

ALLEN & OVERY



22 November 2011

Joanna Page & Jason Rix

*Will we soon have a single
pan-European contract law?*

Route map

1. Setting the scene: What is it? Who is it for? Who can chose it? What is the scope?
2. The politics
3. The controversies
4. A look at the code
5. The statistical basis
6. Next steps / conclusions

What is it?

- A proposed Regulation for a **Common European Sales Law** as an optional supplement to national law for the sale of goods and related services plus digital content
 - Regulation (16 articles) has mechanics of who can choose and in what circumstances as well as how it is to take effect
 - 186 articles of the autonomous code contained in the Annex to the Regulation
 - Code **in parallel** to (not replacing) current national laws
- Sales Law easier to justify when proposing Article 114 (harmonisation of the internal market) as the legal basis?

Who is it for?

- "Mr. Kowalski, the owner of a small Polish company in Radom, develops a uniquely designed organic wooden bed for children. He takes part in a furniture fair organised in Kraków for which he pays a €2,500 participation fee. His beds attract the attention of two well known German and Italian retailers at the fair. Mr. Kowalski's company has the capacity to sell to both retailers and starts negotiations with both of them."
- According to the Commission: legal fees cost an average €10,000 for each additional export market

Who can chose it?

- Business[†] to consumer
- Business[†] to business where at least one SME* (Article 7)
- Consumers must give explicit statement of (informed) consent (Article 8)
- Not consumer to consumer

† actual word is "trader"

*SME = employs <250 person and annual turnover <EUR250m (Article 7)

What's the material scope?

Territory

- Cross border (Article 4)
- Extends to "third countries" (Recital 12)

Subject matter

- Sales of goods and provision of related services (Article 5)
- Supply of digital content
- Nor mixed purpose contracts (Article 6)
- Insurance? Maybe - see Opinion of EP 8 June 2011
- Not financial services (for the moment)

But is it a complete code? What does parallel mean?

- Not "legal personality, the invalidity of a contract arising from lack of capacity, illegality or immorality, the determination of the language of the contract, matters of non-discrimination, representation, plurality of debtors and creditors, change of parties including assignment, set-off and merger, property law including the transfer of ownership, intellectual property law and the law of torts." (Recital (27))
- Also, from a practical perspective, it does not address jurisdiction, service and enforcement
- "Flanking measures" including developing European model contract terms

The politics behind the proposal

- "...will help kick-start the Single Market Europe's engine for economic growth. It will provide firms with an easy and cheap way to expand their business to new markets in Europe while giving consumers better deals and a high level of protection" (Viviane Reding)
- "Traders who are dissuaded from cross-border transactions due to contract law obstacles forgo at least **€26 billion** in intra-EU trade every year."

The political support

- European Commission ✓
 - European Parliament vote in plenary on 8 June 2011
 - 521 in favour, 145 against, 8 abstentions ✓
 - Polish Presidency ✓
 - Subsequent presidencies: Denmark, Cyprus, Ireland?
 - Council of the European Union?
 - Estonia, Luxembourg, Netherlands & Poland ✓
 - Germany "could be advantageous to [SMEs]" but need detailed scrutiny
 - France & Sweden: need more empirical evidence
 - Belgium & