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** **The Law Society of England and Wales would like to request that its response to the consultation be published in full, rather than in a summarised form.***



The Law Society

January 2011

Response to Commission Green Paper on policy options for progress towards a European Contract Law for consumers and businesses

SUPPORTING
solicitors

EUROPEAN CONTRACT LAW

The Law Society of England and Wales (“the Society”) is the representative body of over 140,000 solicitors qualified in England and Wales. The Society negotiates on behalf of the profession and makes representations to regulators and government in both the domestic and European arena.

The Society has consulted widely on the Green Paper on policy options for progress towards a European Contract Law for consumers and businesses. This briefing paper includes input from practitioners working in a range of different fields both in-house and in private practice, including those who specialise in business-to-consumer and business-to-business contracts, and those serving the needs of small and medium-sized enterprises (SMEs). Contained in this paper are the preliminary views of the Society. The Society will follow developments and may update its views.

EXECUTIVE SUMMARY

1. The Society would like to work with policymakers to improve the functioning of the internal market. It supports the initiative for a non-binding “toolbox” that could be used by European legislators to improve the quality, coherence and consistency of European legislation. A set of common terminology could be of considerable assistance and could lead to a growing shared understanding of relevant concepts and more consistent transposition of European Union (EU) law throughout the Community.
2. In addition, the Society believes that an initiative to create some optional standard form terms and conditions for use in cross-border contracts, rather than an optional “28th regime” of European contract law, could be a pragmatic, achievable and low-cost option that could deliver benefits for both SMEs and consumers in cross-border contracts.

Need

3. The Society does not agree that a need for an “optional instrument” of European contract law has been demonstrated and consequently opposes its introduction.
4. The Society agrees fully that increasing cross-border sales, especially to end-consumers, would assist in the integration of the internal market. However, it does not agree that the mere diversity of national contract laws in fact impedes such trade. It believes that many of the barriers to cross-border trade are practical and procedural. In the case of consumers, it is the problem of obtaining practical redress when a problem arises in a cross-border contract that is believed to be the key issue. In the same way, for businesses, we understand that some of the greatest barriers to entering the markets of other Member States relate to the different court processes (and fears as to whether proceedings will be fair and efficient), regulatory hurdles, means of seeking redress and problems relating to enforcement mechanisms.
5. The diversity of contract laws does mean that businesses may wish to take legal advice, but in-house lawyers that we have consulted are unconvinced that an instrument of European contract law would be of assistance because it would lack any established jurisprudence and it would not be possible to ensure uniform interpretation of a new instrument across the Member States and so national divergences would continue. Practitioners note that, in practice, when advising businesses on cross-border transactions, the underlying contract law does not differ greatly between Member States. The laws in relation to other topics, e.g. advertising, packaging requirements, product liability and non-contractual representations, are also relevant and equally important. For business, the uncertainty about these requirements greatly increases the risk of making overseas sales.
6. For business-to-consumer contracts, practitioners note that businesses’ fear of selling into another Member State often relates to contracts being subject to the consumer protection offered to consumers by their home Member State laws. An “optional instrument” would only enable sellers to know the consumer protection rules across the Member States if these were harmonised or if all

such transactions were governed by the 28th regime. It is also unclear whether all parties to a contract would have to agree that the “optional instrument” should be used or whether, if all the consumers who were party to the contract wanted to use the “optional instrument”, the business party or parties would be forced to use this, or vice versa.

7. The Society does not believe that the issue of inequality in bargaining power between businesses of different sizes, which occurs in any market, should be addressed through an “optional instrument”. The Society is supportive of the freedom of parties to contract on the terms that they wish. Contracting parties negotiate and, for the contract to be agreed, each side needs to be satisfied that the contract is fairly drafted from their perspective. Weaker parties in a market will often group together to negotiate standard form contracts. In the case of two SMEs of equivalent bargaining power from different Member States, an example of an obvious “neutral law” would be Swiss law with its established jurisprudence.

Further analysis and an impact assessment

8. The Society believes that there is a need for further analysis of the legal barriers to cross-border trade. It also believes though that, given that discussions in the European institutions are focussing on an “optional instrument”, there is an urgent need for an impact assessment of the key options in the Green Paper and that this must be broad and consider the different options outlined.

Lack of practitioner input (both in general and from common law jurisdictions)

9. England and Wales practitioners would like to be included in the discussions and drafting processes taking place in the European institutions. The profession has great experience working with other jurisdictions and on cross-border contracts and could offer valuable expertise. The Society is concerned that the group of experts convened by the European Commission is mainly comprised of academics and would welcome the direct involvement of common law practitioners in the drafting process.

Uncertainty

10. Whilst there is always a level of inherent uncertainty in new legislation, the Society believes that an “optional instrument” would cause particular problems because there would be uncertainty as to the meaning of the new instrument and its interpretation, which would evolve over time, and also uncertainty as to the scope of its application. It is also unclear how the Court of Justice (both in regard to its role within the Treaties and current capabilities) would be able to create jurisprudence of a commercial nature and this raises concerns because any contract law is closely bound up with the mechanism for its enforcement through the courts. Given that no need has been evidenced for a new instrument, this seems a disproportionately large amount of uncertainty for businesses and consumers and the Society thinks that the result of this is likely to be that the new instrument would not be used much in practice. Instead, the Society would favour legislative initiatives to improve practical means of redress available for businesses and consumers when engaging in cross-border contracts, which it believes would positively improve the functioning of the internal market. The Society could also support the introduction of some optional standard form terms and conditions, as outlined above.
11. In regard to the scope of an “optional instrument”, confusion could be caused if some issues in an agreement fall outside the subject matter covered (which we understand is likely to cover the sale of goods). For example, if the contract also covered the sale of services, this would still need to be governed by the contract law of a Member State. Many cross-border transactions also involve additional areas of law, for example, the law of property and, if something goes wrong, the law of tort. These would still need to be governed by the laws of a Member State.

Legal basis

12. It is unclear whether there is a legal basis under the Treaties to create an “optional instrument”. In order to establish this, the Commission must provide a clear justification for any proposal it makes,

demonstrating that different contract laws do genuinely obstruct the proper functioning of the internal market, and that any obstructions apparently caused by different contract laws are not in fact due to other causes. Any solution proposed to address proven difficulties would need to address those difficulties in a proportionate manner and in accordance with the principle of subsidiarity.

Cost

13. The only body that would be able to announce authoritatively on the meaning of an “optional instrument” would be the Court of Justice. This is by nature a constitutional court, unable to substitute its own decision for that of a national court or EU regulatory body. The cost of expanding the Court of Justice’s role and workload would be considerable. In general, its judges do not have commercial experience and parties encounter long delays even with its current workload. This would, we believe, lead to a divergence in the application of a new instrument between Member States as many parties would not elect to appeal to the higher courts in disputes. (The suggestion that there could be a database of decisions across the EU is interesting but would not have the legal effect of decisions by senior courts or the Court of Justice. There would be no means of knowing which one of conflicting interpretations was the correct one.)
14. The legal professions and judiciary across the Member States would need to be re-trained. The Society notes that, without further information on the content or scope of a new instrument, it is impossible to give an accurate calculation of the training costs it would create. As contract law is a core subject studied as part of a Law degree, there would be further costs in training sufficient academics and, for students, there would be an impact on the other topics they were able to study if this initiative became compulsory.

SUGGESTED APPROACH

An initiative to deliver EU-endorsed contractual terms and conditions for various transactions

15. The Society believes that an initiative to deliver EU-endorsed simplified conformed contractual terms and conditions for certain types of transactions ("Common Ts and Cs") could be used by contracting parties in cross-border contracts, together with guidance on the Common Ts and Cs. The Society believes that this would bring many of the benefits that it has been argued an "optional instrument" would deliver, but without the uncertainties and practical difficulties associated with that proposal. It is currently developing the approach in greater detail.

What types of contract might be appropriate for Common Ts and Cs?

16. The Commission has identified a category of potential on-line transactions which are not currently being entered into as regularly as would be expected in a single market. The Society recognises that these contracts might become more attractive if the retailer could elect to use common contractual terms across the Member States in a form which has some independent EU accreditation. These contracts could be enforced under a Member State's national legal system and could be made available on an on-line platform together with guidance as to how they would work in practice. For consumers, such a proposal would be fully compatible with Article 6 of the Rome I Regulation in that the terms would be common, but the governing law would be the country of habitual residence of the consumer. The guidance would help to demonstrate how the Common Ts and Cs would be expected to work in practice under the relevant national law.

17. Clearly it would be important to set the boundaries for any such project which could be delivered in stages. In time, the project could be rolled out (possibly in conjunction with industry associations and consumer interest groups) to consider a wider range of transactions.

An achievable and pragmatic proposal which could be delivered in the short term

18. We consider the proposal for a programme to deliver Common Ts and Cs to be an achievable, pragmatic and efficient way for the EU Institutions to deliver on the promise to remove barriers to cross-border transactions, thus:

- making cross-border transactions simpler, easier and more frequent; and
- supporting both consumers and SMEs which may have been deterred from doing business in markets outside their home jurisdiction by concerns about the way in which their terms and conditions would be interpreted.

19. The project would, through the negotiation of the Common Ts and Cs and the provision of guidance about them, identify areas where the sale of goods and services legislation of various member states is inconsistent or in conflict. Accordingly, the project would highlight areas where focussed harmonisation initiatives might be undertaken.

20. We feel that EU endorsed Common Ts would:

- be a pragmatic and proportionate response to the legitimate concerns and objectives which have been raised;
- be deliverable in the short to medium term; and
- would be easier for Member States to agree and of more benefit for consumers and businesses.

21. The creation of Common Ts and Cs would go a long way to satisfy the objectives of the Commission as set out in the Green Paper but without the additional complications and jurisdictional challenges of Options 3 to 7 as set out in that Green Paper. Furthermore it is a project that should be deliverable within a shorter time period than an “optional instrument”.
22. Given the different standards across the Member States, the Common Ts and Cs would have to be compliant with rules in all Member State jurisdictions, and would consequently be overly compliant with national rules in some jurisdictions. The Common Ts and Cs would essentially comprise an EU “gold standard” that contracting parties could access on-line and be assured would be acceptable in the Member State that they wished to contract in. It would leave businesses and consumers with the option to take specific advice on a specific national legal system if they wished to.

What would the EU endorsed Ts and Cs look like?

23. Parties would only contract under the national law of a Member State on the terms of the Common Ts and Cs if a contract was reduced to writing and they chose to use the Common Ts and Cs. This approach would be necessary to rebut the national laws of member states (where contracts may arise as a matter of law and may not need to be reduced to writing).
24. We would suggest any document would follow an approach as follows:
- a standard set of contract terms;
 - a schedule detailing specific variations;
 - a front sheet setting out the subject matter of the contract and key negotiated terms (price/quantity/timing/delivery); and
 - guidance as to how the Ts and Cs would be expected to work in example situations.
25. A Common Ts and Cs project could be rolled out across a range of transactions for specific types of goods and/or services but would be entirely optional. Cooperation with industry associations and consumer interest groups would further embed the principles across the member states, deliver common best practice and create a broad constituency of advocates for the initiative who would have practical experience of the sorts of issues that need to be dealt with – so that the Ts and Cs would work well in practice.
26. An example:

I want new glazing in my home. I go to a firm in the UK accredited by the relevant UK industry body and government department. If the terms of contract also being offered by a French or Italian glazier were the same, I might consider using them instead. However, I am unlikely to go abroad if I have no comfort I will get the same benefits as in the UK market.

