize and unify general contract law cannot meet the needs of international trade. Rather, different legal regimes in different regions lead to fragmentation. Instead of saving transaction costs and thus facilitating cross-border trade, international contracting may become even more complicated. Regional unification adds yet another layer to domestic rules and the well-established instrument of the CISG. Additionally, in many instances, not only does the terminology used in the general contract law instruments differ from that of the CISG, which in itself leads to confusion; frequently, there will also be contradicting solutions to one and the same legal problem. Finally, regionalization of legal systems reduces the number of cases decided on a truly international level and hence has a negative impact on the predictability of the outcomes.

Given its mandate, UNCITRAL clearly seems the most appropriate forum for such a project. According to General Assembly Resolution 2205 (XXI), para. 8: "The Commission shall further the progressive harmonization and unification of the law of international trade by: (c) Preparing or promoting the adoption of new international conventions, model laws and uniform laws […]."

VII. Feasibility of further work in the area of international contracts

Future work in the area of general contract law could cover a considerable array of issues.[4] At this point, work should start with the identification of the areas where a practical need for UNCITRAL work is felt that would be complementary to existing instruments. At the same time and possibly in parallel, UNCITRAL should carefully discuss what particular form UNCITRAL's future work on general contract law might take. Indeed, what delegations are able and willing to agree to on substance is often closely linked to the question of the possible form of an instrument.

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[4] In particular: **general provisions**, among others: freedom of contract, freedom of form; **formation of contract**, among others: offer, acceptance, modification, discharge by assent, standard terms, battle of forms, electronic contracting; **agency**, among others: authority, disclosed/undisclosed agency, liability of the agent; **validity**, among others: mistake, fraud, duress, gross disparity, unfair terms, illegality; **construction of contract**, among others: interpretation, supplementation, practices and usages; **conditions**; **third party rights**; **performance of contract**, among others: time, place, currency, costs; **remedies for breach of contract**, among others: right to withhold performance, specific performance, avoidance, damages, exemptions; **consequences of unwinding**; **set-off**; **assignment and delegation**, among others: assignment of rights, delegation of performance of duty, transfer of contracts; **limitation**; **joint and several obligors and obligees**.

General contract law belongs to the core of private law in any domestic legal system. It has usually developed in a long tradition. It might therefore be wise for UNCITRAL, given its mandate, to focus its discussions on international commercial contracts only, without interfering with questions related to purely domestic contracts.

VIII. Conclusion

As has been shown, there is an urgent need for a global reflection on the further unification of contract law beyond the endeavours already carried out by UNCITRAL. In light of the above, Switzerland proposes that UNCITRAL give a mandate for work to be undertaken in this area.

Switzerland looks forward to fruitful debates on the scope, timing, form and nature of such work, including the question of coordination with international organizations and institutions active in related fields.