

WHO NEEDS A UNIFORM CONTRACT LAW, AND WHY?

*Ingeborg Schwenzer**

Contract law and especially commercial contract law has always been at the forefront of harmonization and unification of private law. The reason is that different domestic laws are perceived as an obstacle to international trade.¹ This has always been true and still holds true nowadays as has been proven by many recent field studies around the world.² In the 19th century this prompted unification at the nation state level all over Europe; in the 20th century the Uniform Commercial Code in the United States can be mentioned as a prominent example as well as endeavours especially on the European level³ but also in Africa⁴. Most recently there are similar movements in East Asia with PACL.⁵ Professor Schwenzer here briefly discusses who needs a uniform contract law and why.

* Prof Dr Ingeborg Schwenzer, LL.M. (Berkeley) is a professor of private law at the University of Basel. The author is deeply indebted to ref iur Lina Ali for editing the footnotes. All web pages were last accessed on 14 February 2013.

- 1 Cf Ewan McKendrick "Harmonisation of European Contract Law: The State We Are In" in Stefan Vogenauer and Stephen Weatherill (eds) *The Harmonisation of European Contract Law, Implications for European Private Laws, Business and Legal Practice* (2006) 5, 14-15.
- 2 See only Stefan Vogenauer and Stephen Weatherill "The European Community's Competence to Pursue the Harmonisation of Contract Law – an Empirical Contribution to the Debate" in *The Harmonisation of European Contract Law, Implications for European Private Laws, Business and Legal Practice*, above n 1, 105, 125-126.
- 3 See, for example, the Principles of European Contract Law (PECL) (1999), available at <http://frontpage.cbs.dk/law/commission_on_european_contract_law/PECL%20engelsk/engelsk_partI_og_II.htm> for more information on PECL see Ole Lando and Hugh Beale (eds) *Principles of European Contract Law, Parts I and II* (2000) and Ole Lando et al (eds) *Principles of European Contract Law, Part III* (2003).
- 4 See, for example, the Uniform Act on General Commercial Law by the Organization for the Harmonization of Business Law in Africa (OHADA) (Acte uniforme portant sur le Droit commercial général) available at <www.ohada.org/presentation-generale-de-lacte-uniforme/telechargements1.html>.
- 5 For further information on the Principles of Asian Contract Law (PACL) see Shiyuan Han in this issue; see also <www.fondation-droitcontinental.org/jcms/c_7718/projet-commun-de-droit-des-contrats-en-asie-du-sud-est>.

In general, on the international level we may roughly distinguish three different scenarios of contracting parties.

In the first group we find parties from countries where the same language is spoken. In general, these countries also belong to the same legal family with differences between the legal systems being minor if not negligible.⁶ This first of all applies to parties from English-speaking Common Law countries, like parties from the United States and Canada, from Australia and New Zealand, or from India and the United Kingdom. But it also holds true for other scenarios like those of parties from France and Cameroon, from Argentina and Mexico, or from Germany and Austria. First, it is well possible that the parties can agree on one of their respective legal systems. If this is not the case they can be expected to choose the law of a third country with the same language and belonging to the same legal tradition. In any case, the outcome of a possible dispute – be it litigated or arbitrated – will be more or less predictable. This group comes close to purely domestic contracts and there is hardly any need for a unification of contract law as the parties would still prefer the law that is more familiar to them than any unified law.

In the second group a – most probably western – company with overwhelming bargaining power contracts with an economically weaker party. The powerful company usually will be able to impose anything that it wants on its contract partner. It has sophisticated in-house lawyers who carefully draft the contract preferably with a choice of law clause designating its own domestic law. If this is combined with a forum selection clause designating the domestic courts of the economically stronger party usually there will be no problems at least not for the powerful party and thus no need for a uniform contract law. The domestic courts apply their domestic law which in general will yield predictable and satisfactory results for the company seated in this country. The picture may immediately change, however, if the other party brings suit in the domestic courts of its own country and there the forum selection clause and/or the choice of law clause are not honoured.⁷ But even if these courts accept the choice of law, it is a totally different question how the courts will apply this foreign law. By agreeing on arbitration many of the aforementioned imponderabilities may be circumvented. Still,

6 For an overview of the legal families with regard to domestic sales laws see Ingeborg Schwenzer et al *Global Sales and Contract Law* paras 2.01-2.135 (2012).