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ABBREVIATIONS

Brussels I = Regulation 44/2001 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters

CISG = United Nations Convention on Contracts for the International Sale of Goods (1980)

CJEU = Court of Justice of the European Union

Consumer Rights Directive = Proposal for a Directive on Consumer Rights (COM(2008) 614/3, 08.10.2008)

DCFR = Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference, Outline Edition prepared by the Study Group on a European Civil Code and the Research Group on EC Private Law (Acquis Group) (Sellier, 2009)

Expert Group = Group of experts convened by the Commission following Commission Decision setting up the Expert Group on a Common Frame of Reference in the area of European contract law (2010/233/EU, 26.04.2010)

Green Paper = Green Paper from the Commission on policy options for progress towards a European Contract Law for consumers and businesses (COM(2010) 348 final, 1.7.2010)

PECL = The Principles of European Contract Law prepared by the Commission on European Contract Law (Part I, published 1995; Part II, published 1999; and Part III, published in 2003)

PICC = UNIDROIT Principles of International Commercial Contracts (2004)

Rome I = Regulation 593/2008 on the law applicable to contractual obligations

Rome II = Regulation 864/2007 on the law applicable to non-contractual obligations

TEU = Consolidated version of the Treaty on European Union (2010/C 83/01)

TFEU = Consolidated version of the Treaty on the Functioning of the European Union (2010/C 83/01)

UCC = United States Uniform Commercial Code (first published 1952)

1. INTRODUCTION

27. We are not aware of any significant problems (economic or legal) arising from any divergence of contract laws at a national level between Member States. In our experience parties simply choose the national contract law that best suits them (and less sophisticated parties may give little or no thought to the matter). Rome I addresses any conflicts that may arise if there is a dispute with regard to the governing law of the contract.¹
28. The existing laws of contract in Member States are long-established and most have been in place for many years (e.g. the first edition of the English textbook Chitty on Contracts was published in 1826 and the principles of English contract law go back several centuries before that). Their strengths and weaknesses are known and have been tested before the courts. There is a body of case law which allows lawyers to advise on, and clients to assess, the risks. Standard contractual provisions such as those limiting liability or confirming the parties' non-reliance on representations have been well-explored.
29. Moreover there are existing initiatives that have attempted to harmonise contract law and to which the Commission briefly refers in the Green Paper. These include: the CISG, which has been widely adopted (though not by the UK); the PICC, which has been used in CISG arbitrations and has acted as a gap-filling neutral option in arbitrations where parties have come up with unusual or vague applicable law provisions, or even where there is no choice; and in the US, the UCC.² Consumers and businesses (small and large) are already able to incorporate uniform codes into their contracts but, from what we can see, they rarely do so, preferring instead to use national laws or, in federal systems where contract law is not a federal competency (e.g. the US), State laws.³ A move in the direction of taking contract law from national/State competency to federal/Community competency would entail major changes and is not something that the US has attempted in its 250-year history.
30. In September and October 2010, the Society conducted telephone interviews with senior representatives from 602 private practice law firms across England and Wales.⁴ 91 firms had advised on a deal with a party from another jurisdiction in the last year. Our findings show that "legal certainty" and "familiarity with the legal system of contracting parties" are the most important factors for the choice of governing law.

¹ Below, paras 100-102.

² See further A. Sinclair "Using the UNIDROIT principles of international commercial contracts in international arbitration", [2003] Int ALR Issue 3.

³ Some practitioners noted however that incorporating the PICC into a contract is different from appointing it as the governing law. If incorporated into a contract, it is, in effect, a set of standard terms which is still subject to a national law that governs the contract.

⁴ The Society has published a report including these results. See Law Society Report - Firms' Cross-Border Work - December 2010. This report also included the results of two on-line questionnaires that the Society conducted (targeting in-house legal departments and law firms and which also included input from firms focussing on domestic work) between October and November 2010, in which familiarity and legal certainty were again the most important factors.

2. FURTHER STUDY AND IMPACT ASSESSMENT

31. The Society believes that a thorough empirical study should be undertaken to identify current barriers to cross-border trade. We are not aware of a comprehensive study (at least from a business-to-business perspective) ascertaining whether there really is a need for a change to the current system of governing laws.
32. If the choice of governing law were to be identified as a significant barrier, then a thorough impact assessment should be undertaken (including a cost/benefit analysis) on whether and how it would be beneficial to address this problem. Any impact assessment should be broad and include Option 1 (“publication of the results of the Expert Group”) and Option 2 (“an official “toolbox” for the legislator”) from the Green Paper, rather than only Option 4 (“Regulation setting up an optional instrument of European Contract Law”). It would also be helpful for the Commission to consider in greater depth the possible ceilings on the amount of cross-border commerce that is possible for SMEs and e-commerce to achieve.⁵ Other solutions for increasing cross-border trade should also be considered.⁶ These would include increasing redress and enforcement mechanisms for consumers and businesses and the possibility of revising Rome I.
33. We understand that the Expert Group has already been instructed to try to draft an “optional instrument” and, due to this, we consider that a full impact assessment should be undertaken as soon as possible. Indeed, the work required for an impact assessment is vital in order to establish that the EU has power to legislate for an “optional instrument”.
34. In the Green Paper, the Commission appears to use the justifications put forward to support the Consumer Rights Directive of “simplifying and consolidating the existing legislation in the area of consumer contract law” as justification also for an instrument of European contract law. The impact assessment from that proposal cannot be used to try to justify an “optional instrument”. As a general point, we understand that much of it has been challenged and subsequently rejected by policymakers. In addition, there has been no in-depth study of the differing requirements of business-to-business and business-to-consumer agreements and no analysis of the cost of introducing an “optional instrument”.

3. CHALLENGES FOR THE INTERNAL MARKET

35. In general, practitioners consider that neither a buyer nor a seller would want to enter into a cross-border agreement unless he or she either felt confident that he or she would be able to secure practical redress or he or she did not care about the consequences if things went wrong. Many sellers might also not want to supply their products or services in a jurisdiction with which they were not comfortable. We have not seen any evidence that demonstrates that the choice of governing law in a contract is key to increasing the confidence of buyers and sellers in cross-border transactions. The terms of a contract are, of course, important but there does not appear to be any evidence that these determine whether a person will offer or agree to commit themselves to a cross-border agreement.

⁵ E.g. Due to the nature or location of some businesses, they are unable or unlikely to trade cross-border.

⁶ Practitioners have also noted that other practical initiatives that would be of assistance could include increasing the availability of explanatory material and copies of relevant national instruments and existing standard forms of agreement in use.

3.1. Business-to-consumer contracts

36. At consumer level, practitioners felt that most consumers were largely unaware of the contents even of their own national contract law. In relation to small value transactions, consumers do not normally litigate if there is a dispute. Either they resolve the dispute with the supplier without regard to the law (and often the supplier will rectify the problem to preserve goodwill); or they will not attempt to seek redress given the low value of the transaction. With higher value transactions, contracting parties take advice either beforehand (e.g. for house purchases) or after a problem has arisen (e.g. with defective building works). Given that a lack of knowledge of national contract law does not seem to be a deterrent to domestic contracts such as those above, it is hard to see that the law of another state is a significant deterrent for entering into smaller value transactions. As an example, people travel abroad and enter into contracts (e.g. hotels, car hire, purchases) without knowledge of the governing contract law of their destination.
37. Where low-cost redress systems, such as ombudsmen, industry funded arbitration or mediation are available, these provide a valuable resource for consumers with low-value claims. Many practitioners believe that an extension of such systems providing consumers with practical means of redress would benefit consumers and could lead to greater confidence in entering into cross-border contracts.^{7 8} Practitioners believe that, rather than the diversity of Member State legal systems (including contract laws), the impediments to cross-border trade between Member States at the consumer level are much more likely to be due to other factors, such as:
- The ability of parties to secure practical redress (e.g. a refund or adequate compensation) should anything go wrong in the course of the contract;⁹

⁷ Practitioners believe that the court process in nearly all Member States is inefficient to protect consumers' rights for relatively small claims (notwithstanding the introduction of the Regulation establishing a European small claims procedure (861/2007)). Some practitioners have suggested that it would be useful to consider effective procedures to settle consumers' complaints outside the court system. A template might be the Telecoms Ombudsman system in the UK, which requires all telephone network operators and service providers in the UK to have a neutral, privately run, dispute settlement procedure to deal with consumer complaints. Bodies providing this service to telecoms users include the Office of the Telecommunications Ombudsman (Otelo) and the Communication and Internet Services Adjudication Scheme (CISAS). Another example is the service for the resolution of complaints involving consumers provided by the Financial Ombudsman Service in the UK.

⁸ It has also been commented that there already appears to be the start of a potentially effective framework of consumer protection enforcement in place in Member States. This includes the Regulation on consumer protection co-operation (2006/2004), which sets out a framework of co-operation on cross-border enforcement, and the European Consumer Centre Network, which helps consumers who have a cross-border complaint or dispute and wish to pursue redress. In the UK, consumers also benefit from Section 75 of the Consumer Credit Act 1974 (as amended). This provides consumers who purchase relatively expensive goods and services with a range of protection including from fraud or problems in transit. Practitioners felt that initiatives such as these gave consumers greater comfort in entering into contracts.

⁹ It was also noted that more could be achieved in terms of enforcement and redress if greater resources could be made available for the operation of domestic enforcement agencies. In the UK, domestic enforcement agencies (Trading Standards) were felt by some practitioners to be fragmented and under-funded. They were given more

- Differences in VAT rates and difficulties for the seller, especially the SME seller, in charging and collecting VAT;
- Intellectual property rights and distribution agreements (which may have territorial restrictions);
- Concerns of both consumers and SME sellers regarding payment (e.g. whether there is to be cash on delivery or payment in advance);
- Language differences, cultural attitudes and habits;
- Shipment costs, particularly for long distances or where sea or air transport is required;
- Differences in advertising legislation, which cause sellers to hesitate before marketing in other Member States;
- Protection of personal data and compliance with information security standards, including the PCI Data Security Standard (for card transactions), and perhaps fear of a greater exposure to fraud; and
- Other impediments, such as regulatory compliance and differing national standards (labelling, packaging and technical standards).¹⁰

Operation of cross-border commerce

38. For larger contracts which may well be individually negotiated, the issues listed above can be agreed between the parties so that the risks are allocated to each party according to which party is best capable of dealing with the risk. In the case of standard terms, however, the seller or provider of services must make up his/her own mind on the matter by balancing all the concomitant risks. Some practitioners commented that it was not surprising, therefore, that so many businesses offering goods or services for sale want to restrict the territory into which they sell. These practitioners were of the view that the choice of law is of lesser importance in the making of this decision than many of the above criteria. Practitioners also commented that it is unlikely that businesses of any size should want to offer goods or services for sale unless they are properly able to discharge their obligations wherever those obligations must be discharged or litigated.
39. Whilst many SMEs and larger companies want to trade cross-border, this will depend on the characteristics of the individual business. (For example, a window-cleaner or handyman might not want to operate cross-border, whilst a larger business might have particular operational or intellectual property reasons for wishing to concentrate in one Member State.) Whilst the internet may open up the whole of the EU to an entrepreneur, depending on the type of the goods and services to be offered, it may be sensible for many businesses to make the offering to a part only of the EU where they can operate without risking a breach of their obligations or applicable local regulations. Undertakings may be able to service EU-wide offerings with safety both for themselves and for their customers because they anticipate that the business to be generated in a territory will be great enough to justify full investigation of local conditions and they have the

flexible enforcement tools through the Regulatory Enforcement and Sanctions Act 2008 and this approach might be worth developing further.

