

# The Parties' Choice of 'Neutral Law' in International Sales Contracts

Christiana Fountoulakis\*

## A. The Importance of Making the 'Right' Choice of Law

When negotiating an international contract, it is important to make the 'right' choice of law.<sup>1</sup> Why, one might ask, should emphasis be placed on which law governs the contract if most conflict of laws rules entitle the parties to draw up their agreement as they wish? The answer is that it is practically impossible for the parties to individually negotiate every point that may arise under a contract. In fact, the parties will usually only settle the main questions. The essential points in a contract for the sale and purchase of goods are the specification of the kind and quantity of the purchased goods, as well as their price. By including an INCOTERM<sup>2</sup> or another international trade term, the parties may settle further aspects which do not directly affect the reciprocal terms of the contract, such as the terms of delivery, passing of risk, insurance obligations, etc. However, the parties will usually not regulate every contingency.

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\* Dr. iur., Assistent Professor of Private Law, University of Basel, Switzerland.

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<sup>1</sup> Party autonomy in choice of law issues is nowadays, though not completely unrestricted (Article 3(3) of the Rome Convention 1980; § 187(2) Restatement of the Law (Second), Conflict of Laws 2d (1971)), a mere matter of course, *see* R. Weintraub, Functional Developments in Choice of Law for Contracts, 187 *Recueil des Cours* 239, at 271 (1984-VI); S. Symeonides, W. Perdue & A. Van Mehren, Conflict of Laws: American, Comparative, International 318 (1998); O. Lando, The Conflict of Laws of Contracts, General Principles, 189 *Recueil des Cours* 225, at 255 *et seq.* (1984-VI); O. Sandrock, *Handbuch der Internationalen Vertragsgestaltung*, Vol. I, para. 136 (1980); S. Leible, *Aussenhandel und Rechtssicherheit*, 97 *Zeitschrift für vergleichende Rechtswissenschaft* 286, at 288 (1998); H. Harries, Die Parteiautonomie in internationalen Kreditverträgen als Instrument der Vertragsgestaltung, in F. Kübler, H.-J. Mertens & W. Werner (Eds.), *Festschrift für Theodor Heinsius zum 65. Geburtstag am 25. September 1991*, 201 *et seq.* (1991); O. Sandrock, Die Bedeutung des Gesetzes zur Neuregelung des internationalen Privatrechts für die Unternehmenspraxis, 1986 *Recht der Internationalen Wirtschaft* 841, at 846; G. Wagner, The Economics of Harmonization: The Case of Contract Law, 39 *Common Market Law Review* 995, at 997 (2002); on the history of development of party autonomy in private international law *see* J. Püls, *Parteiautonomie: Die Bedeutung des Parteiwillens und die Entwicklung seiner Schranken im deutschen Rechtsanwendungsrecht des 19. und 20. Jahrhunderts* (1996).

<sup>2</sup> International Commercial Terms, developed by the International Chamber of Commerce (ICC) in Paris, France. The current version is the INCOTERMS 2000.

Where the contract volume is extraordinarily high, the parties normally make the effort to expressly negotiate as many terms of the contract as possible. One might think that here, the question of the applicable law is of secondary importance, since the parties will try to exhaust the full potential for leeway allowable under the applicable law, and it will not be worth making more detailed investigations into the *lex causae*. However, even in lengthy and meticulously drawn-up contract documents, it is not realistic for the parties to try to agree on every point that theoretically might occur. It remains important to know which law applies to the contract because that law governs those issues not expressly settled by the parties. Moreover, the parties will be interested in having the largest party autonomy possible, i.e. they will be looking for a *lex causae* which grants it in the desired extent. Making the ‘right’ choice of law is therefore essential.<sup>3</sup>

## **B. Looking for the Right Choice of Law: Choosing the Domestic Law of one of the Parties**

### **I. Both Parties Want Their Own Domestic Law to Apply**

In practice, the choice of the law that is to govern a contract is dominated by the respective interest of each party to have its own domestic law applied.<sup>4</sup> The parties are familiar with their own law and are convinced that they will save considerable costs in not being required to investigate the intricacies of a foreign law. If they have their own law applied, they do not have to consult external experts, but rather, can rely on their usual, well-acquainted legal advisors. Therefore, in order to save costs to investigate foreign laws and avoid increased legal uncertainty that might arise when applying an external law, the parties to an international contract will strive towards an application of their own law,<sup>5</sup> even if that law is less suitable for the transaction at hand than another law might be.<sup>6</sup>

<sup>3</sup> See also Harries, *supra* note 1, at 203 *et seq.*; P. Herbel, *Der internationale Unternehmensjurist – ein vaterlandsloser Geselle?*, in I. Schwenzer (Ed.), *Schuldrecht, Rechtsvergleichung und Rechtsvereinheitlichung an der Schwelle zum 21. Jahrhundert: Symposium aus Anlass des 65. Geburtstages von Peter Schlechtriem*, 1 at 9 (1999); P. Mankowski, *Überlegungen zur sach- und interessengerechten Rechtswahl für Verträge des internationalen Wirtschaftsverkehrs*, 2003 *Recht der Internationalen Wirtschaft* 2.

<sup>4</sup> See Harries, *supra* note 1, at 205; O. Remien, *Rechtseinheit ohne Einheitsgesetze?*, 56 *Rebels Zeitschrift für ausländisches und internationales Privatrecht* 300, at 310 (1992).

<sup>5</sup> See ICC Award No. 7710/1995, 2001 *Journal du Droit International* 1147, at 1150 *et seq.* (note by Y. Derains).

<sup>6</sup> E.-M. Kieninger, *Wettbewerb der Privatrechtsordnungen im Europäischen Binnenmarkt* 287 *et seq.* (2002); F. Oschmann, *Faktische Grenzen der Rechtswahl*, in E. Stiefel *et al.* (Eds.), *Iusto Iure: Festgabe für Otto Sandrock zum 65. Geburtstag* 25, at 31 (1995); T. Kadner Graziano, *Die Zukunft der Zivilrechtskodifikation in Europa – Harmonisierung der alten Gesetzbücher oder Schaffung eines neuen? – Überlegungen anlässlich des 200. Jahrestags des französischen Code Civil*, 2005 *Zeitschrift für Europäisches Privatrecht* 523, at 531.

## II. Inherent Problems When Persevering on One's Own Law: The 'Battle of Forms'

Conflicts are a given when each party insists on its domestic sales provisions. Where one party pushes its own law, it is highly likely that the other party will reject it because it would be at an 'information disadvantage' concerning the other party's law. This, in turn, might have a harmful effect on its legal position. The usual scenario is the clash of standard contract terms containing each party's choice of law clause, the so-called 'battle of forms'. The tricky question of whether the choice of law clause of one party prevails over that of the other party then arises.<sup>7</sup> If both parties have basically the same bargaining power,<sup>8</sup> neither will succeed in enforcing its own domestic law. For these situations, we must look for alternatives.

## C. The Choice of a Third Domestic Law

In order to avoid the situation where the other party has the benefit of having its own law applied to the contract, the parties might agree on the law of a third state, to which neither of them has a particular connection.<sup>9</sup> This begs the question as to which law could be suited to the case at hand. Which qualities must that third law bear?

<sup>7</sup> For the Members of the European Union, the question of whether a choice of law clause has been validly incorporated in a contract is governed by the law appointed in the respective choice of law clause (Art. 8(1) Rome Convention 1980). A comparative survey reveals that there are at least four different approaches as to how domestic law may answer the question of battle of forms: 1) the standard terms of the offeror prevail; 2) the standard terms of the offeree prevail; 3) conflicting terms cancel out each other, the contract is effective without standard terms (Art. 2:209 PECL; Art. 2.22 UNIDROIT Principles); or 4) there is no contract at all; see K. Neumayer, *Das Wiener Kaufrechtsübereinkommen und die sogenannte "battle of forms"*, in W. Habscheid et al. (Eds.), *Freiheit und Zwang: Festschrift zum 60. Geburtstag von Hans Giger*, 501 at 503 et seq. (1989); K. Neumayer, *International Encyclopedia of Comparative Law*, Chapter 12: Contracting Subject to Standard Terms and Conditions (1999). On the discussion of battle of forms in choice of law clauses see the annotations on Art. 2:209 PECL in C. von Bar & R. Zimmermann, *Grundregeln des Europäischen Vertragsrechts*, Teile I und II (2002); S. Tiedemann, *Kollidierende AGB-Rechtswahlklauseln im österreichischen und deutschen IPR*, 1991 Praxis des Internationalen Privat- und Verfahrensrechts 424 et seq.; W. Meyer-Spahrenberg, *Rechtsvereinbarungen in Allgemeinen Geschäftsbedingungen*, 1989 *Recht der Internationalen Wirtschaft* 347 et seq.; see also H. Heiss, *Inhaltskontrolle von Rechtswahlklauseln in AGB nach europäischem Internationalem Privatrecht?*, 65 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 634 et seq. (2001).

<sup>8</sup> This, of course, will not always be the case. Where one party is in a more dominant position than the other, it will simply impose its law on the other party, see Herbel, *supra* note 3, at 9.

<sup>9</sup> F. Vischer, *Die Kollisionsrechtliche Bedeutung der Wahl einer nichtstaatlichen Ordnung für den Staatlichen Richter am Beispiel der Unidroit Principles of International Commercial Contracts*, in I. Schwenzer & G. Hager (Eds.), *Festschrift für Peter Schlechtriem zum 70. Geburtstag* 445, at 449 (2003); J. Kropholler, *Internationales Privatrecht: einschliesslich der Grundbegriffe des internationalen Zivilverfahrensrechts* 296 (§ 40 IV 3.a) (2004); D. von Breitenstein, *Rechtsordnung und "Lex Mercatoria" – Zur vergeblichen Suche nach einem "anationalen" Recht*

## I. The Choice of an Allegedly Particularly ‘Good’ Law

There are some laws that are deemed particularly suitable for sales contracts because they are the law of a state that plays a dominant role in a certain trade area.<sup>10</sup> For example, the law of New York is frequently chosen for specific finance transactions,<sup>11</sup> and parties to ship charter agreements or raw material transactions often agree on English law because London is the leading market place for such contracts.<sup>12</sup> A further popular example is the choice of English law in international contracts for the supply of cereals owing to the leading role of the London Corn Trade Association.<sup>13</sup>

However, the law of a dominant market place is not *automatically* the best law.<sup>14</sup> From a civil law point of view, the problem is that the leading market places are mostly common law countries. This means that, unlike in civil law countries, the primary sources of law are not codes and legal statutes, but case law. Acts and other legislative works are only subsidiary legal sources. This often makes it difficult for lawyers from civil law countries to find the relevant information, i.e., the *status quo* of how a legal issue is currently approached. What may sound trivial is nonetheless often overlooked in day-to-day practice, namely that for a civil law foreigner, the common law is less predictable and, therefore, a dangerous playing field, especially where the other party has profound common law legal advice. In particular, where there is a difference in the legal backgrounds of the parties, and one party is more familiar with the English language and the intricacies of the common law, the other party should be cautious about blindly subjecting itself to the law of a common law country, although it may be the law of a market dominating state.<sup>15</sup>

## II. Confusion with Political Neutrality

### 1. The Facts

Parties often mix up two things: they confuse the need for a law that fairly represents both contractual positions with the political neutrality of the state whose law has been chosen to govern the contract.<sup>16</sup> It is a popular fallacy to designate the law of a politically neutral state to an international contract whose terms have

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für die internationale Arbitrage, in K. Berger *et al.* (Eds.), Festschrift für Otto Sandrock zum 70. Geburtstag 111, at 125 (2000); the thoughts expressed by F. Sandrock, Die Vereinbarung eines “neutralen” internationalen Gerichtsstandes: ausländische Parteien vor “neutralen” inländischen Gerichten 51 (1997), with regard to the choice of the forum are also applicable to the choice of law question.