7 A prominent example is Brazil, where the validity of choice of law and choice of forum clauses is highly controversial. For more information see Dana Stringer, *Choice of Law and Choice of Forum in Brazilian International Commercial Contracts: Party Autonomy, International Jurisdiction, and the Emerging New Way* (2005-06) 44 Colum J Trans'l L 959.

problems of ascertaining and proving the chosen law – as will be described below – can be encountered.

The third group is probably by far the biggest one. It consists of parties from countries where different languages are spoken, be they from a Common Law and a Civil Law country or from two Civil Law countries. If none of the parties has the economic power to impose its own law upon the other party, ie where the parties are dealing at arm's length with one another, more often than not they will agree on a third law. This might be a law that appears to be closely related to both parties because it influenced the law of both parties' countries in one way or the other, like it is true for German law for example in relation to Italian and Japanese or Korean law.⁸ If no such common background exists more often than not the parties think to solve their problems by resorting to what they believe is a "neutral law" thereby often confusing political neutrality with suitability of the chosen law for international transactions.⁹ In particular, this seems to be the case with Swiss law.

In such a case the first hurdle that the parties have to take, at least once it comes to litigation or arbitration, is the language problem. They have to investigate a foreign law in a foreign language. If the language is not the one of the litigation or arbitration in question all legal materials – statutes, case law and scholarly writings – must be translated into the language of the court or of the arbitration. Legal experts are required to prove the content of the law that is chosen by the parties. In some countries the experts may be appointed by the court, in others as well as generally in arbitration each party will have to come forward with sometimes even several experts.¹⁰ Needless to say, the procedures can be very expensive and may be prohibitive for a party who does not have the necessary economic power to invest these monies in the first place. This may even be harsher under a procedural system where each party bears its own costs regardless of the outcome of the proceedings as is especially the case under the so called "American Rule" as it

8 For German influences in the East Asian region see Schwenzer et al, above n 6, paras 2.123-2.127. For German influences on Italian civil law see Konrad Zweigert and Hein Kötz *Einführung in die Rechtsvergleichung* (3rd ed, 1996) 102-104.

9 Cf Christiana Fountoulakis "The Parties' Choice of 'Neutral Law' in International Sales Contracts" (2005) 7 Eur J L Reform 303, 306-07.

10 Cf for court proceedings Michele Taruffo "Evidence" in Mauro Cappelletti (ed) (2010) 16 Int'l Enc Comp L paras 7.65-7.66; cf for arbitration proceedings Gabrielle Kaufmann-Kohler "Globalization of Arbitral Procedure" (2003) 36 Vand J. Transnat'l L 1313, 1330; Siegfried H Elsing and John M Townsend "Bridging the Common Law-Civil Law Divide in Arbitration" (2002) 18 Arb Int'l 59, 63-64; see eg, Article 25(3) ICC Arbitration Rules (2012); Article 27(2) UNCITRAL Arbitration Rules (2010).

applies not only in the US but also for example in Japan.¹¹ However, even if a party is willing to bear all these costs to prove a foreign law in court or arbitration the question as to how this law is interpreted and applied can be highly unpredictable.

Second, the parties will very often be taken by surprise when they realize the true content of the law that they have chosen. Just to give you one example that in my view is rather typical for an international contract between two SMEs; a sales contract between a Chinese seller and an Italian buyer. As German law has had great influence on both Chinese and Italian law¹² the parties – although none of them speaks German – believe to have a rough idea of German law and agree on German law to govern their contract. The Chinese seller, for its standard form contract, copies a form it finds on the internet including a limitation of liability clause. Whereas the clause may well live up to the standards of the US UCC it is totally invalid under German law that provides for substantive control of standard terms even in b2b relationships.¹³ This is certainly not what both parties wanted and expected in choosing German law.

Third, the outcome of the case under the law chosen may be highly unpredictable. This especially holds true if the parties choose Swiss law. As Switzerland is such a small country many central questions of contract law have not yet been decided by the Swiss Supreme Court or if so the decision may have been rendered decades ago and is disputed by scholarly writings. This makes the outcome of the case often rather unpredictable - another reason that may well prevent a party from pursuing its rights under the contract.

Furthermore, especially Swiss domestic contract law in core areas is not suitable to international contracts. This can be demonstrated by reference to only two examples. First, the Swiss Supreme Court distinguishes between *peius*, ie defective goods, and *aliud*, ie different goods;¹⁴ the latter giving the buyer the right to demand performance during ten years after the conclusion of the contract whether it gave notice of non-performance or not¹⁵, while the former requires the buyer to

11 For a comparative overview as to how litigation costs and attorney fees are allocated between the parties in civil litigation see Mathias Reimann (ed) *Cost and Fee Allocation in Civil Procedure* (2012).