¹⁰ See further page 50, The Economist 28 October 2010, "Europe's need for e-reform: Internet commerce reveals the limits of Europe's single market. Freeing it up will bring growth and social benefits", "Charlemagne" Column.

resources to make those investigations and to keep their knowledge of those conditions up to date.¹¹

40. A business which proposes to trade across various territories using a standard document will usually adopt terms which accommodate the particular local requirements, but the consumer will enjoy those rights, enforceable locally, in any event.^{12 13}

E-commerce/on-line transactions

41. We disagree with the view that the reason that there is less cross-border than domestic on-line trade is due to a divergence of the national laws of contract.¹⁴ It is commendable that the Commission should wish to promote cross-border on-line trade. However we suggest that there are more practical reasons which influence why consumers buy on-line from their own state.
42. In March 2009, the Commission published an in-depth analysis of cross-border e-commerce within the internal market.¹⁵ The study listed a range of barriers including: “languages, demographics, individual preferences, technical specifications or standards, internet penetration or the efficiency of the postal or payment system.” A range of practical issues were identified, as set out in the Executive Summary of the report, including the “inability of consumers to access commercial offers”, “lack of information on cross-border offers” and regulatory barriers (which may result in “significant compliance costs for business”) in the domains of consumer law, VAT, “the territorial management of copyright”, or “the national transposition of the European legislation on electronic waste disposal”. There was also a need “to promote on-line trust by strengthening on-line and cross-border enforcement, putting in place efficient and speedy dispute resolution, and by enhanced market monitoring, information and awareness raising.”
43. This was followed by a Commission Communication, which stated that “the main regulatory barriers to cross-border e-commerce originate in the fragmentation of consumer protection rules and other rules on VAT, recycling fees and levies.”¹⁶ The Communication identified key focus points for tackling regulatory barriers to e-commerce. These were to:
- “Address the fragmentation of consumer protection rules”;

¹¹ Many larger undertakings will set up permanent branches in each of the territories where they expect to make a large number of sales. For those smaller undertaking which do not have these resources of skill and money, some of the risk (and margin) of selling into other territories can be reduced by the appointment of agents or distributors.

¹² Below, paras 100-102.

¹³ In the case of on-line transactions, specialist practitioners noted that a business which supplies consumers in multiple jurisdictions, especially via the internet, will, in their experience, usually wish to adopt a single set of standard terms. A supplier usually follows this approach, regardless of where its purchasers are situated. Standard form contracts are also often used in business-to-business agreements, for example concerning the sale of goods.

¹⁴ See Section 3.1 of the Green Paper.

¹⁵ See “Commission staff working document: report on cross-border e-commerce in the EU” (SEC(2009) 283, 5.3.2009).

¹⁶ See “Communication from the Commission on Cross-Border Business to Consumer e-Commerce in the EU” (COM(2009) 557, 22.10.2009).

- “Ensure effective enforcement of Article 20 of the Services Directive” (2006/123);
 - “Increase the efficiency of cross-border enforcement”;
 - “Tackle unfair commercial practices”;
 - “Promote alternative dispute resolution schemes and the cross-border small claims procedure”;
 - “Simplify the VAT reporting obligations of distance sellers”;
 - “Reduce on-line businesses’ administrative burden concerning waste of electrical and electronic equipment”;
 - Find “[p]ractical solutions to the management of copyright levies”;
 - “In the context of vertical restraints, contribute to reducing barriers to on-line sales”; and
 - Assist with “[i]mproving payment systems and logistics and tackling technological barriers”.
44. Nowhere did the Commission identify the diversity of national laws of contract as a significant factor impeding cross-border e-commerce. In its Communication, the Commission observed that “[t]he effect of fragmented consumer protection rules on contracts, in conjunction with rules on the conflict of laws, is to generate significant extra compliance costs for traders wishing to sell in several Member States. The proposal for a Consumer Rights Directive will address this main obstacle to the creation of a retail internal market.”
45. Since this time, it became clear that full harmonisation under Consumer Rights Directive would not be possible to achieve without lowering consumer protection in some Member States. It is not clear that a system of “targeted harmonisation” (as is now proposed) could deliver the same benefits to the internal market as were envisaged from a system of full harmonisation. Subsequently, it has been argued in forums such as the European Parliament that a failure to achieve full harmonisation under the Consumer Rights Directive could be a justification for an “optional instrument”. However, unless an “optional instrument” provided for the full harmonisation of consumer protection rules, nothing would be gained. In view of the failure to secure this in the Consumer Rights Directive, there is no reason to believe that it could be achieved by an “optional instrument”. Practitioners were therefore sceptical as to whether this would increase cross-border e-commerce.
46. In its recent “Consultation on the future of electronic commerce in the internal market and the implementation of the Directive of electronic commerce (2000/31)”, which closed on 5 November 2010, DG Internal Market and Services stated that “[t]he European Commission wishes to study in detail the various reasons for the limited takeoff of electronic commerce”. Categories of particular interest for which the Commission wished to receive feedback from interested parties included “contractual restrictions on cross-border on-line sales” and the “resolution of on-line disputes”. The Society believes that the results of this consultation should first be processed before any policy decisions are made in regard to whether an “optional instrument” would assist in facilitating cross-border on-line transactions.
47. Rather than the detail of the contract terms on-line, practitioners commented that greater importance in a cross-border transaction (for both the buyer and a seller) is likely to be attached to the identity of the other party, their reputation, the reputation of what they have to sell or provide, the brand image and in which territory they are based.

3.2. Business-to-business contracts

48. Some in-house practitioners have commented that having a diversity of contract law systems in Member States does cause some problems for businesses because they need to be aware of the different systems when operating in each Member State which necessitates taking legal advice and the cost attached to this. However, the majority of practitioners we have spoken to (both in-house and in private practice) are not convinced that a European contract law instrument is necessary. Key in-house practitioner concerns are set out below.
- Any new legal instrument of contract law is likely to be interpreted differently in Member States and so within a short period of time, national differences will again appear;
 - In the case of business-to-business contracts (including SMEs), some in-house practitioners believe that the key barrier to entry was the different court processes and procedures in nearly all Member States.¹⁷ There are also concerns regarding the cross-border enforcement of judgments and debt recovery;
 - As regards legal disputes, the law of tort (for example, in regard to negligence and duty of care) is as important as contract law;
 - Even when the EU has sought to centralise legislation in fields such as public sector procurement and data protection, this has resulted in different applications at Member State level;
 - Contract law is one element of the law applicable to business. Others include: corporate law, tort law, intellectual property law, employment law, tax law, accounting standards and financial regulation;
49. The choice of law is usually resolved in favour of the law of the jurisdiction in which the party with greater negotiating power has its seat.¹⁸ In cases where negotiating power is more balanced, the governing law is usually agreed quickly in a negotiation, although in some cases, the parties reach somewhat more sophisticated arrangements as regards law and jurisdiction.
50. The view that a European contract law would have a business-to-business benefit (particularly for SMEs) is not fully explained in the Green Paper. If there is a concern that SMEs may be forced into adopting the choice of law favoured by large businesses then this would presumably also apply to an optional 28th regime. In the case of specialised contracts with a large international dimension, businesses are familiar with the laws that apply. The Commission gives the example of shipping contracts. To this can be added international finance and many commercial agreements where the risks are well understood. Similarly, most European construction contracts of a cross-border nature are based upon internationally recognised standard forms of contract which operate to all intents and purposes as self-contained contract law systems themselves in conjunction with local law rules relating to property law, tort law, quasi contract law, administrative law, environmental law and health and safety matters.¹⁹ In such a context, the introduction of an

¹⁷ E.g. Businesses may be suspicious that those courts are slow, inefficient and, more importantly, biased against the overseas seller. They may lack familiarity with local court procedures, have no knowledge of local legal practitioners and be concerned about operating in a different language.

¹⁸ In the case of construction projects, the law of the jurisdiction in which the property in question is situated may be used.

¹⁹ E.g. the FIDIC (Federation International des Ingénieurs – Conseils) suite of contracts.

“optional instrument” of contract law, which would itself interface not only with the chosen form of contract but also relevant aspects of the local or other law, would surely serve to complicate matters and therefore increase costs.^{20 21}

SMEs

51. Practitioners advising SMEs, some of whom are involved in cross-border work, have not experienced clients calling for a pan-European contract law. Typically, their experience has been that clients want to use a standard form English law contract for their business with counterparts in other Member States. A practitioner is able to review this and advise on appropriate amendments.
52. If the contract was of a high-value or long-term duration, the practitioner would normally suggest that this was given a high-level review by lawyers in the Member State of the other party. This would be to highlight any particular issues which might arise under the law of that Member State, including any inconsistent or unenforceable provisions in the contract. In the experience of practitioners, there are seldom material differences in basic contract law as between Member States.²² Hence, generally only minor changes need to be made to contracts and the cost is relatively low. They did not believe that the current system posed a significant barrier to trade.
53. It has also been argued that in the case of two SMEs of equivalent bargaining power in different member states negotiating, they would want a “neutral” governing law. The Society’s view is that, in this case, SMEs would want to choose a law with jurisprudence and which had previously been tested - an obvious “neutral law” might therefore be Swiss law.

General comments

Value of the England and Wales common law system

54. Some surveys have sought to give an insight into the usage of various national laws. In the Oxford Institute of European and Comparative Law and the Oxford Centre for Socio-Legal-Studies carried out a survey of 100 European businesses. This found that 59% of respondents considered that English law is the most used in cross-border transactions.²³ Another, recent survey carried out by Queen Mary College, University of London entitled “International Arbitration Survey: Choices in International Arbitration” found that 40% of respondents use English law,

²⁰ In the context of specialised contracts in which standard governing laws or standard form contracts are routinely used, it is arguable that it is only in relation to small value contracts, where the parties are of equal bargaining power, that any new governing law might be chosen.

²¹ Below, para 118 onwards. See concerns regarding certainty.

²² On a more general level, academics also draw attention to the similarities between civil and common law systems: “Despite very different legal cultures, processes, and institutions, common law and civil law have displayed a remarkable convergence in their treatment of most legal issues.” See “Civil Law and Common Law: Two Different Paths Leading to the Same Goal” by Caslav Pejovic, Associate Professor of Private International Law, Kyushu University.

²³ See page 16, Oxford Institute of European and Comparative Law and the Oxford Centre for Socio-Legal-Studies report “Civil Justice Systems in Europe: Implications for Choice of Forum and Choice of Contract Law” (2008).

followed by 17% who use New York law, 8% who use Swiss law and 6% who use French law.²⁴ As regards choice of court, statistics indicate that approximately three quarters of claims brought to the Commercial Court involve overseas parties and, in approximately half of these cases, there is no link to the UK besides the selection of London as the dispute resolution centre.²⁵

55. English law and New York law are regarded as the market-standard governing laws for major international financial contracts. Practitioners believe that this is in large part due to the certainty afforded by the contract laws of these jurisdictions (i.e. the contract will normally be enforced in accordance with its terms). Practitioners are concerned that any weakening of the contractual certainty that can be achieved under English law would be likely to result in contracting parties switching to another non-EU common law system (e.g. New York law) with the consequent loss of economic activity and export earnings for the EU as a whole. In developing Asian economies, we understand that systems of common law are regularly used as the governing laws in transactions. In the Law Society Report on Firms' Cross-Border Work (December 2010), more than one third of private practice firms in England and Wales carried out work in the UK on behalf of overseas clients in the past year. The biggest average contributions to the gross fee income of those firms was generated through their work in the EU and Asia.²⁶
56. The City Business Series Report on Legal Services in 2007 valued the contribution of legal services to the UK economy at £14.9bn in 2004. The net exports of UK legal services were valued at £1,776m in 2005.²⁷ The legal services sector in England and Wales also employs a large number of people. As at 31 July 2009, there were 145,381 solicitors on the Roll of Solicitors in England and Wales. The same survey stated that 115,475 of these held a current practising certificate at that time entitling them to act as a solicitor within the definition of the Solicitors Act 1974 or alternative figures from 31 December 2009 stated that 112,589 held a current practising certificate.²⁸ In addition, many further staff are employed in supporting roles or trainee solicitor positions within firms.