<sup>10</sup> See Leible, *supra* note 1, at 289; Oschmann, *supra* note 6, at 27.

<sup>11</sup> W. Döser, Vertragsgestaltung im internationalen Wirtschaftsrecht, para. 240 (2001); Kieninger, *supra* note 6, at 306.

<sup>12</sup> See Kieninger, *supra* note 6, at 304.

<sup>13</sup> See Leible, *supra* note 1, at 289.

<sup>14</sup> See Mankowski, *supra* note 3, at 7.

<sup>15</sup> See Mankowski, *supra* note 3, at 6.

<sup>16</sup> E.-M. Kieninger, *Rechtsentwicklung im Wettbewerb der Rechtsordnungen*, in C. Ott & H.-B.

been carefully drafted and negotiated under another law, perhaps quite different from the law of that politically neutral state. States such as Switzerland have greatly benefited from this confusion.<sup>17</sup> However, political neutrality has little significance when choosing the law to govern an international sales contract.

## 2. Confusion Between Choice of Law and Efficient Jurisdiction

There is, of course, a correlation to the extent that an efficient (arbitral) jurisdiction safeguards the fair treatment of the parties. Defence of actions and recovery under judgments are certainly more problematic in politically instable states. Insofar, however, two things are being confused, choice of law and jurisdiction. For example, the reason why parties have faith in the Swiss legal system is due to the effectiveness of its legal protection. But the latter is also safeguarded if a law other than Swiss law applies. In this respect, the argument that a decision is not of the same high calibre if the court applies foreign law<sup>18</sup> must fail. Let us focus on Swiss arbitration, which enjoys an enviable reputation: a three arbitrators' panel, as it is quite common in international cases,<sup>19</sup> will – due to its variety in nationalities –<sup>20</sup> have to apply a law that is, at least to a part of the tribunal, 'foreign'.<sup>21</sup> So, even if Swiss law was applicable, it would not be the 'tribunal's own law'. Despite this, there is still confidence in Swiss (arbitral) judicature.<sup>22</sup>

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Schäfer (Eds.), *Vereinheitlichung und Diversität des Zivilrechts in transnationalen Wirtschaftsräumen* 72, at 93 (2003); see Sandrock, *supra* note 1, at 850.

<sup>17</sup> In ICC arbitration 2004, 79,1% of all contracts had chosen national laws, with the laws of England and Switzerland being the most frequent choices, see ICC Bulletin 16 (Spring 2005) 5, 11.

<sup>18</sup> K. Zweigert, *Some Reflections on the Sociological Dimensions of Private International Law or What Is Justice in the Conflict of Laws?*, 44 Colorado Law Review 283, at 293 (1973): "The judge who has to apply foreign law is always worse than the judge who is applying his own law."; A. Bell, *Forum Shopping and Venue in Transnational Litigation*, para. 2.46 (2003); G. Kegel & K. Schurig, *Internationales Privatrecht: Ein Studienbuch* 512 (§ 15 V 2) (2004); Kropholler, *supra* note 9, at 456 (§ 52 II 3.c)).

<sup>19</sup> See Swiss Chambers' Arbitration Newsletter 1/2006: 65% of all cases submitted to Swiss Chambers' Arbitration in 2005 provide for a panel of three arbitrators.

<sup>20</sup> This is based on the assumption that usually, only the chair arbitrator is Swiss, whereas the party-appointed arbitrators are of another nationality. Although the Swiss Rules do not provide for any restrictions concerning the composition of the tribunal with regard to the arbitrator's nationality, other International Arbitration Rules, e.g., Art. 9(5) ICC Rules of Arbitration or Art. 16 AAA International Rules, do. Since from the total of cases submitted to Swiss Chambers' Arbitration in 2005, only 16% of the parties were from Switzerland (see Swiss Chambers' Arbitration Newsletter 1/2006), it can be inferred that the vast majority of party appointed arbitrators are non-Swiss nationals.

<sup>21</sup> See also J. Lew, L. Mistelis & S. Kröll, *Comparative International Commercial Arbitration*, para. 18-2, 18-22 (2003).

<sup>22</sup> Switzerland was the second most chosen place of arbitration in ICC arbitration 2004 (total of 78 cases), outstripped only by France (total of 89 cases), see ICC Bulletin 16 (Spring 2005) 5, 10.

### 3. Confusion Between Politically Neutral Law and Contractually Well-Balanced Law: Illustrated by Swiss Sales Law

The choice of Swiss sales law is often recommended, not because of its suitability,<sup>23</sup> but because it constitutes a “reassuring impartiality in cases where none of the parties is Swiss”<sup>24</sup>. However, the following may illustrate that Swiss sales law is, at least currently, rather complicated and does not lend itself to recommendation for international commercial sales transactions as much as its frequent choice as applicable law could lead us to believe.

#### a) *Differentiation between ‘non-delivery’ and ‘defective delivery’*

Swiss sales law differentiates meticulously between ‘delivery’ and ‘non-delivery’ of the ordered goods. At first glance, this might seem to be a differentiation which is internationally accepted. The CISG, the PECL, and the UNIDROIT Principles<sup>25</sup> distinguish between cases where one party does not perform at all and cases where performance has been made, though not as set out in the contract.<sup>26</sup> However, Swiss sales law differs from that internationally established standard: ‘non-delivery’ under Swiss sales law does not mean complete physical absence of the goods at their intended destination at the time they should have been delivered. Instead, ‘non-delivery’ stands for every failure to deliver *exactly* those goods for which the contract provides.<sup>27</sup> If, for example, the seller delivers a ‘Jaguar Mk X, Model 1963’ instead of a Jaguar Model 1964, he has ‘not delivered’ within the meaning of Swiss sales law.<sup>28</sup>

It has been said that the distinction between ‘defective delivery’ and ‘non-delivery’ can be drawn relatively clearly when *identified* goods are at issue, since every delivery of goods other than the identified ones is a non-delivery.<sup>29</sup> However, the distinction dictated by Swiss sales law becomes tricky if the contract provides not for identified goods, but for *generic* goods, i.e., goods of a certain kind. Here, if the seller’s performance is not in accordance with the contract, it becomes extraordinarily difficult to assess whether there is a ‘defective delivery’ or a ‘non-delivery’ within the meaning of Swiss sales law. Does it, for example, constitute

<sup>23</sup> See, however, S. Brachert & A. Dietzel, *Deutsche AGB-Rechtsprechung und Flucht ins Schweizer Recht*, 2005 Zeitschrift für das gesamte Schuldrecht 441, who recommend Swiss law for distribution agreements on the basis of its substance.

<sup>24</sup> N. Magaud, *Die Vorteile der Anwendung schweizerischen Rechts bei verborgenen Mängeln im Recht der internationalen Warenkaufverträge*, 1996 Recht der Internationalen Wirtschaft 387, at 389.

<sup>25</sup> On these rules of law see *infra* sub E.

<sup>26</sup> Cf. Art. 49(1)(a), (b) CISG; Arts. 8 :106(3), 9 :301 PECL; Arts. 7.1.5(3), 7.3.1(1) UNIDROIT Principles.

<sup>27</sup> The fact that Art. 190(1) Swiss Code of Obligations refers to late delivery in commercial sales transactions does not change the aforesaid; it simply establishes the presumption that in commercial sales transactions, where the buyer has fixed a specific date for performance, he will prefer the rescission of the contract rather than specific performance. Late delivery is just one form of ‘non-delivery’ within the meaning of the Swiss Code of Obligations.

<sup>28</sup> Decision of the Swiss Federal Court, 30 January 1968 (BGE 94 II 26).

<sup>29</sup> H. Giger, in *Berner Kommentar* (1979), Vorbemerkungen zu Art. 197-210 para. 46.

a 'defective delivery' or a 'non-delivery' if the delivered wine originates from Montblanch, although the buyer had ordered wine from the district of Panadès?<sup>30</sup> Is the delivery of empty oil barrels instead of empty petroleum barrels defective delivery or non-delivery?<sup>31</sup> How can it be conclusively explained that the delivery of insulation tubes in a zinc jacket instead of insulation tubes in a leaded jacket constitutes a 'non-delivery',<sup>32</sup> whereas the delivery of soap with less fat content than agreed is merely a 'defective delivery'?<sup>33</sup> One might have hoped<sup>34</sup> that Swiss sales law would have done away with this unhappy distinction in view of the CISG and the development<sup>35</sup> in other legal systems. Instead, the Swiss Federal court recently confirmed the distinction, finding that the delivery of a fork lift truck with a manual transmission instead of the ordered fork lift truck with an automatic transmission constituted a 'non-delivery' because the seller had failed to deliver exactly the product ordered by the buyer.<sup>36</sup>

b) *Different remedies depending on how the seller's failure to perform is qualified*

i) *In general*

The distinction between 'non-delivery' and 'defective delivery' is important because of the remedies available to the buyer: in cases of non-delivery, the buyer's remedies are those available under general contract law. He is not restricted to the remedies available under sales law (Arts. 197 et seq. Code of Obligations). Instead, he may grant the seller an additional period of time for performance, and after expiration of that period, he may choose whether to rescind the contract or

<sup>30</sup> Decision of the Swiss Federal Court, 20 June 1914 (BGE 40 II 480, 488): "non-delivery".

<sup>31</sup> Decision of the Obergericht Luzern, 28 February 1908, 5 Schweizerische Juristen-Zeitung 30, No. 52 (1908/09): "defective delivery".

<sup>32</sup> Decision of the Handelsgericht Zurich, 18 November 1920, 20 Zürcherische Rechtsprechung 309, No. 158 (1921).

<sup>33</sup> Decision of the Kantonsgericht St. Gallen, 6 December 1919, 17 Schweizerische Juristen-Zeitung 270, No. 52 (1920/21).