12 Cf above n 8.

13 Cf §§ 305-310 German Civil Code.

14 Bundesgericht [BGer] [Federal Court] 5 December 1995, 121 Entscheidungen des Schweizerischen Bundesgerichts [BGE] III 453 (Switz).

15 Cf Article 127 Swiss Civil Code.

give prompt notice of defect according to art 201 OR to preserve any remedies for breach of contract. Where the line between *peius* and *aliud* will be drawn in a particular case can be extremely difficult to predict.¹⁶ The second example is compensation of consequential losses.¹⁷ Whether there is a claim for damages without fault depends on the number of links in the chain of causation.¹⁸ Extremely short periods for giving notice of defects¹⁹ furthermore militate against domestic Swiss law for the international context. Similar examples could be drawn from many other domestic legal systems.

This background illustrates the urgent need to further harmonize if not unify general contract law.

UNCITRAL would be the most appropriate place for such a project. Whereas any regional endeavour might mainly focus on the laws of the respective countries involved, UNCITRAL has the chance to embark upon a more truly global reflection. Indeed, UNCITRAL is the only forum with universal participation, ie all the regions of the world have a chance to contribute on equal footing.²⁰ This is the reason why in 2012 Switzerland made a proposal for the 45th session of UNCITRAL on possible future work by UNCITRAL in the area of international contract law.²¹ However, this proposal did not suggest how the possible future work should be conducted; especially what kind of instrument should be aimed at if one were to come to the conclusion that such future work is desirable and

16 See Fountoulakis, above n 9, 308-09; for more information on the differentiation between *peius* and *aliud* see Heinrich Honsell, art 206 paras 2-3, in *Basler Kommentar, Obligationenrecht I* Heinrich Honsell et al (eds) (5th ed, 2011).

17 Article 208(2) Swiss Civil Code.

18 See Bundesgericht [BGer] [Federal Court] 28 November 2006, 133 Entscheidungen des Schweizerischen Bundesgerichts [BGE] III 257, 271 (Switz); Heinrich Honsell, Art 208 paras 7-8, in *Basler Kommentar, Obligationenrecht I*, above n 16.

19 Cf Article 201(1) Swiss Civil Code, according to which the notice must be made immediately (*sofort*); see also Bundesgericht [BGer] [Federal Court] 27 June 1950, 76 Entscheidungen des Schweizerischen Bundesgerichts [BGE] II 221, 225 (Switz.) (notice within four days in time as these included a Sunday).

20 UNCITRAL's membership comprises states from Africa, Asia, Eastern Europe, Western Europe, Latin America and the Caribbean, thereby ensuring that the main economic and legal systems of the world are represented. For an overview of the today 60 member states see UNCITRAL, *A Guide to UNCITRAL: Basic Facts about the United Nations Commission on International Trade Law* 37-41 (Annex II) (2013), available at <http://www.uncitral.org/pdf/english/texts/general/12-57491-Guide-to-UNCITRAL-e.pdf> [hereinafter *A Guide to UNCITRAL 2013*].

21 United Nations Commission on International Trade Law, 45th session, New York, 25 June-6 July 2012, *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*, A/CN.9/758 (8 May 2012), available at <www.uncitral.org/uncitral/commission/sessions/45th.html>.

feasible. Let me give some thoughts on this question emphasizing that I am speaking entirely for myself and in no way voicing the official Swiss opinion.

In principle, there is the choice between a convention and a model law. A convention is designed to unify law by establishing binding legal obligations.²² Its aim is to achieve a very high level of harmonization.²³ Although there may be the possibility of having some reservations allowing State Parties a certain but very limited degree of choice, such reservations are easily discernible without the need to have recourse to the respective domestic law.²⁴ Thus, a convention provides the highest level of predictability for private parties. In contrast, a model law only provides for a legislative text that is recommended to State Parties.²⁵ It is used where State Parties want to retain flexibility in implementing or where strict uniformity is not desirable or necessary.²⁶ Furthermore, a model law may be finalized and approved by UNCITRAL at its annual session whereas a convention still, in principle, necessitates a diplomatic conference.²⁷ Although, at the political level it may be certainly easier to convince state governments to agree to a model law allowing them more leeway, the needs of international commerce clearly militate in favour of a convention. Even if states were to implement a model law not only could they deviate from the text of such a model law which would make it difficult to ascertain the content of the applicable law in a specific case. Moreover, there is no obligation for courts of a state that has implemented a model law to regard its international character and the need to promote uniformity in its interpretation, as it is nowadays provided for in all international conventions.²⁸ Thus, a statute implementing a model law is purely domestic law and is legitimately interpreted against the respective domestic background. If a model law may bring about some harmonization at the beginning this will soon be lost. This can especially be expected in a traditional field such as contract law where firm dogmatic conceptions and convictions prevail that have been shaped over centuries and that every lawyer has internalized from the very first day in law school.