Value in diversity of Member State legal systems

57. Practitioners of commercial and contract law are not convinced that the divergence between Member State laws acts as a significant barrier to intra-community trade. An alternative view is that the option of using different laws fosters competition between different legal systems to be the most attractive to contracting parties.

²⁴ See Chart 11, Queen Mary College, School of International Arbitration, sponsored by White & Case on "2010 International Arbitration Survey: Choices in International Arbitration".

²⁵ See page 7, Report by The City UK on "Dispute Resolution in London and the UK 2010".

²⁶ Above, footnote 4. The figures cited can be found in the Law Society Report on Firms' Cross-Border Work (December 2010) and were originally collated as part of the Law Society Firms Omnibus Survey (November 2010).

²⁷ See pages 1 and 11, Legal Services report of the City Business Series by International Financial Services London (February 2007).

²⁸ See Sections 1.2 to 1.3, Trends in the Solicitors' Profession – Annual Statistical Report 2009 (Law Society of England and Wales). Please note that we understand that the Solicitors' Regulatory Authority put the figure of practising certificate holders on 31 December 2009 at 112,589 and that these figures change slightly on a regular basis.

58. Practitioners also noted that national difference should be valued, especially where some national systems have found respect far beyond their home countries and are income producing assets for the EU. As discussed above, the Oxford Institute carried out a survey of 100 European businesses. This found that 23% of respondents favoured English law, 19% Swiss law, 14% German law and 9% French law.^{29 30} Both the Oxford Institute and Queen Mary studies suggest that businesses may favour different national systems for different reasons and support the idea that certain national systems are income producing assets.³¹

Diversity of legal systems within UK

59. England and Wales have been in the UK with Scotland since 1707. There is no real suggestion that differences between English and Scottish contract laws have been a barrier to trade between these countries. Most of the difficulties relate to differences in the law relating to real or personal property, which have much more significant differences. They often arise in a contractual context, but can be distinguished.

Features of the England and Wales common law system

60. Some practitioners thought it would be helpful to provide a brief summary of the key features, from a practitioner-perspective, of the England and Wales common law system:

- In business-to-business, business-to-consumer or consumer-to-consumer contracts, the starting point is that the parties have broad freedom to agree what they like. Such freedom of contract means, in practice, that the parties write down (or say) what they have agreed and show that they intend that agreement to be legally binding.
- If the contract needs additional terms which the parties have not explicitly agreed, in order to make it work, the court will come to their aid and imply these – for example, in an agreement of indefinite duration, that the parties intended that it can be brought to an end on reasonable notice. Similarly, statute may imply some terms e.g. implied terms as to warranty, as to fitness for purpose, etc.³² The parties are however free to agree something different.
- The courts will refuse to enforce contracts which are against public policy and the public interest, such as contracts in restraint of trade. Further, statute may also forbid certain terms as oppressive, for example, under the Consumer Credit Act 1974. There are also established harmonisation measures, such as the domestic regulations and the Directive from which they derive which have targeted effects beneficial to consumers while not impinging on business-to-business freedoms, such as the Unfair Terms in Consumer Contracts Regulations (1999).

²⁹ Above, footnote 23. See page 14.

³⁰ See also para 54.

³¹ Swiss law is the civil law system most commonly chosen in international contracts. Some practitioners commented that it has the advantage of a developed and well-understood jurisprudence and Switzerland offers good dispute resolution services, both in courts and arbitration. They expressed the view that Swiss law might also be a more attractive and already available option than an “optional instrument” of European contract law.

³² E.g. the “fitness for purpose” provisions as contained in the Sale of Goods Act 1979, the Supply of Goods and Services Act 1982 and the Sale and Supply of Goods to Consumer Regulations 2002.

- Importantly, in order to give certainty as to how agreed terms in a contract will be enforced, the courts regard themselves as bound by previous decisions of the courts and, in particular, are bound by the decisions of higher courts as to matters of law, the Court of Appeal and, in turn, the Supreme Court (formerly the House of Lords). This adds certainty to what the law means and businesses can, with greater confidence, rely on it to form the basis of their dealings with each other and with their customers.
- The common law contractual and commercial system is given effect and driven by the courts and their users litigating against other parties; the common law is not driven by the State or by statute. The courts have judges who have practised for thirty years or so as lawyers, before being appointed as judges. They are independent of the State. The courts will continually adapt to social thinking over time and the recent decision of the Supreme Court that prenuptial agreements should be enforceable in England and Wales is a good example of the courts' continued shifting of the law as social attitudes change.

How can any problems be quantified, and who is affected by them?

61. The Green Paper refers to the survey in Special Eurobarometer 292 (2008) to argue that citizens would like a harmonised European law.³³ Practitioners have commented however that the question seems unduly simplistic. Respondents were asked, when signing a contract with an individual or business based in another Member State, whether a party would prefer a contract to be based on the other party's national law, the national law of their Member State or on harmonised European law. If the question had been phrased differently, the answer might have been different. The question also ignored the importance of certainty of outcome, familiarity with a particular system and freedom of contract, all of which are important for commercial parties.³⁴
62. The Green Paper also refers to a study sponsored by Clifford Chance in 2005 of 175 companies, which showed support for an "optional instrument" in principle³⁵ and hinted that different national legal systems might pose some level of barrier to internal market trade.³⁶ The conclusion from the Clifford Chance Survey was that "business wants the European Commission to continue its deliberations on an "optional instrument". Business in the EU is very interested in a neutral, EU

³³ See Section 3.1, Special Eurobarometer 292 (2008), Civil Justice in the European Union.

³⁴ E.g. in the UK there are standard forms of construction contract which have been developed to represent a reasonable balance between the purchaser and supplier of services. The law of contract of England and Wales has informed their development in terms of principle and provides clarification regarding their application. If an optional instrument became applicable to such contracts, it could generate uncertainty as to their application and there would be a risk of further uncertainties regarding the application of mandatory UK legislation in the field of construction contracts, such as Part II of the Housing Grants, Construction and Regeneration Act 1996.

³⁵ See Table A13 which states that 83% of the businesses surveyed favoured the concept of a harmonised European contract law in "The Clifford Chance Survey, European Contract Law, April 2005."

³⁶ See Table 2, *Ibid.* Respondents who believed that obstacles to cross-border trade were present in the internal market were asked to rate the factors that impacted upon their ability to conduct cross-border transactions. From the outcome, the survey concluded that "it is clear that the cost of obtaining foreign legal advice and differences between legal systems are factors that affect cross-border trade, even if they score only marginally higher than differences in the implementation of EU law between member states."

contract law, and would be likely to use it. But this does, of course, depend upon it being a good law that enables trade and gives business the predictability it needs." The survey also asked businesses "how important do you feel the following factors are in developing good contract law?" Fairness received the highest score, followed by a preference for predictability.³⁷

63. However, the Society is concerned that views may be significantly affected by the precise question posed. As explained above, it appears that much depends on how a question is framed. In the research that the Society has recently conducted, both in-house legal departments and private practice firms indicated that legal certainty and familiarity with the legal system of contracting parties were the most important factors for the choice of governing law, rather than the attractiveness of the legal principles within a particular legal system.³⁸ There appears little hard evidence to show that differences in national legal systems significantly affect cross-border trade in the internal market. As with the Clifford Chance Survey, asking respondents whether they would favour an optional European contract law presumes that they are aware of, and have thought through, the implications. In 2005, it was even less clear than today what the substance of the law would be and it would therefore have been difficult for businesses to envisage whether there could, for example, be financial or reputational implications from selecting a new instrument as a governing law in contracts. When answering the questions, there was no consequence whereas, in reality, this might not be the case.
64. According to Flash Eurobarometer 278 (2009), about 71% of retailers surveyed currently refrain from cross-border transactions with consumers and, even if the laws regulating such transactions were completely harmonised, 58% of retailers would still not want to sell to consumers in other Member States.³⁹ This limited benefit in the response is on the basis that harmonisation of the entire law regulating cross-border trade would take place, and therefore such harmonisation would have to include not only contract law but also other areas such as tax law, tort law, product safety and liability law as well as other product requirement regulations. This makes it impossible to attribute the results predicting an increase in cross-border trade to any one element (such as harmonisation of contract law).
65. The existing surveys on consumer behaviour (see in particular Flash Eurobarometer 128 (2002)) do not appear to support the need for contract law harmonisation because the polls showed that more than 50% of consumers already have the same or even greater confidence in cross-border transactions than in domestic transactions while only 26% have less trust in cross-border transactions.⁴⁰ For these 26% of less confident consumers, the survey noted that "[t]he answers reveal that the top reasons for consumers' lack of confidence are difficulties to resolve after sales problems and to take legal action through the courts".⁴¹

³⁷ See Tables A29 and A30, *Ibid*.

³⁸ Above, footnote 6.

³⁹ See Section 2.3, Flash Eurobarometer 278 (2009), "Business attitudes towards enforcement and redress in the internal market".

⁴⁰ See Section I.1.6, Flash Eurobarometer 128 (2002), "Public opinion in Europe: Views on business-to-consumer cross-border trade".

⁴¹ *Ibid*, Section II.1.1.

4. CHOOSING THE BEST INSTRUMENT FOR EUROPEAN CONTRACT LAW

4.1. What should be the legal nature of the instrument of European Contract Law?

Difficulty of not knowing content/substance of reform

66. It seems to us difficult, if not impossible, to decide which of the Commission's proposals to support while the substance of the contract law is still unknown. Nevertheless, practitioners have commented on the seven options to the extent they are able without further information.

Option 1: Publication of the results of the Expert Group

67. Publication of the final outcome of the work of the Expert Group should take place in any event. There is no justification for keeping it confidential.⁴² The issue is, therefore, whether publication is all that should be done with the outcome of that work. In our view, publication alone is a viable option. As the Commission points out, the Expert Group's work could be used by European and national legislators as a source of inspiration and for academic purposes.⁴³ Publication alone would leave it to the legal "market place" to assess what benefit can be derived from the Expert Group's work, whether in the manner suggested by the Commission or otherwise. The Expert Group's work would therefore stand or fall on its own merits rather than being imposed regardless of those merits.

68. The Society was disappointed to note that the Commission Work Programme for 2011, published on 27 October 2010 prior to the close of the consultation, already states that "[a]s part of its efforts at strengthening citizens' rights in 2011, the Commission will propose a legal instrument on European Contract Law."

Option 2: An official "toolbox" for the legislator

69. There is some confusion on the meaning of a "toolbox". The Society believes that a set of non-binding rules and guidelines could enable legislators, businesses and practitioners to identify useful wording for principles, duties and obligations, leaving behind wording in the DCFR that would not function effectively. As stated above, the "toolbox" has previously been described as a "guide or *vade mecum* for use by European legislators to improve the quality, coherence and consistency of European legislation"⁴⁴ and been supported by the Member States.

70. We doubt that the work product of the Expert Group will be capable of acting as a "toolbox" because it is likely to offer a single solution to each issue that arises in contract law.⁴⁵ A "toolbox"

⁴² Short summaries of the meetings of the Expert Group and the stakeholder forum are available on-line at http://ec.europa.eu/justice/policies/consumer/policies_consumer_intro_en.htm.

⁴³ Practitioners commented that the comparative commentary which accompanies the DCFR is a useful starting point for a comparative law discussion and is therefore valuable.

⁴⁴ See Lord Bach (Question 73), House of Lords Report on "European Contract Law: the Draft Common Frame of Reference".