<sup>34</sup> See E. Kramer, *Noch einmal: Zur aliud-Lieferung beim Gattungskauf*, 1997 recht 78, at 83:

The introduction of modern uniform private law should provide a timely opportunity to critically re-evaluate traditional dogmatic incrustation and nitpickiness of domestic legal systems and to abandon these, to the extent that this can be done for good reason, in favour of a harmonisation of uniform private law and domestic private law.

(Translation by the author.)

<sup>35</sup> See *infra*, sub E.V.5.a.

<sup>36</sup> Decision of the Swiss Federal Court, 5 December 1995 (BGE 121 III 453); the decision has been reviewed on various occasions, see, e.g., E. Kramer, *Abschied von der aliud-Lieferung?*, in F. Harrer *et al.* (Eds.), *Besonderes Vertragsrecht - aktuelle Probleme* (Festschrift für Heinrich Honsell zum 60. Geburtstag) 247 *et seq.* (2002); see Kramer, *supra* note 34, at 78 *et seq.*; R. Lanz, *Die Abgrenzung zwischen Falschlieferung (aliud) und Schlechtlieferung (peius) und ihre Relevanz*, 1996 recht 248 *et seq.*; P. Gelzer, *Bemerkungen zur Unterscheidung zwischen aliud und peius beim Gattungskauf*, 1997 Aktuelle Juristische Praxis 703 *et seq.*

insist on specific performance,<sup>37</sup> and he may raise his claim within a comfortable period of, in principle, ten years.<sup>38</sup> If, however, the seller's failure to deliver conforming goods is defined as 'defective delivery', the buyer can, in principle, only rescind the contract or claim a reduction of the price, and he can do so only within strict time limits.<sup>39</sup>

However, to add to the complexity in these cases, attempts have been made by the courts to overcome the difficulties resulting from the said differentiation. The Swiss Federal Court allows for a choice between sales-specific remedies (rescission of the contract, reduction of price) and remedies for vitiated consent.<sup>40</sup> This again leads to a confusing overlap between sales law and laws concerning vitiated consent.<sup>41</sup>

ii) *In particular: the tricky damages concept of swiss sales law provisions*

Where the buyer has received a 'defective delivery', he can also claim damages. This similarly raises difficult questions. Art. 208(2), (3) of the Swiss Code of Obligations requires an assessment of how 'direct' the incurred loss is. If there is a 'direct causal connection' between the seller's delivery of defective goods and the incurred loss, the seller will be held liable for that loss regardless of the existence of fault on his part. If, however, the loss does not directly result from the seller's delivery of non-conforming goods, the buyer will only be compensated for that 'indirect' loss if it is established that the seller was at fault. Therefore, whether the buyer has to prove the seller's fault will depend on the immediacy of causation.<sup>42</sup>

The criterion of 'immediacy of causation' is very vague. We learn, at least, from a decision of the Swiss Federal Court from 1953 that loss of profit falls under Art. 208(3) Swiss Code of Obligations, i.e., the seller is only liable if he fails to prove his absence of fault,<sup>43</sup> but recent case law to illuminate the legal situation is sparse. The situation is, altogether, more than unclear, which is reflected by the great disaccord among legal authors.<sup>44</sup>

<sup>37</sup> Art. 107 *et seq.* Swiss Code of Obligations.

<sup>38</sup> Art. 127 Swiss Code of Obligations.

<sup>39</sup> Art. 201 Swiss Code of Obligations, *see* Th. Koller, *Aliud und peius: wirklich überholt?, oder, Was das CISG und das revidierte deutsche Recht dem OR (noch) voraus haben*, in H. Honsell *et al.* (Eds.), *Privatrecht und Methode: Festschrift für Ernst A. Kramer* 531, at 536 *et seq.* (2004).

<sup>40</sup> Decision of the Swiss Federal Court, 7 June 1988 (BGE 114 II 31, 34).

<sup>41</sup> *See also* I. Schwenzer, *Schweizerisches Obligationenrecht Allgemeiner Teil*, para. 39.40 *et seq.* (2003).

<sup>42</sup> *See* H. Honsell, *Schweizerisches Obligationenrecht Besonderer Teil 105 et seq.* (2003).

<sup>43</sup> Decision of the Swiss Federal Court, 17 November 1953 (BGE 79 II 376, 380 *et seq.*). It is unanimously held that under Art. 208(3), the burden of proof with regard to the seller's fault is upon the seller. This fact simplifies the situation for the buyer, but the basic problem that his compensation depends on the seller's fault remains.

<sup>44</sup> *See* in this regard C. Huguenin, *Obligationenrecht Besonderer Teil*, para. 335 *et seq.* (2004); following the Federal Court M. Keller & K. Siehr, *Kaufrecht* 90 (1995); W. Fischer, *Der unmittelbare und der mittelbare Schaden im Kaufrecht* 287 (1985); another question is whether Art. 208 applies in cases where the buyer claims a reduction of the price, or whether it only applies to cases in which he rescinds the contract; according to the Swiss Federal Court, Art. 208(2), which provides for damages regardless of any fault on the seller's behalf, does not apply to the situation where

c) *Summary*

The overview has shown that the current Swiss sales law is rather intricate. It steadfastly maintains a differentiation inherited from Roman sales law,<sup>45</sup> namely the distinction between the sale of specified goods and the sale of generic goods – a distinction no longer suited to the needs of modern trade. Whereas Germany, for example, which once had a sales law concept comparable to the Swiss, has now adapted its sales law to the international standard,<sup>46</sup> Swiss sales law has not.

3. Conclusion

The analysis above demonstrates that political neutrality of a legal system alone is no helpful criterion in deciding on the 'right' choice of law. The factors that should play a role are different ones. Parties have to look for 'neutrality of the law in relation to themselves', rather than for a politically neutral law.<sup>47</sup>

#### IV. Parameters: Quality, Flexibility, and Stability

By which considerations should the parties be guided in their search for a law suitable to their cause? Above all, the quality of a legal system is decisive.<sup>48</sup> We must ask, is that legal system open to new developments in international trade? Is it able to answer the needs and protect the interests of international economic relationships? The law in question should be modern, flexible, and stable.<sup>49</sup> Another, practical criterion is its availability in a commonly used language.<sup>50</sup> A law drafted in a rare language, where one will need to rely on a private, perhaps not error-free translation, is not a reliable source, and the parties will not give their contract a firm basis by choosing such a law.

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the buyer claims a reduction of the price; this question is disputed in academic circles, see the quotations in BernerKommentar/Giger, *supra* note 31, Art. 208 para. 56.

<sup>45</sup> On the Roman roots of Swiss sales law see W. Ernst, *Die kaufrechtliche Gewährleistung nach der Teilrevision des Obligationenrechts*, in E. Bucher *et al.* (Eds.), Norm und Wirkung : Beiträge zum Privat- und Wirtschaftsrecht aus heutiger und historischer Perspektive : Festschrift für Wolfgang Wiegand zum 65. Geburtstag 255, at 295 *et seq.* (2005); S. Keller, *Die Gefahrtragsregeln im Obligationenrecht*, 2003 Aktuelle Juristische Praxis 1152, at 1154 *et seq.*

<sup>46</sup> See thereto *infra* sub E.V.5.a.

<sup>47</sup> See Harries, *supra* note 1, at 208; Kieninger, *supra* note 6, at 310 *et seq.*

<sup>48</sup> See Harries, *supra* note 1, at 207 *et seq.*; Oschmann, *supra* note 6, at 28 *et seq.*

<sup>49</sup> See C. von Bar, *Internationales Privatrecht*, Vol. II, para. 414 (1991).

<sup>50</sup> U. Magnus, *Einleitung para. 6*, in J. von Staudinger (Ed.), *Kommentar zum Bürgerlichen Gesetzbuch mit Einführungsgesetz und Nebengesetzen*, Wiener Kaufrecht (CISG) (2005); Berger *et al.*, *Anwendung Transnationalen Rechts in der internationalen Vertrags- und Schiedspraxis*, 101 *Zeitschrift für vergleichende Zivilrechtswissenschaft* 12, at 31 *et seq.* (2002).

## V. Disadvantages When Choosing the Law of a Third State

### 1. Exorbitant Investigation Costs

Assuming that the parties to an international commercial transaction have been guided by the parameters discussed above, the choice of the ‘best law’ might still be a myth for practical reasons. The parties may lack the information and capacity to judge whether a certain law is the ‘best’ for their contract. Information is pricey, and the parties will often not deem the expenditure of high sums of money in order to find out the ‘best law’ a worthwhile investment. Rather, they will rely on other people’s experience and ‘post-humous reports’.<sup>51</sup> A comparison of competing legal systems at the stage of contract formation in order to find the law which best suits the contract at issue will only be rewarding for transactions in which huge amounts of money are at stake.<sup>52</sup>

For parties who cannot afford the luxury of expensive scrutiny of the various available legal systems and who consequently agree on a third law at the time of contract formation quite quickly, the expense of investigating the third law inevitably crops up at a later stage. In case of a dispute, each party will need to consult external experts. This, in turn, increases the total transaction costs.<sup>53</sup> Resorting to sophisticated lawyers with local expertise who will generate reliable information about the outcomes obtainable under a certain foreign law is worthwhile only for exceptional transactions of very high importance. For the run-of-the-mill contract, the costs linked to deliberate choice of law procedures are prohibitive.<sup>54</sup>

### 2. The Risk of a Disagreeable Surprise

The choice of a third law might lead to a disagreeable surprise, in particular where one party has invested more time and money in scrutinising the possibly suitable law than the other.<sup>55</sup> Choosing a third law has been characterised as a “jump into the dark”<sup>56</sup>, the dark referring to the depths of the unknown in the foreign law. Indeed, such a choice of law clause may turn out to be a Trojan horse, in that one party, who is aware that the provisions of a particular third law are disadvantageous to the other party, may suggest that law as a good, neutral compromise.<sup>57</sup>

<sup>51</sup> See Wagner, *supra* note 1, at 1010 *et seq.*; see also F. De Ly, *Opting out: some observations on the occasion of the CISG’s 25th anniversary*, in F. Ferrari (Ed.), *Quo vadis CISG?* 25, at 34 (2005).

<sup>52</sup> See Wagner, *supra* note 1, at 1010.

<sup>53</sup> See Kieninger, *supra* note 16, at 83 *et seq.*; C. von Bar & O. Lando, *Communication on European Contract law: Joint response of the Commission on European Contract Law and the Study Group on a European Civil Code*, 2002 *European Review of Public Law* 183, at 217 n. 53.

<sup>54</sup> See Wagner, *supra* note 1, at 1011.

<sup>55</sup> See Kadner Graziano, *supra* note 6, at 529.

<sup>56</sup> L. Raape & F. Sturm, *Internationales Privatrecht*, Vol. I, at 199 (1977).

<sup>57</sup> See Mankowski, *supra* note 3, at 6.