The scope of the envisaged instrument on general contract law should be similar to the one of the CISG except that it should apply to all kinds of contracts and not

22 *A Guide to UNCITRAL 2013*, above n 21, at 13.

23 *Id* at 14.

24 See, for example, Articles 92-96 CISG.

25 *A Guide to UNCITRAL 2013*, above n 21, at 14.

26 *Id* at 14.

27 *Id* at 15.

28 See only Article 7(1) CISG.

just to sales. That means in the first place that the instrument should only be concerned with international contracts but not with purely domestic ones. There is no reason and it is not the mandate of UNCITRAL to interfere with domestic relationships.²⁹ If a State feels the need to simplify the situation for its citizens by having the same law applied to domestic as well as to international contracts it is free to do so and implement correspondent domestic legislation as some States already have chosen in the relation to the CISG.³⁰

Like the CISG the instrument on general contract law should be confined to b2b contracts without touching b2c relationships. Except for internet transactions that become more and more international, b2c contracts to the very day are mostly domestic contracts. Consumer protection asks for mandatory rules which stands in sharp contrast to the need for freedom of contract in b2b contracts. It is not possible to juggle the needs of both – consumers and businesses – in one single instrument. The futility of such an endeavour has been demonstrated lately by the draft of a Common European Sales Law.³¹ Furthermore, the level of consumer protection still differs considerably around the world; an international consensus in this field probably cannot be achieved during the decades to come.

As regards the areas of contract law that should be addressed it is clear that the future uniform contract instrument should cover as many areas as possible. However, there are some fields where unification is more urgent than in others. The most important area where the gaps left by the CISG are most unfortunate because they endanger uniformity already reached are questions of validity. Although, it is now unanimously held that the CISG itself defines what is a question of validity left to domestic law and what is not³², many day-to-day contract problems are issues of validity. To name but a few: questions of consent, such as mistake, undue influence or fraud; and validity of individual clauses and standard terms, such as gross disparity, burdensome obligations, exclusion and limitation of liability clauses as well as fixed sums, ie penalty and liquidated

29 Cf for UNCITRAL's mandate *A Guide to UNCITRAL 2013*, above n 21, at 1-2.

30 Cf Ingeborg Schwenzer and Pascal Hachem "The CISG – Successes and Pitfalls" (2009) 57 *Am J Comp L* 457, 462-63.

31 See Ingeborg Schwenzer "The Proposed Common European Sales Law and the Convention on the International Sale of Goods" (2012) 44 *UCC LJ* 457. The draft forms Annex I of the *Proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law* COM(2011) 635 final (11 October 2012), available at <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0635:FIN:EN:PDF>>.

32 Ingeborg Schwenzer and Pascal Hachem, art 4 para 31, in Schlechtriem and Schwenzer, *Commentary on the Convention on the International Sale of Goods (CISG)* Ingeborg Schwenzer (ed) (3rd ed, 2010) with references.

damages clauses.³³ It is extremely burdensome to have these questions answered by domestic law which might well lead to frictions with unified law. Also very important are issues of the consequences of unwinding of contracts³⁴ and set-off³⁵. Other areas of contract law, such as third party rights, assignment and delegation, or joint and several obligors and obligees might not be at the forefront of desirability for unification.

If one considers working on further unification of contract law the route to be followed seems to be pretty clear. The starting point must be the CISG. It has received such tremendous acceptance that anything that might interfere with it must be refrained from.³⁶ Other UNCITRAL instruments, such as the 1974 Limitation Convention³⁷ or the 1983 Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance³⁸ should be given due consideration and it should be discussed whether they should be amended. Certainly, of utmost importance are the PICC.³⁹ Most valuable work has been completed by UNIDROIT and any duplication of efforts must be prevented. In essence, we face a similar situation as in 1968 when UNCITRAL started working on the CISG drawing heavily on the previous work done by UNIDROIT that had led to the Hague Conventions on the sale of goods, ULIF and ULF respectively.⁴⁰ However, there are certain contradictions between CISG and PICC that need to be

33 For an overview on how the issues of formation and validity of sales contracts are dealt with in the different legal systems see Schwenger et al, above n 6, paras. 9.01-22.25.