⁴⁵ We assume that the work product will appear similar to the relevant sections of the DCFR.

normally presupposes a range of tools. The EU institutions and all others involved in the legislative process will wish to consider whether the single solution proposed by the Expert Group is the one that they should adopt in any relevant piece of legislation, but responsible legislators will also wish to consider what other possible solutions there might be and whether any of those are more appropriate. As Professor Monti explained, in drafting the Consumer Rights Directive, the Commission used the DCFR as a source of inspiration, using its proposals in areas such as withdrawal periods. The Commission deviated from the DCFR where it felt that another approach was more appropriate given the results of the impact assessment.⁴⁶

71. We are sceptical as to the utility of either of the two sub-options proposed. A Commission act on a “toolbox” could reinforce the lack of political legitimacy by not requiring the agreement of the Parliament and Council. An inter-institutional agreement could be viewed as having greater political legitimacy but could constrain all three institutions to follow the “toolbox”, as it is described in the Green Paper. This option also presupposes that there will have been full and informed debate and wider involvement of interested parties in the elaboration of the text. Because of what has happened in the past, we have concerns that any future debates should make sure that experts from all Member States and key legal traditions are involved.⁴⁷
72. Since the Expert Group's work cannot be the only solution considered by the legislator, there seems little to be gained either by the Commission committing to take that work into account or by expending time and effort on securing an inter-institutional agreement to that effect. That said, in principle a “toolbox” is the Society's preferred solution and it believes that consideration should be given to whether the work of the Expert Group could be developed into a form to contribute to a “toolbox” to assist EU legislators.

Option 3: Commission recommendation on European Contract Law

73. Again, the Green Paper offers two sub-options: a Commission recommendation to replace Member States' national laws, along the lines of the UCC; or encouragement from the Commission to Member States to incorporate the European contract law as an optional regime in their national laws. We are sceptical as to the utility of either of these sub-options.
74. Any Member State is currently free to incorporate into its domestic law the DCFR, the PICC, PECL or any other draft contract code produced by a national or transnational group (including the Expert Group), whether in addition to or as a replacement for its current national law. We doubt whether a recommendation or otherwise from the Commission will have any, certainly any significant, impact in this regard. A decision by an individual Member State to replace or supplement its national law raises issues extending beyond the internal market concerns in the Green Paper.

UCC

75. The Green Paper refers to the UCC, which is widely used in the US. There are significant differences in the political landscape and in the legal underpinnings of the US' federal system and the EU, which render any comparison of limited value. Nevertheless, the success of the UCC over

⁴⁶ See discussion of Consumer Rights Directive, Legal Affairs Committee of the European Parliament, 2 September 2010.

⁴⁷ The Legal Affairs Committee of the European Parliament conducted a “Workshop on European Contract Law” (29 April 2010) and a “Workshop on an optional instrument for EU contract law” (27 October 2010). These did not include a common law expert on the substance of a European contract law / optional instrument.

its near 60-year history may offer some guidance to the EU, especially with regard to the manner of preparation of a law that aspires to be adopted across existing legal borders. In particular, the UCC:

- is drafted by a group of academics, judges, State legislators and active practitioners, with representation from every State;
 - has been drafted through an open and deliberative process which, though time-consuming, has ensured its wide acceptance;
 - has no independent legal import, only attaining force of law upon adoption by individual State legislatures - contract law is a State matter not a federal matter;
 - is subject, in the form adopted by each State, to the sovereign interpretation of the judiciaries of each such individual State;
 - cannot be chosen by private parties to apply to contracts or transactions (parties rather choose which State's law to apply);
 - distinguishes between consumer contracts and other contracts;
 - does not altogether replace the common law of contract otherwise applicable nor supersede State law; and
 - has evolved and become more uniformly accepted over time, as individual State legislatures have adopted more and more of the uniform provisions. It is a dynamic system of contract law.
76. Accordingly, the UCC is not necessarily exactly the same in each adopting State. As such, it is hard to see how this model would achieve the Commission's internal market aims, especially given the difficulties caused by Article 6(2) of Rome I.⁴⁸
77. The UCC has been overwhelmingly the most successful harmonising code produced by the Uniform Law Commissioners and the American Law Institute. Despite that, approximately half of the Commissioners' proposals have not been adopted by any US State, and even those that have enjoyed a measure of success have still commonly fallen well short of adoption by even half of the US States.
78. The UCC's success has, nevertheless, been exceptional, and results from the UCC's own intrinsic merit. That merit derives in the main from the open and collaborative, albeit time-consuming, method of its preparation, coupled with the resulting merits of the UCC. This method of preparation is in marked contrast to the manner of preparation of the DCFR and to the work of the Expert Group. These have involved mainly academics, with little involvement from practitioners with experience of how contract law operates in practice. The Commission secured some practitioner input at an early stage in the preparation of the DCFR through the group of "stakeholder experts" it assembled. Those drafting the DCFR were obliged to consult with these stakeholder experts and were originally intended to provide detailed comments on the observations made by the stakeholder experts. This practitioner involvement did, however, not continue for long, leaving those contracted to produce the DCFR to work on their own. The Expert Group now has, we understand, a relatively small stakeholder forum, but this cannot be a

⁴⁸ Below, para 100-102.

substitute for a wide and open practitioner involvement in all aspects of the policy and drafting of the putative code and a full consultation on its terms.

79. Practitioners are doubtful whether a document prepared in a largely closed manner has any real possibility of winning practical acceptance across numerous countries with different legal traditions. As we have said, there are many possible solutions to any particular problem in contract law, not merely one objectively "right" answer. Contract law raises social, political, economic and other issues, and it is therefore necessary to debate widely what the solution to any particular problem should be – and the answer to that particular problem will also be influenced by the way in which other problems are to be dealt with. Different Member States' laws can often reach a similar approach. That debate must involve not only academics and legislators, but also businesses, economists, practitioners, and consumer representatives in order to ensure that any work product is not only theoretically impeccable but is also practically workable. Without that wide involvement, no European contract law can, or should, win wide acceptance.
80. That is why the more cautious approach of using a non-binding "toolbox" to try to overcome problems legislating to achieve harmonisation in different legal systems is more appropriate. This would enable the Community to better understand the differences and to be sensitive to them, while seeking to achieve common goals.

Option 4: Regulation setting up an optional instrument of European Contract Law

81. The Society does not support this option. If there is to be an instrument, an optional one is obviously less objectionable than a mandatory one but providing an alternative law with no cultural heritage or clear meaning is considered by the majority of practitioners to be undesirable. There are a number of serious areas of concern in relation to an "optional instrument".

Legal basis

The Society is grateful for the contributions of the Financial Markets Law Committee and individual practitioners.

82. As stated above, the work required for an impact assessment is vital in order to establish that the EU has power to legislate for an "optional instrument". The Commission conspicuously fails to address in the Green Paper the legal basis of any of its proposals. The Commission must establish a clear justification for any proposal it makes, demonstrating that different contract laws do genuinely obstruct the proper functioning of the internal market, and that any obstructions apparently caused by different contract laws are not in fact due to other causes. There is uncertainty as to which legal basis in the Treaties it could use. This poses clear problems. As Martin Hesselink has commented:⁴⁹
83. *"Another source of possible legal uncertainty, temporary but nevertheless potentially devastating, is the legal basis for an optional instrument. The Green Paper does not address the issue at all but if the instrument that will be adopted is in fact ultra vires, or if there is uncertainty as to its legality, then until the issue is finally resolved this will remain an important source of legal uncertainty. In practical terms, two possible challenges can be awaited. First, challenges*

⁴⁹ See Prof. Dr. Martijn Hesselink from the Centre for the Study of European Contract Law (University of Amsterdam) "An optional instrument on EU contract law: could it increase legal certainty and foster cross-border trade?" <http://www.europarl.europa.eu/webnp/cms/lang/en/pid/1483>. (Presented at the "Workshop on an optional instrument for EU contract law" in the Legal Affairs Committee of the European Parliament on 27 October 2010.)

submitted to the CJEU via motions for preliminary rulings. Secondly, ultra vires challenges in certain national constitutional courts.”

84. Some initial thoughts on the principal possible sources of constitutional power are below.

Article 114 TFEU

85. Article 114 provides for measures to be adopted “for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market”.⁵⁰ While it is clear that, were a mandatory instrument to be adopted, this would have the effect of approximating Member States’ contract laws, it is not clear (i) that this would contribute to the functioning of the internal market; or (ii) that such an action would be consistent with the principles of subsidiarity and proportionality.⁵¹

86. In order for the enactment of such an instrument to be possible under Article 114, it would be necessary to show that the internal market is not functioning optimally in some way, and that the introduction of a European contract law would ameliorate the problem identified. The Commission would also need to demonstrate why amending Article 6(2) of Rome I was not more in keeping with these important principles than preparing an entire new European contract law. (It is unquestionably far more straightforward to amend Rome I than to prepare a whole new contract law consistent with respect for the EU’s diverse legal traditions.)

87. While the Commission has identified certain problems—that some businesses refuse to sell cross-border, for example—it has not provided evidence that these problems are caused by divergences in national contract law. Indeed, the Green Paper cites the statistic that in 61% of cross-border e-commerce offers consumers were not able to place an order mainly because businesses refused to serve the consumer’s country, while the report from which this statistic is taken highlighted that this was largely due to technical problems or payment options not being available, rather than due to divergent contract laws.⁵² Other contributing factors might include language barriers, divergent packaging requirements, delivery pricing, divergent procedural requirements relating to claims and so on. It is not obvious that such problems would be solved by a European contract law. Even if such evidence can be provided that divergences between national contract laws are a barrier to trade and that this barrier would be removed by a European contract law, it would only justify measures relating to consumers and SMEs.

Article 352 TFEU

88. Article 352 provides power to adopt measures which are necessary to attain one of the Treaty objectives where the Treaties do not otherwise provide the power. This wider power, whilst requiring the consent of the Parliament, the Commission and unanimity in the Council, might

⁵⁰ Article 26 TFEU requires that “[t]he Union shall adopt measures with the aim of establishing or ensuring the functioning of the internal market, in accordance with the relevant provisions of the Treaties.” The *Tobacco Advertising* judgment establishes that mere differences between the contract laws of the Member States on their own are not sufficient for this purpose, nor is a desire by business for a European contract law. (See Case C-376/98 Germany v Parliament and Council [2000] ECR I-2247.)

⁵¹ Article 5(1) TEU

⁵² See sub-paragraph 2, Section 3.1 of the Green Paper. Data taken from “Communication from the Commission on Cross-Border Business to Consumer E-commerce in the EU” (COM(2009) 557, 22.10.2009).

provide a wider basis for adopting a European contract law. We note however, that the provision explicitly requires the measures to be necessary to achieve one of the Treaty objectives, and that the uncertainties highlighted above in relation to Article 114 would therefore apply equally.

89. Moreover, if a lack of cross-border trade is identified and correctly attributed to divergences in national contract law, it is not clear that a mandatory European contract law is the most appropriate way of resolving this. There is, therefore, a risk that such a measure (whichever Treaty article is used as a basis for adoption) would be inconsistent with the principles of subsidiarity and proportionality.
90. In respect of consumers, measures such as the Consumer Rights Directive and a revision of the current legislation in force regarding e-commerce are arguably a more appropriate forum for addressing such issues. In respect of businesses, an “optional instrument” (or indeed simply publication of the DCFR) would achieve the same aims with less impact on Member States’ national laws: businesses who wished to contract subject to the terms of the DCFR would be free to do so and those that wished to use an established legal system would also be free to do so. Indeed, if the DCFR is widely used, this might provide the necessary justification to form a basis for introducing a mandatory instrument.

Optional instrument

91. Article 114 has most frequently been suggested as a possible basis for an “optional instrument”. It is, however, difficult to see how an “optional instrument” could be said to have the purpose of approximating Member State’s laws. As Prof. Dr. Martin Hesselink has commented, “[a]lthough an optional 28th regime would be much more in line with the principles of proportionality and subsidiarity, somewhat ironically it is easier to find a legal basis for a non-optional European code (with the same scope) because an “optional instrument” would not lead to harmonisation.”
92. If the European contract law is recognised as a model of sound legal principles and clear drafting, it may be that Member States’ legal systems will over time adopt parts of the instrument and therefore become more similar. However, this is at best an indirect side-effect of the new law.
93. Alternatively, Article 352 has been put forward as a basis for an “optional instrument”. For the reasons highlighted above in relation to a mandatory instrument, there appears to be uncertainty as to whether there is sufficient evidence to show that an optional law is necessary to enhance the functioning of the internal market. Without firmer evidence that such a law is necessary legal challenges to an instrument based on Article 352 are a real possibility.