### 3. 'Neutral' Law Arguably More Related to one Party's Legal System Than to the Other

One should not forget that even when choosing a third law allegedly equally unfamiliar to both parties, that law might have a closer connection to the law of one of the parties than to the law of the other party. This could have the consequence that, yet again, one party will take advantage of being more akin to the applicable law than the other.<sup>58</sup>

## D. A Progressive Summary

As an intermediate result, first and foremost, both parties will try for the application of their own domestic law. The benefit of knowing the legal situation and being aware of the intricacies of one's own legal system will usually prevail over considerations as to whether that law *is* indeed good law for one's own position. Alternatively, the parties will be guided by considerations such as choosing a law that is equally neutral for both parties or one that is especially suited to that kind of transaction. Nonetheless, the risks are that a neutral law might be more related to the legal system of one of the parties, with the consequence that it is not 'equally' neutral. In addition, when looking for the 'best law in this trade branch', one might be misguided by the sheer number of contracts applying a particular law and deem that law the 'best' for the contract at hand, whereas in reality, other, less known laws would be more appropriate. However, the search for the 'best law' will often be so expensive that it is not worth the effort.

## E. The Choice of Unified Sales Law: CISG

### I. 'Hard Law' for International Sales Contracts

What has not yet been discussed is the possibility of choosing genuine international law, that is to say, sets of rules that exist on a supranational level and are detached from a national context. Examples of such unified laws are the CISG, the UNIDROIT Principles, the Principles of European Contract Law, or the *lex mercatoria*.<sup>59</sup> Whether those set of rules might constitute instruments to solve some of the difficulties encountered when trying to agree on a choice of law clause will be discussed in the following.

<sup>58</sup> See von Bar & Lando, *supra* note 53, at 217 n. 53.

<sup>59</sup> See on the various sources of international trade law L. Mistelis, *Is Harmonisation a Necessary Evil? The Future of Harmonisation and New Sources of International Trade Law*, in I. Flechtner, L. Mistelis & M. Cremona (Eds.), *Foundations and Perspectives of International Trade Law* 3, at 12 *et seq.* (2001).

To start with, the CISG<sup>60</sup> has been described as one of the most successful unification of law projects.<sup>61</sup> It is a Convention applying automatically if both parties have their place of business in a contracting state.<sup>62</sup> At present, there are sixty-seven contracting states to the Convention, among them the USA, China, and most European countries.<sup>63</sup> The CISG also applies where the rules of private international law lead to the sales law of a contracting state.<sup>64</sup> Moreover, even where the CISG does not apply by way of law, it is worth choosing it as the law governing an international sales contract. From a conflict of law rules perspective, the choice of the CISG does not raise any difficulties. We will see that for the other international rules of law to be discussed (UNIDROIT Principles, PECL, *lex mercatoria*), it is partially doubted whether they qualify as a valid choice of law in state courts, arbitration proceedings, respectively.<sup>65</sup> This question does not arise with regard to the CISG. It is a Convention and, as such, ‘hard law’ of the same authoritative quality as any chosen domestic sales law.

## II. Neutrality

The CISG is neutral law by nature. Neither party has a particular advantage when applying it; the parties are quasi on the same ‘level playing field’. Additionally, and closely linked to this, the application of the CISG eliminates the question of prestige, since neither party risks ‘losing face’.<sup>66</sup>

## III. Cost-Effective Examination Possibilities

The costs for examining the content of the CISG are low because it is outstandingly well-documented. There are six equally authentic language versions of the CISG, namely in Russian, Arabic, Chinese, English, French, and Spanish,<sup>67</sup> and the CISG has been translated into innumerable other languages. Though these last-mentioned translations are not official, they are mostly of excellent quality.<sup>68</sup> In addition, case law referring to the Convention is very easily accessed. There are at least four pre-eminent online databases<sup>69</sup> with user-friendly search screens allowing for a search as to case law and literature on a specific provision or on

<sup>60</sup> United Nations Convention on the International Sale of Goods (1980).

<sup>61</sup> P. Schlechtriem, *Einleitung*, in P. Schlechtriem & I. Schwenzer (Eds.), *Kommentar zum Einheitlichen UN-Kaufrecht: das Übereinkommen der Vereinten Nationen über Verträge über den internationalen Warenkauf – CISG –*, at 27 (2004); W. Witz, H.-C. Salger & M. Lorenz, *International einheitliches Kaufrecht: Praktiker-Kommentar und Vertragsgestaltung zum CISG*, *Einleitung*, para. 5 (2000).

<sup>62</sup> Art. 1(1)(a) CISG.

<sup>63</sup> See [http://www.uncitral.org/uncitral/en/uncitral\\_texts/sale\\_goods/1980CISG\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG_status.html) (last accessed on 1 August 2006).

<sup>64</sup> Art. 1(1)(b) CISG.

<sup>65</sup> See *infra* sub F.III, G.II.

<sup>66</sup> See De Ly, *supra* note 51, at 36 *et seq.*; Herbel, *supra* note 3, at 11.

<sup>67</sup> See <http://www.uncitral.org/index.html>.

<sup>68</sup> On the formulation of the German text of the CISG see Schlechtriem, *supra* note 61, at 29.

<sup>69</sup> CISG-online (<http://www.cisg-online.ch>); CISG Pace Database (<http://www.cisg.law.pace>).

indicated key words. There is virtually no other legal instrument that can lay claim to such a comprehensive collection of case law. Similarly unique is the willingness of various CISG databases to collaborate.<sup>70</sup> UNCITRAL<sup>71</sup> has edited an official commentary to the CISG in which case law from all over the world has been addressed. An Advisory Council<sup>72</sup> on the CISG providing interpretative guidance has been formed,<sup>73</sup> and there are a great number of commentaries and handbooks<sup>74</sup> that are published or have been translated into English and several other languages. All those factors minimise transaction costs, and it has been demonstrated that a law that is easy to examine and accessible reduces uncertainty and keeps examination costs at a low level. This, in turn, leads to a reduction in the transaction costs, which renders the contract altogether more efficient.

#### **IV. Rationalisation Potential**

In addition, if a party becomes accustomed to generally conducting its sales transactions under the CISG, it will quickly come to have a large stock of various CISG contracts at hand and will, therefore, experience a rationalisation effect similar to the situation that develops when always applying one's own law or the law of a market-dominating state.<sup>75</sup>

#### **V. Legal Qualities**

##### **1. Practicability by 'Open Terms'**

The foregoing reasons are rather practical. Focusing on the *legal quality* of the CISG, it is accepted that the CISG consists of flexible and functional provisions. It has often been complimented on its core element, the term 'fundamental breach of contract' (Art. 25 CISG). Indeed, this is a highly successful tool for assessing whether a party should be entitled to resort to the ultimate remedy, the termination

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edu); UNILEX (<http://www.unilex.info>); CLOUT ([http://www.uncitral.org/uncitral/en/case\\_law.html](http://www.uncitral.org/uncitral/en/case_law.html)).

<sup>70</sup> See, e.g., the links to other databases at CISG-online. Additionally, for non-English cases, CISG-online provides for direct links to CISG Pace Database and UNILEX for an English abstract or full translation.

<sup>71</sup> United Nations Commission on International Trade Law, the subcommission of the UNO which drafted the CISG, <http://www.uncitral.org/index.html>.

<sup>72</sup> See L. Mistelis, *CISG-AC Publishes First Opinion*, at [http://www.cisg-online.ch/cisg/docs/CISG-%20AC\\_Mistelis\\_intro.pdf](http://www.cisg-online.ch/cisg/docs/CISG-%20AC_Mistelis_intro.pdf); R. Herber, *Eine neue Institution: Der CISG Advisory Council*, 2003 Internationales Handelsrecht 201 *et seq.* The Opinions of the CISG-AC are published at <http://www.cisg-online.ch/cisg/cisgacopinions.html> and <http://www.cisg.law.pace.edu/cisg/CISG-AC.html>.

<sup>73</sup> These developments satisfy the request for support and guidance in the uniform interpretation and application of the CISG as expressed by J. Murray, *The Neglect of CISG: A Workable Solution*, 17 *Journal of Law and Commerce* 365, text at n. 46 *et seq.* (1998), <http://www.cisg.law.pace.edu/cisg/biblio/murray1.html>.

<sup>74</sup> See the bibliography in Schlechtriem & Schwenzer (Eds.), *supra* note 61.

<sup>75</sup> See Mankowski, *supra* note 5, at 9.

of the contract. At the time the CISG was passed, most civil law sales laws did not provide for such a broad term to circumscribe one party's failure to fulfill a contractual obligation. Instead, many of them showed – and most of them still do – a differentiation comparable to the system of Swiss sales law.<sup>76</sup>

The CISG abandoned that concept and opted for one single technical term to cover all breaches of contract. 'Breach of contract' is the key to the variety of remedies available under the CISG. Whether a particular remedy is open to the aggrieved party will depend not on whether the buyer received defective goods of the kind agreed upon in the contract (in Swiss terminology: 'defective delivery') or whether he received goods of another kind ('non-delivery'), but rather on the severity of the breach. In other words, the decisive factor is whether the breach was 'fundamental'. The term 'non-delivery' is not unknown to the CISG. However, it is restricted to a complete physical absence of any goods at the time delivery is due.<sup>77</sup> It constitutes merely one out of several forms of 'failure to perform properly', and its consequences fit in the ordinary remedies regime provided by the CISG. With this integrative approach (i.e., every failure to perform is a – not further specified - breach of contract), the CISG provides for a simply manageable system that is suitable for international commercial transactions. The specific dogmatic peculiarities of the particular domestic laws become irrelevant, a fact which has a positive impact on transaction costs and promotes contractual neutrality.<sup>78</sup> The concept of 'fundamental breach' and the remedies system of the CISG have influenced many other sets of rules world-wide.<sup>79</sup>

## 2. Flexibility

Another feature of the CISG worth mentioning is Art. 6, which gives it the utmost flexibility.<sup>80</sup> It allows the parties to modify or opt out of particular CISG provisions or to even opt out of whole chapters of the CISG. For example, Art. 39 of the CISG requires the buyer to notify the seller of any non-conformity of the goods 'within a reasonable time', but the parties may derogate from this and agree

<sup>76</sup> For an overview of the various European sales laws see A. Schwartze, *Europäische Sachmängelgewährleistung beim Warenkauf: optionale Rechtsangleichung auf der Grundlage eines funktionalen Rechtsvergleichs* 42 *et seq.* (2000).

<sup>77</sup> Art. 49(1)(b) CISG.

<sup>78</sup> The advantages of the CISG over, e.g., the Swiss sales law have already been pointed out by I. Schwenzer, *Das UN-Abkommen zum internationalen Warenkauf (CISG)*, 1991 *recht* 113, at 121; see also Kramer, *supra* note 34, at 83; W. Stoffel, *Ein neues Recht des internationalen Warenkaufs in der Schweiz*, 1990 *Schweizerische Juristen-Zeitung* 169, at 177; J. Schmid, *Die positive Vertragsverletzung im System des schweizerischen und des europäischen Privatrechts*, in J. Basedow *et al.* (Eds.), *Aufbruch nach Europa: Festschrift 75 Jahre Max-Planck-Institut für Privatrecht* 1021, at 1023, 1033 *et seq.* (2001).