34 For an overview on how the unwinding of contracts is dealt with in the different legal systems see id paras 50.01-50.36.

35 For a comparative discussion on set-off see Christiana Fountoulakis *Set-off Defences in International Arbitration: A comparative analysis* (2011).

36 The CISG now has 80 member states with the number continuously increasing. Recently, the Brazilian Senate approved the text of the CISG. Upon completing the accession process Brazil will become the 79th contracting state. For a list of the current contracting states to the CISG see <www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG_status.html>. See also Ingeborg Schwenger and Pascal Hachem "The CISG – A Story of Worldwide Success" in CISG Part II Conference 119 Jan Kleinemann (ed) (2009).

37 Convention on the Limitation Period in the International Sale of Goods (1974), available at <www.uncitral.org/pdf/english/texts/sales/limit/limit_conv_E_Ebook.pdf>.

38 Available at <www.uncitral.org/pdf/english/texts/sales/contract/vol14-p272-273-e.pdf>.

39 UNIDROIT Principles of International Commercial Contracts (PICC) (2010), available at <www.unidroit.org/english/principles/contracts/principles2010/integralversionprinciples2010-e.pdf>.

40 For more information on the drafting history of the CISG see Peter Schlechtriem *Uniform Sales Law – The UN-Convention on Contracts for the International Sale of Goods* (1986) 17-21.

eliminated;⁴¹ in other areas the possible acceptance of PICC rules at a global level must be carefully scrutinized and discussed.

Having regard to what already has been achieved at the international level a global contract law appears to be feasible within a reasonable amount of time and without consuming too many resources needed elsewhere.

How would the global picture for internationally contracting parties change if there were an UNCITRAL instrument on general contract law?

First, this instrument – just like the CISG – could be expected to represent a good compromise between Common and Civil Law.⁴² It would be acceptable to any party regardless of its own legal background. It would be a truly neutral law.

Second, it would be drawn up in the six UN languages and would be translated into the languages of the states adopting this instrument and thus be readily available in court and arbitral proceedings rendering costly translations and expert testimony superfluous. Just as the CISG it could serve as a model for further harmonization of contract law also on a domestic level.⁴³ And it could be used to teach traders that cannot afford in-house counsel or legal advice the basics of contract law.⁴⁴

Third, it would lead to much more predictability in international contracts. It can be expected that the same mechanisms that now support and enhance the uniform application and interpretation of the CISG will also play a decisive role for such an instrument. It must be recalled that by now there are about 3000 published cases on the CISG⁴⁵, about 4000 publications freely accessible on the internet⁴⁶, we

41 For a comparison of the two instruments see Michael Joachim Bonell "UNIDROIT Principles of international commercial contracts and the United Nations Convention on Contracts for the International Sale of Goods – alternatives or complementary instruments?" (2000) *Bus L Int'l* 91, 94-96.

42 Cf for the CISG Ulrich Magnus "The Vienna Sales Convention (CISG) between Civil and Common Law – Best of all Worlds?" (2010) 3 *J Civ L Stud* 67.

43 Cf for the CISG as a role model for domestic legislators Schwenzer and Hachem, above n 31, at 462-463.

44 As it is true with regard to the CISG; cf Schwenzer et al, above n 6, para 3.21.

45 See for cases on the CISG, for example, the online case database CISG-online.ch, available at <www.globalsaleslaw.org/index.cfm?pageID=29> and the Pace Law School CISG database, available at <www.cisg.law.pace.edu/>.

46 See for publications freely accessible on the internet, for example, the online collection of scholarly writings at the Pace Law School CISG database, available at <www.cisg.law.pace.edu/>.

have CLOUT⁴⁷ – Case Law on UNCITRAL texts, we have the UNCITRAL Digest⁴⁸ and further institutions worldwide such as the CISG Advisory Council⁴⁹, that strive to guard uniformity. Commentaries with article by article comments will be published in different languages. Uniform standard forms that facilitate contracting will soon emerge on the basis of such an instrument and further add to predictability.

All in all it can be expected that an UNCITRAL instrument on general contract law may considerably save transaction costs. It may help companies with lesser funds to be able to pursue their legal rights under an international contract and thus further promote international trade. Finally, it can support the rule of law worldwide.

47 Available at <www.uncitral.org/uncitral/en/case_law.html>.

48 Available at <www.uncitral.org/uncitral/en/case_law/digests.html>.

49 For more information on the CISG Advisory Council and for the CISG Advisory Council Opinions see <www.cisgac.com/>.