Article 81 TFEU

94. Article 81 provides that “the Union shall develop judicial cooperation in civil matters having cross-border implications, based on the principle of mutual recognition of judgments and of decisions in extrajudicial cases. Such cooperation may include the adoption of measures for the approximation of the laws and regulations of the Member States.”
95. Article 81 is generally understood to refer to procedural matters rather than adoption of a substantive body of law: the Article refers, for example to the recognition of judgments, service of judicial documents, training for the judiciary, etc. Contract law does not of itself involve “judicial cooperation”, nor is it based on “the principle of mutual recognition of judgments” and practitioners are not aware of this Article having been used as the basis for the adoption of substantive European laws. The Society respectfully suggests that it does not provide a sound basis for adoption of an optional law in this instance.

Article 169 TFEU

96. Article 169 has also been suggested in some circles as providing a possible basis. However, since this article only refers to the protection of consumers, it does not appear a possible candidate for a wider-ranging instrument than one dealing only with consumers.

Risk of uncertainty

97. In the view of practitioners who advise on financial transactions, there is a real possibility that, if an optional or mandatory instrument is enacted on the basis of one of the Treaty Articles considered above, market participants (and Member States) will be hesitant to use the new law for fear that it was invalidly enacted. It is possible that a legal challenge to the constitutional basis of the law would be brought, causing further uncertainty pending resolution of such a challenge.

98. Could this uncertainty be resolved? The principal options would appear to be:

(i) to amend the Treaty to explicitly confer the power to create such an instrument. Given the political processes required in each Member State to authorise such an amendment, it is doubted whether this is a realistic option; or

(ii) to adopt the DCFR, for example as part of a “toolbox” for European legislators.⁵³

Need

99. The Society is not convinced that there is a need for an “optional instrument”. As outlined above, in order to determine whether there is such a need, a broad study into the barriers of cross-border trade would need to be undertaken. We doubt if concern over the governing law of a contract deters a significant number of consumers from purchasing goods or services, whether on-line or otherwise, across the EU’s internal borders. Nor was this a barrier to cross-border e-commerce identified in the Commission study published in March 2009.⁵⁴

Rome I and consumer rights

100. Some particular issues have been raised in relation to Rome I, which concerns the applicable law of contractual obligations. Recital (14) of that Regulation anticipates the possibility of an instrument on contract law but says no more than that any such instrument may provide for the parties to choose any new substantive rules of contract law. In the Green Paper, the Commission acknowledges that it will be necessary to address the relationship of a new instrument with Rome I but does not elaborate. At the moment, in England and Wales, the courts have decided that a choice of law must be that of the law of a particular country and not, for example, Sharia law. Moreover “European contract law” could not at the moment be the governing law where the parties have made no choice. The rules in Rome I for determining the governing law of a contract in the absence of choice would all identify the law of a country as the governing law.

101. As to the cost to businesses of trading with consumers across borders, it is correct that, due to Article 6(2) of Rome I, a diligent business is required to take legal advice on the consumer protection laws in each Member State into which it sells because, whatever governing law is

⁵³ As stated above, the Society believes that any “toolbox” should be non-binding on legislators, who will wish to consider a range of options when legislating.

⁵⁴ Above, footnote 15.

chosen, consumers cannot be deprived of the protection of the mandatory rules in their home Member State. This imposes additional costs on business, and may deter some businesses from dealing with consumers in other Member States. This is despite the fact that, if the contract is subject to the law of a Member State, the consumer would benefit from the relevant national law which must, as a minimum apply the standards required by EU consumer protection Directives. The solution, however, is not to create a European contract law but to address the cause of the problem, namely Article 6(2) of Rome I. For example, Article 6(2) could be amended to exclude from its ambit transactions governed by the law of a Member State on the basis that consumers are already protected by the mandatory rules of EU law. Moreover this would also be consistent with the principle of mutual trust in other Member State legal systems developed by the Court of Justice in relation to Brussels I.

102. We recognise that the above approach raises issues covered in the recent discussions about the Consumer Rights Directive. These issues cannot be avoided, as the Green Paper tacitly recognises.⁵⁵ Even if there were to be an “optional instrument”, it would not achieve the Commission’s objectives if it merely sat alongside the national laws of the Member States. The choice of the “optional instrument” as the governing law of a consumer contract would still be subject to the consumer’s home consumer protection laws by virtue of Article 6(2) of Rome I and thus the potential deterrent effect on businesses identified above would continue. To achieve the Commission’s objectives, it would be necessary for the “optional instrument” to include its own consumer protection provisions and for those provisions to apply in place of the consumer’s home law, even if that home law offered the consumer more (or, indeed, less) favourable treatment than the “optional instrument”. As we have said, this leads to the issues raised by a possible Consumer Rights Directive but, without a resolution of these issues, an “optional instrument” will achieve very little. However, if those issues can be addressed through a Consumer Rights Directive or alternative dedicated consumer protection legislation, the supposed need for an “optional instrument” is much reduced.
103. As explained above, efforts are also ongoing to ensure full implementation of Article 20 of the Services Directive and a Commission Communication in regard to a new e-commerce initiative is expected in 2011 following a recently closed consultation by DG Internal Market and Services on the future of electronic commerce in the internal market and the implementation of the Directive on electronic commerce (2000/31). Taken together with the ongoing debate on consumer rights, the Society would like to see the outcome of these initiatives, and to what extent there are still significant cross-border trade issues, to determine if there is a need for further measures and to avoid an overlap or incoherence in new legislation.

Cost

104. In our view, it is also necessary to consider the practical consequences, particularly as regards cost, of the introduction of an “optional instrument”. Even if the instrument is optional, there will be (and already have been) significant costs for both the private and public sector. Over the last decade significant time and effort has already had to be spent by national governments, professional and trade associations, businesses and practising lawyers in following the European contract law project.

Application of optional instrument as EU law, rather than a foreign law

⁵⁵ Footnote 27 of the Green Paper states that “[i]t would be necessary to articulate in the instrument itself the relationship with the provisions of the Rome I Regulation”.

105. The cost issue with the proposal seems to centre on the different effect of the “optional instrument” from that of simply another jurisdiction with its own laws emerging giving the possibility of additional choices of law. This is because the “optional instrument” would be EU law and the courts of the EU would have to apply it as their own law, not as a foreign law.
106. In the courts of England and Wales, when a court deals with a contract governed by a law of a different jurisdiction, that other law is a matter of evidence, which the parties must prove. If they do not, it is presumed to be the same as the substantive law of the jurisdiction of the court. However, that would not be the case with the “optional instrument”. The courts in every jurisdiction would be faced with an alternative law which they were bound to apply as if it were the law of the jurisdiction - they would be addressed on its effect and could not presume it was the same as their domestic law, unless the parties all invited them to do so.
107. While this would be a difficult matter in civil law countries - it would look quite like their own contract law, but not necessarily be the same - there are some strongly divergent approaches as between the Code Napoleon countries and those with German style civil codes - for common law countries (the England and Wales and Northern Ireland jurisdictions within the UK, Ireland, Cyprus and Malta) it would be a completely different set of rules, which the entire legal profession would have to be educated to apply.⁵⁶ As civil law codes are not often used in English speaking countries, this would have to be done without the benefit of commentaries on similar domestic law, but from the ground up. Some practitioners have commented that this would be oppressive on common law countries and believe that this would put a disproportionate cost on them.

Increase in workload of the CJEU

108. An “optional instrument” would take time to develop its own jurisprudence.⁵⁷ Practitioners were generally of the view that, if the “optional instrument” were used, there would be more litigation than under national law because of parties’ lack of familiarity with it, particularly in business-to-business cases. More, and potentially longer, cases and more appeals would impose additional costs on business and require additional court and judicial resources, adding to public costs.
109. A further consequence of the “optional instrument” being a system of European law is that the only body that could pronounce authoritatively on its meaning would be the CJEU. The CJEU is in the nature of a constitutional court without power to substitute its own decision for that of the national court or national or EU regulatory body whose decision it is reviewing. Its judges do not generally have commercial experience. As presently constituted, all it could do is answer questions referred to it by national courts. It is overwhelmed by its current case load with periods of 3 to 5 years for decisions being quite common. The burden of a large number of commercial or consumer cases would add to delays.⁵⁸ The delays would add to the uncertainty and costs for the parties concerned.
110. Practitioners believe that the CJEU is wholly unsuited to dealing with an “optional instrument”, unless it is reformed, with a much larger budget and the expertise and capacity to hear commercial

⁵⁶ Gibraltar is also another affected common law jurisdiction.

⁵⁷ Some practitioners believe that this would take many decades or even more than a century.

⁵⁸ Practitioners further commented that, with an established set of rules for choice of court (Brussels I) and choice of law (Rome I), there are still a large number of preliminary references and disputes concerning these issues. The introduction of an optional regime was only likely to increase this.

cases. They believe that a new optional law would not lead to quicker or simpler or more uniform decisions, but to lengthy delays for test cases and others raising similar issues awaiting the views of the CJEU and, for parties not prepared to wait, decisions which are likely to be inconsistent across the Member States, representing local pre-conceptions, with even more room for unpredictability than when an existing national system is applied. In addition, where the law is applicable in arbitration, it would be more likely that the arbitral body would need to seek guidance from national and EU courts, adding to delay and costs in such dispute resolution also.

111. The suggestion that there could be a database of decisions across the EU is interesting but would not have the legal effect of decisions by senior courts or the CJEU. There would be no means of knowing which one of conflicting interpretations was the correct one. It would also involve a large and costly bureaucracy in establishing and maintaining the database and translating the decisions and the need to have a detailed process for reporting the cases in the first place.

Education and training

Training of legal practitioners in public and private employment

112. All judiciary and lawyers would have to be educated on the nature of the “optional instrument” (or at least all those whose work might involve contract law within the scope of the instrument). No-one has costed this exercise for the whole EU or explained how the tools of education would be created with no case law and no commentary on interpretation.
113. Without further information, it is impossible to quantify or understand what training would be required for England and Wales practitioners. However we understand from training providers that, if a final text were mainly based on civil law principles, a possible training process for common law practitioners could involve: (i) background training on the principles of civil law systems and how these principles are applied; (ii) training on the substantive rules in a new instrument; and (iii) training on how the new instrument would relate to the current national contract law system in place.
114. It is not possible to provide an indication as to training costs, but we believe that these would be very substantial.⁵⁹ As contract law is a core subject studied as part of a Law degree, there would be further costs in training sufficient academics and, for students, there would be an impact on the other topics they were able to study if this initiative became compulsory. We are in contact with training providers on this issue.
115. In the public sector, lawyers and judges would spend time away from carrying out their public duties in order to receive the training. There would also be ongoing costs of keeping up-to-date with decisions in various Member States and the CJEU.

Study by businesses (including SMEs) and education of consumers

116. Businesses would need to study the “optional instrument” and be advised on it by their lawyers in order to know whether or not they wished to agree to use it and to work out the consequences for

⁵⁹ There are no exact figures for the number of lawyers in the European Union, but the Council of Bars and Law Societies of Europe (CCBE) claims to represent over 700,000 European lawyers. As stated above, in 2009 in England and Wales there were between 112,589 and 115,475 solicitors holding practising certificates and 145,381 solicitors on the Roll of Solicitors (based on July 2009 figures). Presumably trainee solicitors and other legal professionals would also require training.

their businesses. It is not a question of just agreeing to use a different law but of working out the practical implications for their usual terms of business and their internal procedures. They would then need to have parallel systems in place depending on the law chosen. (This is why, in many organisations and markets, businesses often have a policy to use one legal system as the market standard for the relevant market.)

117. In addition, in regard to business-to-consumer contracts, it is unclear how consumers would be educated about the new law and, given what challenging questions it poses for lawyers, how consumers would assess the advantages and disadvantages of opting for it.⁶⁰ They would need to understand how the different options of governing law could affect their rights under a given contract. Practitioners instead believe a gradual approach towards the introduction of minimum standards for consumers and a step-by-step approach to harmonisation of consumer protection would better serve consumers' needs.

Inherent uncertainty in a new legal system

118. Whilst every piece of new legislation necessitates a certain level of uncertainty, practitioners were concerned that an "optional instrument" would raise this on many levels, including the interpretation of the new wording, its scope of application, its legal basis and how the CJEU could interpret it and standardise its application across the Member States. The Green Paper rightly refers to the need for an "optional instrument" to provide legal certainty in order to build the confidence of parties in the instrument. The "optional instrument" would not however be based on the established meanings and interpretations of existing legal systems. The closed manner of its preparation offers few grounds for confidence that it will provide the legal certainty offered by national laws, which often have many decades of experience to draw on (or even centuries). The new instrument would start without any established jurisprudence or any common understanding between Member States as to what it was intended to mean. Practitioners are not confident that it would deal with issues in a way that would receive the support from the parties who would be expected to use it.

Jurisprudence

119. All systems develop extensive jurisprudence on the meaning and application of provisions. The standard editions of the French and German civil codes have more space devoted to a discussion of the jurisprudence arising out of previous court decisions than to the articles of the codes themselves.
120. Without established and consistent jurisprudence, it would be difficult for the courts to come to consistent judgments and, more importantly, it would be difficult for clients to obtain firm and reliable advice in order to know how to structure agreements and draft contracts. This applies as much in the civil systems as in the common law systems which have the doctrine of precedent. Civil systems' courts may not decide a case on the basis of the decision of a previous court but, in applying the law to the facts, they need to know what the correct and consistent interpretation is of the law in question. Otherwise the application of the law becomes unpredictable and loses credibility with businesses and citizens.
121. The experience in The Netherlands is instructive where the development of jurisprudence is still very much continuing following the introduction of its new civil code in 1992. It takes time for disputes to arise, for cases to come to judgment, for appeals to be heard and for a body of

⁶⁰ Below, paras 132-133. See discussion regarding choice.

jurisprudence to develop. If this is then replicated across the Member States, there will be the problem of separate evolution within each Member State, with consistency only being achieved after cases have been to the CJEU.

122. There is considerable substantive uncertainty in the provisions of the DCFR. The Green Paper only poses questions at the conceptual level and does not seek comments on the substance of the DCFR but the text contains provisions which would result in legal uncertainty because of their inherent nature (for example, the scope and application of the general principle of “good faith and fair dealing” and how this would be applied, for example, in business-to-business contracts).⁶¹

Uncertainty regarding issues not covered in scope

123. We understand that the Expert Group is trying to draft an “optional instrument” comprising 150 articles and covering the sale of goods. This raises a number of concerns in regard to scope and what happens when some issues that parties would like to include within a contract fall outside of the scope of the new instrument (e.g. if parties wanted to produce a contract for the supply of goods and services) or if the new instrument was found to contain loopholes.
124. There could also be problems of multiple systems of law being applied in a dispute, which should be avoidable if a national system of law is chosen. With no optional system available for tort or property law, other systems of law would apply to related tort claims (e.g. misrepresentation or negligence) or property law disputes. Currently, following the introduction of Rome II, it is the norm that such tort claims are under the same system of law as the contract. Similarly, an appropriate choice of national law would enable property claims (including IP/IT issues like copyright and trademarks) also to be determined under the same system of law. This new instrument could therefore deharmonise the current system and be viewed as complicating, rather than simplifying, the existing structure.

Uncertainty for business

125. Given the lack of jurisprudence and the substantive uncertainty of the current DCFR (we anticipate that this is unlikely to be resolved in the work product of the Expert Group), if businesses opted for the new instrument, they would be well advised to draft their contracts with more detail and background included. This is in order either for it to be clear what is intended and to make it less likely that a provision would be held to be unreasonable or to override some of the rules and presumptions likely to be contained in an “optional instrument”. This could result in contracts having to be longer and more detailed than is common in some legal cultures and would impose additional costs on businesses.
126. Legal certainty is not achieved by merely being certain of the scope of application of the “optional instrument” and ensuring that texts are simple and accessible for citizens and practitioners. Whilst these issues are important, they would not address the underlying concerns regarding certainty.
127. For business (including SMEs dealing with other businesses, large and small) practitioners believe that legal certainty is more important than uniformity. That is why systems of law which are well developed and provide a high degree of certainty are popularly used.

⁶¹ See further S. Whittaker, Professor of European Comparative Law, University of Oxford, “A critical assessment of the content and possible role of the draft Common Frame of Reference for European contract law, published by the Academic Research Network in December 2007.”

Risk of lack of flexibility of a new instrument

128. There is concern in the lack of flexibility inherent in an “optional instrument”. Practitioners are concerned about how a codified instrument could be modified to take account of changing social attitudes and the needs of the markets. There is a risk that it could become out-of-date. The DCFR (and the work of the Expert Group) is regarded by some practitioners as having used a “snapshot” of different Member State systems as its basis. These systems are constantly evolving through court decisions and changing commercial practice and over time they are likely to move away from the foundations of the DCFR. Even if the CJEU takes on a role in developing the jurisprudence, practitioners are not convinced that it would be possible for it develop jurisprudence as is currently possible, for example, in the England and Wales courts, because it is unlikely to have the same through-put/volume of cases in relation to a new instrument and longer delays would be likely before important issues could be considered. Resources would need to be committed at EU-level to keep such an instrument up-to-date.

Cost on businesses

129. The survey of 100 European businesses by the Oxford Institute showed that 78% of respondents did not agree that variations in European civil justice systems deter them from doing business in certain jurisdictions and 58% did not agree that such differences constituted, overall, a barrier to trade. Respondents saw lower costs as the main advantage of a more harmonised European civil justice system.⁶²

130. In fact, practitioners believe that there would be costs for businesses that wished to adopt the “optional instrument”. For example, standard terms of business would need to be re-drafted in order to ensure that they were consistent with an “optional instrument” if businesses wished (or were required)⁶³ to offer this.

131. Practitioners did not believe that businesses would see positive benefits from an “optional instrument” in a measurable timescale. In the Green Paper, the Commission argues that “[a]n instrument of European contract law could help the EU to meet its economic goals and recover from the economic crisis”. This is an assertion (and we have not seen the evidence on which it is based) and practitioners disagree that an “optional instrument” should be portrayed as a solution to any immediate problem. Again, this demonstrates the urgent need for an impact assessment and further analysis before discussions continue.

Concern as to ability to choose

132. If, notwithstanding our doubts, there were to be an “optional instrument”, it must be truly optional. There should, for example, be no compulsion on businesses to offer it as an option when dealing with consumers or others across the EU’s internal borders. (In other words, contracting parties would have to “opt-in” to using the instrument, rather than “opt-out”.) If there were any compulsion on businesses to offer this option to consumers, it would discourage, rather than encourage, cross-border trade because it would impose an additional cost on the conduct of that trade.

133. On the other hand, from the point of view of consumers, there might a concern as to inequality of bargaining power if both they and businesses were free to agree to opt either for the law of a Member State legal system or the “optional instrument”, as it is likely that businesses would be

⁶² Above, footnote 23, pages 40 and 42.

⁶³ Below, para 132-133. See discussion regarding choice.

better informed as to the ramifications of choosing the different regimes as governing laws. It is possible that consumers could be disadvantaged by the proposal.

General comments on remaining options

134. Options 5, 6 and 7: These options would signal the end of national contract law systems (and, for Option 7, a much wider range of areas of law). As such there would be even greater objections on legal, constitutional, economic and cultural grounds. The objections raised in relation to Option 4 above would be equally applicable. Practitioners are unconvinced that the EU has the power to introduce any of these options and believe that these would infringe the principles of subsidiarity and proportionality.

Option 5: Directive on European Contract Law

135. Even if the EU had power to make a Directive on European contract law, which we doubt, it would be disruptive and costly, and would fail to achieve the Commission's aims. A Directive would be likely to result in minimum harmonisation of Member State contract law systems, but differences would be likely to continue.

136. It would be disruptive because the contract laws of all the Member States would need to be reviewed and, in most instances, changed in order to ensure that they complied with the Directive. The disruption that this would cause to established and successful national contract laws is obvious. Indeed, fears over the effect of changes and the resulting a lack of certainty may well lead parties to choose the contract law of a country outside the EU, which would be detrimental to the EU and the UK, as the success of English law internationally would be undermined. The consequences would be a loss of economic activity and export earnings for the EU as a whole.

137. It would be costly because of the training needed and because all contractual terms and conditions would need to be revised in order to ensure that they met the requirements of the amended law.

138. It would fail to achieve the Commission's objectives because national contract laws would remain different, even if they were somewhat closer than is the case now, both because of different understandings of the Directive and because each Member State could have provisions in addition to the Directive. Consumers and businesses dealing across borders would still, therefore, be faced with similar issues to those that they face now.

Option 6: Regulation establishing a European Contract Law

139. Even if the EU had power to make a Regulation providing for a European contract law that replaced Member States' existing national laws, which we doubt, it would be inconsistent with the EU's approach to freedom of contract and would be seriously detrimental to business within the EU.

140. Rome I is committed to party autonomy in the choice of the law that governs a contract (see, for example, Recital (11)). Reducing that choice to one law within the EU would be wholly contrary to this approach, as well as to the EU's commitment to respect the diverse cultural traditions of its Member States.

141. Given that the common law is used in only a small minority of Member States of the EU, it is almost inevitable that the common law approach to legal analysis, reasoning and drafting would be side-lined, if not eliminated entirely, despite its continuing to be a more successful "export" than any civil law system. As stated above, the uncertainty and novelty inevitable in any new law would be likely to drive parties to choose the law of a country outside the EU to govern their contracts with negative consequences for the EU and UK in particular.

Option 7: Regulation establishing a European Civil Code

142. This option has all the same objections as Option 6, but multiplied across the range of law to which it applies. Like options 5 and 6, it has nothing whatsoever to commend it.

4.2. What should be the scope of application of the instrument?

4.2.1. Should the instrument cover both business-to-consumer and business-to-business contracts?

Business-to-consumer

143. As stated above, the Society is unconvinced of the need to continue with work in regard to the options in the Green Paper. The Society supports a step-by-step approach to the harmonisation of consumer protection rules but believes this to be a separate issue from the underlying governing law of a contract and that it should be resolved either in the Consumer Rights Directive or an alternative piece of legislation focussing on consumer protection. If the “optional instrument” is to be pursued, given its background as an instrument designed for business-to-consumer transactions, practitioners do not accept that it is suitable business-to-business contracts, which have different characteristics.

144. It is possible to superimpose EU consumer protection provisions onto national contract law as has been done in the past. This would achieve the desired political and economic outcomes without incurring the disadvantages of the legal uncertainties mentioned in relation to an “optional instrument” and at less cost both for the public and private sector.

Business-to-business

145. In the experience of practitioners practising commercial law, when businesses enter into contracts with businesses in other Member States, generally legal differences between national legal systems are not a substantive difficulty. Coupled with the lack of evidence that the choice of law is a significant barrier to trade or that a business-to-business “optional instrument” would provide benefits, there does not seem to be a clear case for continuing with work on this instrument. Again, practitioners have raised practical concerns about cross-border trade, for example regarding different court processes and procedures between Member States, and issues of enforcement. As stated above, the Oxford Institute survey showed that 78% of respondents did not agree that variations in European civil justice systems deterred them from doing business in certain jurisdictions and 58% did not agree that such differences constituted, overall, a barrier to trade.⁶⁴

146. Practitioners believe that there is an important problem with the project in that it excludes any in-depth economic analysis and its origins lie in providing a high level of consumer protection for users so that this is not an appropriate basis from which to produce an instrument for business-to-business contracts.

147. Business-to-business contracts are different from business-to-consumer contracts. This is recognised in national systems either by having a more business-friendly commercial code (e.g. France) or by having specific consumer laws (whether or not in a consumer law code) which only

⁶⁴ Above, para 129.

apply to consumer contracts. Practitioners were generally of the view that businesses value the importance of certainty and predictability of outcome in their dealings while consumers are more concerned with fairness and remedies.⁶⁵

148. The Society does not believe that the issue of inequality in bargaining power between businesses of different sizes, which occurs in any market, should be addressed through an “optional instrument”. The Society is supportive of the freedom of parties to contract on the terms that they wish. Contracting parties negotiate and, for the contract to be agreed, each side needs to be satisfied that the contract is fairly drafted from their perspective. Weaker parties in a market will often group together to negotiate standard form contracts.
149. Much is made of the importance of extending consumer protection laws to SMEs. SMEs also need certainty of meaning and enforceability in relation to their contracts with other businesses. While larger businesses are better placed to deal with the significant additional costs of understanding the “optional instrument” and reconfiguring their processes and systems to handle it, the costs in time and money for SMEs are disproportionate. We understand that the experience in the Netherlands in relation to their new civil code in 1992 was that this was a huge exercise for business.
150. In the case of two SMEs of equivalent bargaining power from different Member States, an example of an obvious “neutral law” would be Swiss law with its established jurisprudence.
151. In contracts concerning the financial markets, in determining the capital requirements of financial institutions, the ability to net transactions and set-off matching assets and liabilities is crucial. In the absence of legal opinions that this can be done, institutions would have to account for their positions on the basis of their gross positions and not their net positions. If the meaning and/or enforceability of their contracts was unpredictable (for example because of the lack of jurisprudence or the discretions given to courts by an “optional instrument” based on the content of the DCFR), we understand that the opinions would not be able to be given with sufficient certainty to satisfy the requirements of the institutions’ regulators. Accounting for gross positions could have severe consequences and be detrimental to the global financial system. Some practitioners commented that great care therefore has to be taken to ensure that in pursuing the objectives of increased cross-border trade the financial system is not unintentionally adversely affected through this initiative. If EU institutions such as the European Investment Bank were to insist on the “optional instrument” being used, it could introduce systemic risks into the financial system both in relation to capital requirements (and therefore costs) and in the legal basis risk as there would be no certainty that hedging operations would result in uniform interpretation of contracts.

E-commerce/On-line transactions

152. As set out above, there are significant barriers to cross-border e-commerce across the internal market. Again, we are unconvinced that the governing law in a contract poses a significant barrier to trade. It seems more appropriate for the concerns with regard to e-commerce to be dealt with under the Consumer Rights Directive or as part of a new specialist proposal with regard to e-commerce. Some felt that whether consumers were willing to enter into an e-commerce

⁶⁵ Above, paras 61-63. Different surveys deliver different results as to which issues are important to business (e.g. fairness, predictability, legal certainty, familiarity, etc). The Society believes that much depends on how the questions are framed in each survey and that a thorough in-depth and broad-ranging study would be needed to understand these issues in greater depth.

transaction with a cross-border element was more likely to depend on the reputation of the seller and whether there was sufficient comfort that they would be able to obtain practical redress in the case of a problem.

153. Practitioners also questioned the scope of the term “e-commerce”. As an example, would the use of email in the formation of a contract by the contracting parties bring that contract within the meaning of “e-commerce”?

4.2.2. Should the instrument cover both cross-border and domestic contracts?

154. Whilst practitioners do not support an “optional instrument”, some thought that treating cross-border contracts separately from domestic contracts might be useful. On the basis that the new system would be inevitably more uncertain than those currently in place, it should not be required to be available, even on an optional basis, for purely domestic contracts. Practitioners expressed the view that domestic contract law should be a matter for Member State governments and their populations.

155. In contrast, other practitioners have commented that treating cross-border and domestic contracts separately could pose difficulties. They believe that solutions adopted should be capable of applying both to cross-border and to domestic contracts. They argue that if they are dealt with separately, this would lead to complication for consumers and businesses and would lead to uncertainty in establishing whether a contract was cross-border or domestic. A definition of a cross-border contract would also be needed. How would a contract be classified if, for example, an Italian national entered into a contract when present in a UK jurisdiction?

4.3 What should be the material scope of the instrument?

156. We are unconvinced of the need for an instrument of European contract law for the benefit of consumers, SMEs or e-commerce. As stated above, the Society believes that there needs to be far greater recognition of the differences between business-to-business and business-to-consumer contracts in the current drafting process.

4.3.1. A narrow interpretation of scope

157. If, despite the concerns raised, the instrument is to proceed, it should have a narrow scope. This would make it more readily achievable. The broader scope referred to in the Green Paper strays into areas of great complexity, such as property law, which are very specific to national legal systems.⁶⁶ As there are grey areas between contract and property issues which vary between Member States, this could pose problems in the development of a 28th regime. A change to the rules on the passing of title on the sale of goods would be an enforced change to the system of property ownership for goods in the affected Member States.

158. Although we would not support an “optional instrument” and although practitioners have drawn attention to the benefits of the common law system in which standard contract law is of universal application, if there is to be an instrument, we would favour a narrow scope embodying particular types of contract being specified, such as sale of goods in on-line transactions.

⁶⁶ Article 345 TFEU states that “[t]he Treaties shall in no way prejudice the rules in Member States governing the system of property ownership”.

4.3.2. A broad interpretation of scope

159. Tort, unjustified enrichment and benevolent intervention should not be covered. These are all enormous subjects in themselves. Changes to these would require more debate and cultural changes. Most importantly, they are not subjects which lend themselves to optionality and so have no place in an “optional instrument”. They arise because of circumstances or actions (or omissions) that are independent of a mutually agreed contract.
160. Practitioners noted that an “optional instrument” is likely to have unintended consequences (e.g. the scope for uncertainty regarding different governing laws when, in addition to contract law, other areas of law also apply in a transaction) and that these unintended consequences would be likely to increase in number if the Regulation was to become a mandatory system, rather than a parallel or optional contractual system.^{67 68}

Potential for confusion

161. We understand that the Expert Group is producing a draft “optional instrument” for sale of goods contracts. Some practitioners have commented that there is often no clear distinction between the service element and goods element of a contract. For example, on the sale of office equipment, the sale of the equipment, its loan financing and the maintenance contract may be bound up in one single contract. There is concern as to how the Expert Group intends to draw a distinction and whether uncertainty will arise in the classification of contracts subsequently.

4.3.3. Should specific types of contracts be covered in the instrument?

162. The Green Paper discusses specific types of contract. Some practitioners felt that one of the disappointments of the DCFR was its maintenance of the civil law concepts of specific rules for different types of contract whilst they saw one of the strengths of common law systems as the ability to treat contract law as of universal application regardless of the type of contract, with limited special rules for some types of contract. It was felt that this avoided the problems of categorisation which can occur under civil legal systems and enabled commercial flexibility and innovation.
163. A small number of practitioners have commented that the contract for the sale of goods is likely to be the most relevant form of specific contract and that, if service contracts are to be included, there would need to be specific provisions for specific types of service contracts.

Concern regarding matters outside the scope

164. Any new instrument would need to contemplate the fact that some matters would fall outside the scope of the instrument and be determined in accordance with another law. This is a point of general concern to practitioners. Whilst we do not want a new instrument to have a broad scope for all the reasons outlined above, in a case where some matters would fall to be determined in accordance with another area of law, we see potential for complication and uncertainty.

⁶⁷ E.g.1 In regard to mandatory requirements, one pertinent example for private client solicitors is the proposed application of the Consumer Rights Directive provisions on withdrawal periods to the provision of legal services outside of the office (for example in the drafting of a will at a client’s home).

⁶⁸ E.g.2 If the “optional instrument” extended into areas such as benevolent intervention, it would presumably have a direct effect on national legislation, such as, in the UK, the Mental Capacity Act 2005 and the supervision of Lasting Powers of Attorney.

Private client perspective

165. From the point of view of the private client/trust practitioner, any Regulation with uncertain boundaries has to be closely scrutinised. Given that civil law systems tends to equate or regard fiduciary relationships as being in many cases contractual, there is scope for confusion and potentially a restraint on the fundamental concept of the trust within the common law.
166. Private client/trust practitioners would stress, however, that if the broader material scope is introduced it may open up the EU to the benefit of the law of trusts. However, given the relative lack of common law input to date in the preparatory work on the Regulation this may now be difficult to achieve. It is therefore vital that the development of the Regulation is kept under scrutiny, not only in respect of the basic aspects of commercial contract law but also in its inevitable extension to gifts and other non-commercial matters. The Common Frame of Reference would create both threats and opportunities for private client practitioners.⁶⁹

⁶⁹ Other practitioners have however stated that they do not agree that the agenda should be driven by a desire to expand the remit of trust law given the possible implications of a new instrument on contract law.

5. FINAL COMMENTS

Purpose of the project

167. This paper has not sought to analyse the text of the DCFR but practitioners note that there are helpful critiques available which provide a valuable insight into the work on European contract law already produced.⁷⁰ If the conclusion is that a new pan-European “optional instrument” is to be made available, practitioners believe that there should be in-depth consideration of the form that this should take, including whether such an instrument should follow the common law models favoured internationally, rather than a civil law approach, and that market participants should be closely involved.

Need for wider stakeholder involvement and inclusion of common law practitioners

168. As referred to above, the experts in the Expert Group are mainly academic lawyers and many have been closely involved with the promotion of a European civil code and/or the elaboration of the DCFR for some time. This does not objectively sit easily with the statement in the Green Paper that they are “they are acting independently and in the public interest”. England and Wales practitioners feel that they could contribute valuable expertise and would like to be included in ongoing discussions. The profession has a large amount of expertise working with other jurisdictions and on cross-border contracts. In addition, as stated above, the Society would encourage the facilitation of greater involvement of consumer, business and practitioner groups from all jurisdictions within the European Union.⁷¹

169. It is also difficult to see how a group of academic lawyers with some practitioners can make decisions (even preliminary ones) as to what is desirable unless the economic objectives have been discussed and analysed by the appropriate experts and the results of the Commission’s consultation collated. Practitioners do not agree that a relatively small stakeholder forum is sufficient to provide this input.

170. At a time of austerity, it is important that money and resources are spent only on initiatives that are likely to benefit EU citizens in a cost-effective manner.⁷²

⁷⁰ Above, footnote 61.

⁷¹ Article 67(1) TFEU states that “[t]he Union shall constitute an area of freedom, security and justice with respect for fundamental rights and the different legal systems and traditions of the Member States.” In the Stockholm Programme (see footnote 51), in paragraph 3.1.2., it states that in regard to civil law initiatives, “the Commission could submit appropriate proposals taking into account the different legal systems and traditions in the Member States”.

⁷² Practitioners cited previous instances where the creation of a legal instrument for commercial use has been unsuccessful, e.g. the European company (Societa Europea). Work started in 1970 and the Regulation ((EC) 2157/2001) was adopted in 2001. Despite over 25 years’ of negotiations, in practice it has been little used. Similarly, the European Economic Interest Grouping (EEIG) for the promotion of cross-border business on a joint venture basis has been little used.