<sup>79</sup> See *infra* sub E.IV.5.a.

<sup>80</sup> See J. Meyer, *UN-Kaufrecht in der deutschen Anwaltspraxis*, 69 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 457, at 481 *et seq.* (2005); Mankowski, *supra* note 3, at 10; Witz, Salger & Lorenz, *supra* note 61, *Einleitung*, para. 6; S. Zwart, *The New International Law of Sales: A Marriage Between Socialist, Third World, Common, and Civil Law Principles*, 13 *North Carolina Journal of International and Commercial Regulation* 109, 112, 127 (1988); this fact has been overlooked by Leible, *supra* note 1, at 309.

on another period for notification.<sup>81</sup> Accordingly, the parties have the power to deviate from the principle of freedom from form requirements<sup>82</sup> and provide that the contract, or any other statements such as the notice of non-conformity of the goods,<sup>83</sup> must be in a particular form. The parties can also agree – in derogation from Art. 38 CISG, according to which the buyer has to inspect the goods – that the conformity of the goods, namely their quantity and quality, must be assessed by a neutral third party inspection body.<sup>84</sup> Finally, Art. 6 paves the way for a 'trade-specific' drafting of a contract, since it enables the various trade branches to exclude particular CISG provisions and replace them with their own branch-specific rules.

### 3. Impartiality

That the CISG has not been influenced by any association of professions or trade branches supports the well-balanced nature of this instrument. Rather, it comprises the work of academics, predominantly university professors and representatives of the ministries of justice, who were not representing the interests of either buyer- or seller-oriented branches, but were, in a positive way, uncommitted and impartial.<sup>85</sup>

### 4. Doubts Raised by the Opponents: Uncertainty and Buyer-Friendliness

Despite all those factors, it is reported in literature that the CISG is often excluded by the parties in day-to-day-practice.<sup>86</sup> The opponents of the CISG consider the concept of operating with open terms such as 'fundamental breach' too uncertain.<sup>87</sup>

A second objection to the CISG is that it is allegedly too buyer-friendly.<sup>88</sup> The opponents base this objection on the argument that less-developed countries

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<sup>81</sup> Practical proposals are made by R. Koch, *Wider den formularmässigen Ausschluss des UN-Kaufrechts*, 2000 Neue Juristische Wochenschrift 910 *et seq.*; De Ly, *supra* note 51, at 41 *et seq.*

<sup>82</sup> Art. 11 CISG; although Art. 11 CISG speaks only of the conclusion of the contract, its systematics makes it clear that the principle of freedom from form requirements applies to all statements made under the contract, *cf.* Schlechtriem/Schwenzer/Slechtriem, *supra* note 61, Art. 11 para. 9, with further references.

<sup>83</sup> *See, e.g.*, Oberster Gerichtshof (Austria), 15 October 1998, CISG-online 380.

<sup>84</sup> Arbitration (ICC), June 1999, Case 9187, CISG-online 705.

<sup>85</sup> R. Herber, *Das UN-Übereinkommen über internationale Kaufverträge*, 1980 *Recht der Internationalen Wirtschaft* 601 *et seq.*

<sup>86</sup> V. Stadie & W. Nietzer, *CISG – Das UN-Kaufrecht in der Anwaltspraxis*, 2002 *Monatsschrift für Deutsches Recht* 428, at 431; F. Ferrari, *Zum vertraglichen Ausschluss des UN-Kaufrechts*, 2002 *Zeitschrift für Europäisches Privatrecht* 737; F. Ferrari, *Exclusion et inclusion de la CVIM*, 2001 *Revue de droit des affaires internationales* 401; Herbel, *supra* note 3, at 6, 12; *but see also* Meyer, *supra* note 82, at 483 *et seq.*: his survey among German lawyers who are often involved in the drafting of international sales contracts reveals a tendency to agree on the CISG more frequently; Magaud, *supra* note 26, at 389, also observes a creeping tendency to opt in to the CISG.

<sup>87</sup> Meyer, *supra* note 80, at 474; *see also* the quotations in B. Piltz, *UN-Kaufrecht* 76 (2001).

<sup>88</sup> *See, e.g.*, G. Manz & S. Padmann-Reich, *Introduction to the UN Convention of International*

participated in the drafting of the CISG.<sup>89</sup> As such countries are mainly import-oriented, they allegedly provided the impetus for a great deal of buyer-friendly rules.

## 5. Appreciation of Those Objections

### a) *The concept of 'open terms' has been a success*

As to the first argument, the term 'fundamental breach of contract' has stood the test of time.<sup>90</sup> Notwithstanding, or even *because* of its 'openness', it is perfectly possible to apply the concept in practice. Case law and literature have developed quite clear rules as to when the breach of a contract becomes fundamental.<sup>91</sup> Considerable other sets of *unified* law, such as the UNIDROIT Principles<sup>92</sup> or the Principles of European Contract Law<sup>93</sup>, have adopted a very similar solution.<sup>94</sup> The same is true for the European Directive on certain aspects of the sale of consumer goods of 1999.<sup>95</sup> Furthermore, the OHADA, a union of sixteen African states, has adopted a common sales law that follows the CISG almost to the letter.<sup>96</sup> Finally, the German Civil Code (*Bürgerliches Gesetzbuch*) may serve as a recent example of a *domestic* sales law that has adopted this concept.<sup>97</sup>

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*Sale of Goods in Germany*, 1991 International Business Lawyer 300; Magaud, *supra* note 24, at 389.

<sup>89</sup> See Zwart, *supra* note 80, at 118 *et seq.*

<sup>90</sup> See also B. Zeller, *The CISG in Australasia: an overview*, in F. Ferrari (Ed.), *Quo vadis CISG?* 293, at 322 (2005); Kropholler, *supra* note 9, at 470 *et seq.* (§ 52 IV 2. b)); Mankowski, *supra* note 3, at 9; H. Westermann, *Das UN-Kaufrecht im Aufschwung? Anwendungsbereich und Anwendungsvoraussetzungen*, in H. Honsell *et al.* (Eds.), *Privatrecht und Methode: Festschrift Ernst A. Kramer* 717, at 732 (2004).

<sup>91</sup> See the classification of cases in Schlechtriem/Schwenzer/Slechtriem, *supra* note 61, Art. 25 para. 17 *et seq.*

<sup>92</sup> Art. 7.3.1 UP.

<sup>93</sup> Art. 9:301 PECL.

<sup>94</sup> On the influence of the CISG on UNIDROIT and PECL *see, e.g.*, P. Schlechtriem, *Internationales UN-Kaufrecht* para. 3 *et seq.* (2005).

<sup>95</sup> Directive 1999/44/EC of the European Parliament and of the Council of 25 May 1999 on certain aspects of the sale of consumer goods and associated guarantees, Official Journal L 171, 07/07/1999 P. 0012 – 0016. On the influence of the CISG on the EU-Directive *see, e.g.*, T. Pfeiffer, *Systemdenken im neuen Leistungsstörungs- und Gewährleistungsrecht*, 2002 *Zeitschrift für das gesamte Schuldrecht* 23, at 24; W. Faber, *Zur Richtlinie bezüglich Verbrauchsgüterkauf und Garantien für Verbrauchsgüter*, 1999 *Juristische Blätter* 413, at 418; D. Staudenmayer, *Die EG-Richtlinie über den Verbrauchsgüterkauf*, 1999 *Neue Juristische Wochenschrift* 2393, at 2394 *et seq.*

<sup>96</sup> See the references in Staudinger/Magnus, *supra* note 50, Einleitung para. 2.

<sup>97</sup> §§ 280, 281, and 323 BGB, which are the core provisions of the German default law (Leistungsstörungsrecht), have adopted the term 'breach of obligation' (Pflichtverletzung) as the general concept for all kinds of contractual breach. Like the CISG, the BGB has not completely abandoned the differentiation between various categories of breach of contract (this is particularly emphasised by J. Wilhelm, *Die Pflichtverletzung nach dem neuen Schuldrecht*, 2004 *Juristenzeitung* 1055 *et seq.*). For example, where performance has been made, though not properly, the remedies available to the aggrieved party are more restricted than where there has been no performance at all, § 281(1) BGB; Arts. 49, 64 CISG. On the similarity between the CISG and the new BGB *see*,

b) CISG is neither too buyer-friendly nor too seller-friendly

The second reproach, that the CISG is too buyer-friendly, must likewise be rejected. On the contrary, the CISG is considered to be a very well-balanced law.<sup>98</sup> Art. 48 CISG serves to portray it as an outspokenly modern and efficient system. Art. 48(1) CISG provides that the seller's right to cure a defect in its performance takes precedence over the buyer's right to avoid the contract; in other words, the buyer must allow, if it does not cause him unreasonable inconvenience and if he is compensated, for the seller to rectify any defects.<sup>99</sup> That concept reflects the approach of the CISG that international contracts should be upheld as much as possible in order to keep the considerable costs of winding-up the contract at a minimum.

Arts. 38, 39 CISG may serve as a second example. According to those provisions, the buyer is required to examine the goods within "as short a period as is practicable in the circumstances", and give notice of any non-conformities "within a reasonable time" after he (ought to have) discovered them. The CISG's approach of not stating an *exact* period of time within which examination and notification are to take place corresponds to most (domestic and international) sales laws and allows for reasonable scope of interpretation based on the goods involved. Where complicated technical facilities are sold, the complexity of which renders it difficult for the buyer to assess whether defects in the system result from the facility itself or from an incorrect operation, the examination and notification might take even weeks.<sup>100</sup> However, this is nothing unusual. It is only in Germanic legal systems that periods for examination and notification are alarmingly short.<sup>101</sup> The international standard is more buyer-friendly; significant domestic sales laws clearly grant more generous examination and notification periods which, for example in French cases, might be up to two years.<sup>102</sup> In light of this overview, the CISG can be regarded neither as too seller-friendly nor as too buyer-friendly. It is, in fact, a well-balanced law.

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*e.g.*, Stadie & Nietzer, *supra* note 86, at 432 *et seq.* For further domestic laws applying the notion of fundamental breach or similar key concepts within the framework for avoidance or cancellation of the contract *see* the Scandinavian sales laws (§ 39 Norwegian Sale of Goods Act 1988; Sec. 39 Finnish Sale of Goods Act 1987) and Art. 6:265 of the Netherlands Wetboek.

<sup>98</sup> *See* Staudinger/Magnus, *supra* note 50, Einleitung para. 8; Koch, *supra* note 81, at 915; J. Lookofsky, *In dubio pro conventione? Some thoughts about opt-outs, computer programs and preemption under the 1980 Vienna Sales Convention (CISG)*, 13 Duke J. of Comp. & Int'l L. 263, at 273, 289 (2003); De Ly, *supra* note 51, at 37 *et seq.*; Meyer, *supra* note 80, at 484.

<sup>99</sup> For details *see* C. Fountoulakis, *Das Verhältnis von Nacherfüllungsrecht des Verkäufers und Vertragsaufhebungsrecht des Käufers im UN-Kaufrecht*, 2003 Internationales Handelsrecht 160 *et seq.*

<sup>100</sup> It seems now to have become a standard that with durable goods, the notification period in Art. 39(1) CISG should be one month, Schlechtriem/Schwenzer/Schwenzer, *supra* note 61, Art. 39 para. 17, with further references.

<sup>101</sup> Art. 201 Swiss Code of Obligations; § 377 German and Austrian Commercial Code.

<sup>102</sup> Art. 1648(1) French Civil Code originally spoke of a "short period" ("bref délai"), within which the buyer had to raise his claim for non-conformity of the goods. The provision was changed in the course of implementing the Directive 1999/44/EC and now expressly provides for a period of two years: "L'action résultant des vices rédhibitoires doit être intentée par l'acquéreur dans un délai de

## 6. Real Motives for Not Choosing or Excluding the CISG

The real motives for opting out of the CISG are probably quite simple. As a lawyer of a national law society, one hesitates to open up for something new and instead, tries to promote one's own law according to the saying "better the devil you know than the devil you don't"<sup>103</sup>. The lawyers are unfamiliar and unready to deal with unknown provisions, and this is the reason for why they shy away from applying the CISG.<sup>104</sup> Instead of revealing those facts in public, however, pseudo-scientific aspects are brought into play when trying to explain why the CISG is excluded as the applicable law. It must be added as a most gratifying development that there now seems to be a tendency to desist from opting out of the CISG, in particular where there are only minor differences between the domestic law and the CISG.<sup>105</sup>

## VI. The Necessity of a Supplemental Choice of Law

It has been said that the CISG is a set of rules highly recommendable for international sales transactions. It is a genuinely neutral law and of outstanding legal quality. Its application avoids any imbalance between the parties, both with regard to familiarity with the applicable law and investigation costs. Yet another not insignificant contribution to a reduction in transaction costs is that the CISG is extraordinarily well-documented. Continuously applied, it may have a rationalisation effect similar to the situation achieved when always applying one's own law, or the law of a market-dominating state.

One more advantage is that, indirectly, the application of the CISG reduces the incentive to forum-shop because at least for the questions governed by it, the CISG constitutes a uniform legal basis. This has a highly positive effect on legal certainty and predictability as to the outcome of a dispute.<sup>106</sup> However, two more issues should be addressed in this respect. First, Art. 28 CISG states that "a court is not bound to enter a judgment for specific performance unless the court would do so under its own law in respect of similar contracts of sale not governed by

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deux ans à compter de la découverte du vice." For references to case law under the UCC, the Sale of Goods Act, French, and Dutch case law, see Schlechtriem/Schwenzer/Schwenzer, *supra* note 63, Art. 38 para. 16; Art. 39 para. 17.

<sup>103</sup> See Koch, *supra* note 81, at 910.

<sup>104</sup> Meyer, *supra* note 80, at 475; U. Magnus, Diskussionsbeitrag, in I. Schwenzer (Ed.), *Schuldrecht, Rechtsvergleichung und Rechtsvereinheitlichung an der Schwelle zum 21. Jahrhundert: Symposium aus Anlass des 65. Geburtstages von Peter Schlechtriem* 25 (1999); D. Martiny, *Traditional Private and Commercial Law Rules under the Pressure of Global Transactions: The Role for an International Order*, in R. Appelbaum, W. Felstiner & V. Gessner (Eds.), *Rules and Networks: The Legal Culture of Global Business Transactions* 123, at 140 (2001); Kieninger, *supra* note 6, at 288 *et seq.*; De Ly, *supra* note 51, at 29; Ferrari, *Zum vertraglichen Ausschluss des UN-Kaufrechts*, *supra* note 86, at 737; Murray, *supra* note 73, text at n. 34 *et seq.*; see also Berger *et al.*, *supra* note 50, at 15, 34 with regard to CISG and other 'transnational law'.

<sup>105</sup> Meyer, *supra* note 80, at 483 *et seq.*; De Ly, *supra* note 51, at 28 *et seq.*; Magaud, *supra* note 24, at 389.

<sup>106</sup> Staudinger/Magnus, *supra* note 50, Einleitung para. 6.

this Convention.” Therefore, one might argue, the CISG does not completely eliminate the question as to the most favourable forum because the party seeking specific performance could still avoid a forum whose law would not grant it in the situation at hand.<sup>107</sup> In practice, however, the remedies sought by the parties to an international sales contract will often be dictated by their needs, and the number of cases in which a party will request specific performance where the relevant court would not grant it is small.<sup>108</sup> Art. 28 CISG does not, in fact, lead to a palpable constriction on the general view that an application of the CISG in international sales contracts minimises the incentive to forum shop.

At first sight, actually, another provision might feed ‘best forum’ concerns. According to Art. 7(2) CISG<sup>109</sup>, for questions not governed by the CISG, the conflict of laws rules of the forum remain relevant, with the consequence that for those questions not governed by the CISG, the state in which jurisdiction is established plays a very significant role indeed. However, this concern is not insurmountable, either. The principle of party autonomy gives the parties the right to *choose* the law that governs those questions of the transaction not governed by the CISG,<sup>110</sup> thereby avoiding, to a large extent, forum shopping considerations with regard to the substantive part of the case. In any case, foresighted parties will not leave that issue unaddressed.<sup>111</sup>

Of course, one might argue that if the parties have to agree on another law besides the CISG, the same difficulties will arise that have been described above, namely that both parties will insist on their own law or will be guided by irrelevant considerations such as the political neutrality of the state whose law is chosen, etc. Those difficulties can, however, be overcome if the law subsidiary to the CISG fulfills the same requirements as the CISG itself, namely that it offers genuine neutrality and high legal quality. That question is to be more closely examined in the following. In particular, three sets of rules are to be discussed on an international level: the UNIDROIT Principles, the Principles of European Contract Law (PECL), and the *lex mercatoria*.

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<sup>107</sup> F. Ferrari, “*Forum shopping*“ *trotz internationaler Einheitssachenrechtskonventionen*, 2002 *Recht der Internationalen Wirtschaft* 169, at 176; id., *What sources of law for contracts for the international sale of goods? - Why one has to look beyond the CISG*, 1 *Internationales Handelsrecht* 1, at 19, with further references (2006); Staudinger/Magnus, *supra* note 50, *Einleitung* para. 6.

<sup>108</sup> Müller-Chen, *in* Slechtriem & Schwenzer, *supra* note 61, Art. 28 para. 4, with further references.

<sup>109</sup> Art. 7(2) CISG: “Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, *in conformity with the law applicable by virtue of the rules of private international law*.” (emphasis added.)

<sup>110</sup> As to the limits of party autonomy *see infra* sub F.III.

<sup>111</sup> Similarly Ferrari. Sources, *supra* note 107, at 20 (2006).

## F. UNIDROIT Principles or PECL as the Law Supplementing the CISG

### I. UNIDROIT Principles

To start with, the UNIDROIT Principles<sup>112</sup> “set forth general principles for international commercial contracts”,<sup>113</sup> but do not possess the quality of formal law that, once enacted, becomes binding. They define themselves as a contribution to non-legislative unification of law by compiling, arranging, and structuring international contract law.<sup>114</sup> They are, therefore, sometimes characterised as a restatement of the *lex mercatoria*,<sup>115</sup> although their function appears to exceed that of a mere compilation of existing principles. Rather, the UNIDROIT Principles constitute a set of rules which, in its unifying and comparative approach, clearly develops and enhances international commercial contract law.

In many aspects, the UNIDROIT Principles are similar to the CISG. They differ, however, in scope, as they do not deal with sales law in particular, but intend to provide solutions for all sorts of international commercial contracts. They are, therefore, on the one hand broader in their scope and on the other hand of a more unspecific nature than the CISG.

Their broad scope, together with their similarity to the CISG, in particular with regard to their concept of remedies, renders them a suitable supplement to the CISG. Where the latter leaves a question unsettled, the UNIDROIT Principles might fill the gap. For example, according to Art. 4 CISG, the CISG is not concerned with the validity of the contract, whereas the UNIDROIT Principles have settled that question in their Chapter 3. Likewise, the CISG does not deal with agency, whereas the UNIDROIT Principles do (Art. 2.2.1-2.2.10). Furthermore, although the CISG might have provisions addressing a particular problem, they might be less detailed than the corresponding provisions in the UNIDROIT Principles. An apt illustration are the provisions on the formation of a contract, which are similar under the CISG and the UNIDROIT Principles. However, the latter are clearly more detailed and address several questions that the CISG leaves open, such as merger clauses or the inclusion of standard terms.<sup>116</sup>

<sup>112</sup> UNIDROIT Principles of International Commercial Contracts, 2<sup>nd</sup> ed. (2004).

<sup>113</sup> See the Preamble, 1st line.

<sup>114</sup> E. Kramer, *Funktionen allgemeiner Rechtsgrundsätze – Versuch einer Strukturierung*, in H. Koziol & P. Rummel (Eds.), *Im Dienste der Gerechtigkeit: Festschrift für Franz Bydlinski* 197, at 213 (2002); K. Berger, *The Principles of European Contract Law and the concept of the “Creeping Codification” of law*, 2001 (1) *European Review of Private Law* 21, at 24.

<sup>115</sup> See Leible, *supra* note 1, at 312.

<sup>116</sup> Art. 2.1.17 *et seq.* UNIDROIT Principles.

## II. PECL

The same is true for the Principles of European Contract Law (PECL), which have been described as the counterpart of the UNIDROIT Principles.<sup>117</sup> The PECL, like the UNIDROIT Principles, are considered to be part of the *lex mercatoria*<sup>118</sup> and are intended to be applied as general rules of contract law in the European Community.<sup>119</sup> Their main purpose is to serve as a draft of a part of a European Civil Code. Having also been influenced by the CISG<sup>120</sup> and developed to now cover a respectable part of contract law,<sup>121</sup> the PECL are, like the UNIDROIT Principles, an ideal supplement to a choice of law clause nominating the CISG. Here again, the parties can agree on the CISG *and*, for questions not governed by it, on the PECL. By applying the PECL, the parties are assured of receiving a genuinely international – and therefore neutral – solution to their case, together with all of the privileges and advantages of applying a neutral law.

What has been said on the documentation of the CISG<sup>122</sup> also holds true for the UNIDROIT Principles and the PECL: there is a remarkable amount of literature referring to and analysing the provisions of the UNIDROIT Principles and the PECL. Particularly helpful with regard to a choice of law of 'the CISG and the PECL' or 'the CISG and the UNIDROIT Principles' is academic writing that takes a comparative approach, namely by juxtaposing the CISG, the PECL, and the UNIDROIT Principles for the sake of comparison.<sup>123</sup>

## III. Eligibility of UNIDROIT Principles and PECL as the *Lex Causae*

### 1. In State Court Proceedings

Opponents to the idea of choosing either the PECL or the UNIDROIT Principles as the law governing an international contract refer to the fact that they are not 'real law', but rather a mere collection of generally acknowledged principles. They should therefore, as the argument goes, not be eligible to replace the otherwise applicable law, including its mandatory provisions.<sup>124</sup> Indeed, this question

<sup>117</sup> See Berger, *supra* note 114, at 22.

<sup>118</sup> Art. 1:101(3)(a) PECL; see also O. Lando, *The Principles of European Contract Law and the lex mercatoria*, in J. Basedow *et al.* (Eds.), *Private Law in the International Arena: Liber Amicorum Kurt Siehr* 391, at 397 (2000).

<sup>119</sup> Art. 1:101(1) PECL.

<sup>120</sup> See *supra*, sub E.V.5.a.

<sup>121</sup> Parts I and II cover the core rules of contract formation, authority of agents, validity, interpretation, contents, performance, non-performance (breach) and remedies. Part III covers plurality of parties, assignment of claims, substitution of new debt, transfer of contract, set-off, prescription, illegality, conditions and capitalisation of interest.

<sup>122</sup> See *supra*, sub E.III.

<sup>123</sup> O. Lando, *Das neue Schuldrecht des Bürgerlichen Gesetzbuchs und die Grundregeln des europäischen Vertragsrechts*, 67 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 231 *et seq.* (2003); for multiple references see Kegel & Schurig, *supra* note 18, at 116, footnotes 459 and 460.

<sup>124</sup> See, e.g., C.-W. Canaris, *Die Stellung der "UNIDROIT Principles" und der "Principles of*

depends on the applicable choice of law rules. As to state court proceedings, the spectrum of opinions reaches from ineligibility of the UNIDROIT Principles and the PECL (i.e., mandatory domestic law remains applicable)<sup>125</sup> to acceptance of those sets of rules as a comprehensive choice of law by the parties.<sup>126</sup> The latter position is increasingly winning recognition: pursuant to Art. 3(2) of the European Regulation Proposal on the law applicable to contractual obligations (Rome I) of December 2005, “[t]he parties may also choose as the applicable law the principles and rules of the substantive law of contract recognised internationally or in the Community”. The proposed provision “authorise[s]”, according to the wording in the explanatory note, “the choice of the UNIDROIT principles, the *Principles of European Contract Law* or a possible future optional Community instrument [...]”.<sup>127</sup>

This development comes as no surprise. The PECL and the UNIDROIT Principles are not merely an unstructured bundle of principles common to the international commercial market. On the contrary, they are presented in the form of a code, comprising articles which, like the American Restatements, are supplemented with comments explaining their operation, and their legal quality is regularly emphasised. Several court decisions and arbitral awards have interpreted domestic commercial law provisions in light of the corresponding provisions of the PECL and the UNIDROIT Principles.<sup>128</sup> These principles encapsulate the common core of internationally accepted or acceptable principles in contract law

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*European Contract Law*” in *System der Rechtsquellen*, in J. Basedow (Ed.), *infra* note 128, at 17 *et seq.*; for further references see Leible, *supra* note 1, at 314 n. 134.

<sup>125</sup> The majority in German legal literature denies the eligibility of the UNIDROIT Principles and the PECL as the law that would supersede any mandatory provisions of the law applicable under the German conflict of laws rules in state court proceedings (Art. 27 EGBGB), see F. Blase, *Die Grundregeln des Europäischen Vertragsrechts als Recht grenzüberschreitender Verträge* 221 *et seq.* (2001); for a contrary view see Leible, *supra* note 1, at 315 *et seq.*

<sup>126</sup> According to most legal authors, the Swiss conflict of law rules are more generous, both for state court and arbitration proceedings, see Art. 116(1), 187(1) Swiss Private International Law; J. Frick, *Die UNIDROIT-Prinzipien für internationale Handelsverträge*, 2001 *Recht der Internationalen Wirtschaft* 416, at 419; M. Keller & J. Kren Kostkiewicz, *Art. 116 para. 17*, in D. Girsberger (Ed.), *Zürcher Kommentar zum IPRG* (2004); A. Heini, *Art. 187 para. 7 et seq.*, in (same volume),

<sup>127</sup> Art. 3 of the Proposal for a Regulation of the European Parliament and the Council on the law applicable to contractual obligations (Rome I), COM(2005) 650 final, 2005/0261 (COD); this amendment was already proposed by K. Boele-Woelki, *Principles and Private International Law — The UNIDROIT Principles of International Commercial Contracts and the Principles of European Contract Law: How to Apply Them to International Contracts*, 1996 *Uniform Law Review* 652 *et seq.*; U. Drobnig, *Vereinheitlichung von Zivilrecht durch soft law: neuere Erfahrungen und einsichten*, in J. Basedow *et al.* (Eds.), *supra* note 78, at 753; Berger *et al.*, *supra* note 50, at 31.

<sup>128</sup> See ICC Award No. 8486, *Clunet* 1998, 10478, with note Y. Derains, 1050 *et seq.*, construing the provision on force majeure of the Dutch Civil Code in light of the UNIDROIT Principles; see also on this award Berger, *supra* note 114, at 31 *et seq.*; see furthermore H. Wiedemann’s case review of the German Bundesgerichtshof, 26 September 1997, in 1998 *Juristenzeitung* 1173 *et seq.*; an interesting dogmatic approach has been provided by E. Kramer, *Konvergenz und Internationalisierung der juristischen Methode*, in C. Meier-Schatz (Ed.), *Die Zukunft des Rechts* 71, at 82 (1999): the reference in the last sentence of the Preamble of the UNIDROIT Principles to “national and international legislators” should be construed in a functional manner so as to encompass domestic judges who develop the law “like legislators” under Art. 1(2) Swiss Civil

and are based on a thorough comparative analysis of a large number of domestic legal systems. They mirror a concise, comprehensive, and workable statement of principles of contract law derived from the 'best pickings' of various legal systems.

## 2. In Arbitration Proceedings

With regard to arbitration, the UNCITRAL Model Law on International Commercial Arbitration from 1985, on which practically all modern arbitration laws are based,<sup>129</sup> allows the parties to subject their contract to the "rules of law" they wish (Art. 28(1), sentence 1). The annotated UNCITRAL Explanatory Note states that "by referring to the choice of 'rules of law' instead of 'law', the Model Law gives the parties a wider range of options as regards the designation of the law applicable to the substance of the dispute in that they may, for example, agree on rules of law that have been elaborated by an international forum but have not been incorporated into any national legal system."<sup>130</sup> The parties' right to choose the UNIDROIT Principles and the PECL as the applicable law (which supersedes any mandatory provisions that would be applicable by way of conflicts of law rules) is, therefore, widely recognized.<sup>131</sup>

## IV. Reduction of Forum Shopping

Finally, when choosing them as the subsidiary law in an international sales contract, the problem of forum shopping can be reduced. First, the substantive law is genuine international law. One need not consider, as a precautionary measure, the possibly applicable conflicts of law rules for questions not governed by the CISG because the subsidiary law applicable to the dispute is certain – and it is neutral, possessing all the positive consequences described above. Secondly, since the procedural rules in international arbitration are more or less comparable to each other, major incentives for a particular forum are lacking.

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Code. On the discussion under the German Civil Code, see the contributions in J. Basedow (Ed.), *Vertragsrechtsvereinheitlichung und deutsches Recht* (2000).

<sup>129</sup> See the status on legislation based on the UNCITRAL Model Law at [http://www.uncitral.org/uncitral/en/uncitral\\_texts/arbitration/1985Model\\_arbitration\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration_status.html).

<sup>130</sup> Explanatory Note by the UNCITRAL Secretariat on the Model Law on International Commercial Arbitration, n. 35, [http://www.uncitral.org/uncitral/en/uncitral\\_texts/arbitration/1985Model\\_arbitration.html](http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration.html).

<sup>131</sup> From the lengthy list of authorities see, e.g., Canaris, *supra* note 124, at 20; H. Kronke, *Internationale Schiedsverfahren nach der Reform*, 1998 *Recht der Internationalen Wirtschaft* 257, at 262 *et seq.*; F. Vischer, *The Relevance of the UNIDROIT Principles for Judges and Arbitrators in Disputes Arising out of International Contracts*, 1 *European Journal of Law Reform* 203, at 206 (1999); H. van Houtte, *The UNIDROIT Principles of International Commercial Contracts*, 11 *Arbitration International* 373, at 382 (1995); H. Schlosser, *Das Recht der internationalen privaten Schiedsgerichtsbarkeit*, 2<sup>nd</sup> ed., para. 191, 732, 749, 836. (1989)

## V. Summary

In conclusion, both the UNIDROIT Principles and the PECL constitute a perfect supplement to the CISG. If the advice here is not to choose the PECL or the UNIDROIT Principles alone, without referring to the CISG as well, it is only because the CISG is an international *sales* convention and, as such, much more detailed as to the specific sales-related questions. It is proper sales law, dealing with the rights and duties of seller and buyer, passing of risk, the definition of the term ‘non-conformity’ in a sales law context, etc. Nonetheless, for those questions not addressed by the CISG, the PECL and the UNIDROIT Principles are recommendable as a complementary choice of law,<sup>132</sup> because their legal solutions are on an international par with the CISG.

## G. The *Lex Mercatoria* to Supplement the CISG?

### I. The Vagueness of *Lex Mercatoria*

There is an ongoing debate as to whether a *lex mercatoria* exists and, if it does, what its content is.<sup>133</sup> The UNIDROIT Principles and the PECL do define themselves as possibly applicable where the parties have chosen the *lex mercatoria*.<sup>134</sup> The equation of *lex mercatoria* with the PECL and the UNIDROIT Principles, respectively, has been disputed,<sup>135</sup> although a clear definition is still lacking. Instead, one frequently finds rather vague descriptions circumscribing the *lex mercatoria*, for example, as “a set of rules finding their origins outside domestic legal systems which is applicable to international business transactions” and which, “[b]y and large, [...] is composed of international sources of law and self-regulatory rules.”<sup>136</sup>

<sup>132</sup> Holding a different view R. Herber, “*Lex mercatoria*” und “*Principles*” – gefährliche Irrlichter im internationalen Kaufrecht, 2003 Internationales Handelsrecht 1, at 4; Mankowski, *supra* note 3, at 11: “Die Principles bleiben gleichsam ein virtuelles ‘Recht’.”

<sup>133</sup> See the references in J. Lew, L. Mistelis & S. Kröll, *supra* note 21, n. 47; Berger *et al.*, *supra* note 50. The *lex mercatoria* has also raised a lively debate in legal theory as to its quality as a new ‘world trade law’, see, e.g., G. Teubner, *Die unmögliche Wirklichkeit der lex mercatoria: Eine Kritik der théorie ludique du droit*, in M. Lieb, U. Noack & H. P. Westermann (Eds.), Festschrift für Wolfgang Zöllner zum 70. Geburtstag 565 *et seq.* (1999); P. Zumbansen, *Lex mercatoria: Zum Geltungsanspruch transnationalen Rechts*, 67 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 637 *et seq.* (2003).

<sup>134</sup> See *supra* sub F.I, II.

<sup>135</sup> Qualifying the UNIDROIT Principles and the PECL as *lex mercatoria* would require its “acceptance by the international community of traders (‘societas mercatorum’) and by international arbitral tribunals as the natural judges of international trade and the social engineers of transnational commercial law.”, Berger, *supra* note 114, at 33. Likewise, Lando, *supra* note 118, at 399 *et seq.*, does not equate *lex mercatoria* with PECL; see, further, the discussion in Blase, *supra* note 125, at 248 *et seq.*

<sup>136</sup> F. DeLy, *Lex Mercatoria (New Law Merchant): Globalization and International Self-Regulation*, in R. Appelbaum, W. Felstiner & V. Gessner (Eds.), *Rules and Networks – The Legal Culture of Global Business Transactions* 159, at 161 (2001).

It has been said that, under this approach, the *lex mercatoria* is, to a certain extent, influential on scholars; furthermore, it has had an impact on the French International Arbitration Act<sup>137</sup> and in mega-arbitration, such as in the petroleum industry.<sup>138</sup> The latter cases often involve state contracts which raise specific problems; therefore, they are not representative of international commercial arbitration in general.<sup>139</sup> In other cases, the *lex mercatoria* has had only limited practical impact. In ICC arbitration in 2004, for example, only one contract provided for a choice of “general principles of law”.<sup>140</sup>

Within the scope of ‘normal-sized’ commercial sales transactions, as are being dealt with here, the *lex mercatoria* is yet to be entirely accepted in the legal world.<sup>141</sup> It appears, after all, as a fragmentary, unsystematic, and intransparent body of law.<sup>142</sup> This becomes evident if it is compared to the UNIDROIT Principles and the PECL, which are clearly researched, structured, and compartmentalised sets of rules. Through this effort to structure and elucidate principles and valuations derived from thorough comparative analysis, the UNIDROIT Principles and the PECL distinguish themselves from the *lex mercatoria*. As Drobnig has pointed out, “already in condensing uncertain, often rather unconscious thoughts and expectations to specific words, there is a considerable intellectual achievement and, in particular, an attainment of scientific knowledge, because of the necessary comparative preparatory work.”<sup>143</sup> The *lex mercatoria* within the broad meaning set out above is yet to take that step.

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<sup>137</sup> It is acknowledged that the idea of a *lex mercatoria*, as it is understood today, was primarily developed in the 1920s in France, in some instances to relieve international transactions from mandatory provisions of domestic law, e.g., to abolish the prohibition on arbitral clauses for merchants or the non-severability of arbitral clauses, F. De Ly, *International Business Law and Lex Mercatoria* 293 *et seq.* (1992); Breitenstein, *supra* note 9, at 114, 125 *et seq.*

<sup>138</sup> See De Ly, *supra* note 137, at 176 *et seq.*

<sup>139</sup> *Ibid.*; see also F. Dasser, *Lex Mercatoria – Critical Comments on a Tricky Topic*, in R. Appelbaum, W. Felstiner & V. Gessner (Eds.), *Rules and Networks – The Legal Culture of Global Business Transactions* 189, at 191 *et seq.*

<sup>140</sup> ICC Bulletin 16 (spring 2005) 5, 11.

<sup>141</sup> See Mankowski, *supra* note 3, at 13; Martiny, *supra* note 104, at 148.

<sup>142</sup> Attempts to structure and systematise the rules that, in their entirety, should constitute the *lex mercatoria*, are ongoing, see the Transnational Law Database operated by CENTRAL, <http://www.tldb.de/>; K. Berger, *The CENTRAL-List of Principles, Rules and standards of the Lex Mercatoria*, in Center for Transnational Law (Ed.), *Transnational Law in Commercial Legal Practice* (1999) 121 *et seq.*; however, differences in definition and conception among legal scholars and practitioners are still considerable, unless the *lex mercatoria* is limited to very basic principles such as *pacta sunt servanda* or *force majeure*, see in this regard the survey by J. Lew, L. Mistelis & S. Kröll, *supra* note 21, para. 18-57; Berger *et al.*, *supra* note 50, at 32 *et seq.*

<sup>143</sup> Drobnig, *supra* note 127, at 750:

Allein in [der] Reduktion von unbestimmten, oft eher unbewussten Gedanken und Vorstellungen zu konkreten Worten liegt aber bereits wegen der erforderlichen rechtsvergleichenden Vorarbeiten eine erhebliche intellektuelle Leistung und insbesondere ein Erkenntnisgewinn.

## II. *Lex Mercatoria* – Not Recommendable in a Choice of Law Clause

Accordingly, the question of whether the parties to an international sales contract are entitled to choose the *lex mercatoria* as the law governing their contract in non-arbitral proceedings is highly disputed.<sup>144</sup> The Proposal to the Rome I Regulation of December 2005 excludes the possibility of choosing the *lex mercatoria*.<sup>145</sup> More precisely, the *lex mercatoria* is subject to the mandatory provisions of the objectively applicable law. This leads to the consequence that its choice does not spare the parties the objective determination of the applicable substantive law, the avoidance of which was precisely the parties' goal.<sup>146</sup>

For international arbitration, the parties' choice of the *lex mercatoria* as the law governing the contract appears to be widely accepted.<sup>147</sup> Turning, however, to the question of whether the parties to an international sales contract should choose the *lex mercatoria* as the law governing their contract, the answer must be in the negative. Its lack of public acceptance, its uncertainty as to what exactly it comprises, and its 'invisibility' might be a blessing in mega-arbitration, but in an ordinary sales contract, if the parties make the effort at all to agree on a choice of law, they will usually desire clear, legal, and credible rules. Unfortunately, a choice of the *lex mercatoria* will not avoid disputes as to the content of the applicable law – which is the intention – but rather create them.<sup>148</sup>

## H. Final Summary

It has been shown that the dominant factor when making a choice of law is each party's respective interest in the applicability of its own domestic law. It has the advantages of being familiar and cost-saving, in that the party whose law has been

<sup>144</sup> Art. 116(1) Swiss Private International Law provides, according to prevailing legal opinion, for such a possibility, see Keller & Kren Kostkiewicz, *supra* note 126, Art. 116 para. 17, with further references; for the situation in other European states see, e.g., H.-P. Schroeder & B. Oppermann, *Anerkennung und Vollstreckung von Schiedssprüchen nach lex mercatoria in Deutschland, England und Frankreich*, 99 Zeitschrift für vergleichende Rechtswissenschaft 410, at 423 *et seq.* (2000).

<sup>145</sup> Explanatory Memorandum to the Proposal relating to Art. 3, which deals with the parties' choice of law:

The form of words used [in Art. 3] would authorise the choice of the UNIDROIT principles, the *Principles of European Contract Law* or a possible future optional Community instrument, while excluding the *lex mercatoria*, which is not precise enough ....

<sup>146</sup> Mankowski, *supra* note 3, at 13 *et seq.*

<sup>147</sup> Mistelis, *supra* note 59, at 25; on ICC arbitration see H. Grigera Naón, *Choice-of-Law Problems in International Commercial Arbitration*, 289 *Receuil des Cours* (2001); on the Swiss international arbitration see Heini, *supra* note 126, Art. 187 para. 7a; on France see Schroeder & Oppermann, *supra* note 144, at 425; on Art. 28(1), sentence 1 UNCITRAL Model Law on International Commercial Arbitration 1985 and the domestic legislation which has adopted this provision see Lando, *supra* note 118, at 400 *et seq.*

<sup>148</sup> O. Sandrock, *Internationales Wirtschaftsrecht*, in *Theorie und Praxis* (1995), at 441 (quoted in von Breitenstein, *supra* note 9, at 135).

chosen will not need to incur the high costs of examining and familiarising itself with another foreign law. It stands to reason that since both parties will usually insist on their own law, a dispute may arise as to which choice of law clause takes precedence. The choice of a neutral law should prevent one party from having a comparative advantage over the other with respect to the costs of 'bringing itself up to speed' in the law chosen. However, sometimes the law of a third state will be more related to the legal system of one of the parties anyway, thereby discrediting this argument. Furthermore, the neutral domestic law chosen might, in fact, contain legal concepts unsuited to the contract at hand. There is the risk that, in agreeing on a neutral law, the law of a politically neutral state is chosen, although the question of political neutrality has nothing to do with the question of whether a law provides for a well-balanced allocation of contractual rights and duties. After all, choosing a neutral domestic law might be too expensive since both parties will be burdened with the high costs of examining such a law.

There is one possible way to overcome these difficulties, namely through the application of unified sales law in the form of the CISG. The CISG is genuinely neutral law and provides a well-balanced concept for both buyer and seller. It is flexible, it has rationalisation potential, and it raises only negligible costs of examination since it is very well-documented. These factors keep transaction costs at a low level altogether. The choice of the CISG *alone* does, in fact, not avoid forum shopping since the CISG has only a limited scope of application, leaving questions not dealt with by it to be decided according to the domestic law indicated by the applicable conflict of laws rules (Art. 7(2) CISG)). This difficulty can be avoided to a great extent if the parties logically continue their approach that led to their choice of the CISG and agree on the UNIDROIT Principles or the PECL as the supplementary law. The possibility of choosing these sets of rules in arbitration is now widely accepted (see Art. 28(1) UNCITRAL Model Law), and many conflict of laws rules allow that choice in non-arbitral proceedings as well. The UNIDROIT Principles and the PECL encapsulate the common core of contract law principles accepted internationally, or Europe-wide, respectively, and constitute a concise, comprehensive, and workable set of rules.

The *lex mercatoria*, in contrast, lacks the elements of structure, systemisation, and transparency. These significant deficiencies seriously speak against choosing it as the law applicable to a sales contract. The need for foreseeability and reliability in the law cannot be safeguarded. On the one hand, party autonomy in non-arbitral proceedings is often restricted to the effect that the *lex mercatoria* cannot be the *lex causae*; a choice of *lex mercatoria* will always be subject to the mandatory provisions of the latter. In arbitration, on the other hand, the flexibility and creativity given to arbitrators when applying the *lex mercatoria* might be a desire in mega-arbitration, but it will not usually be of benefit in 'normal-size' sales contracts.

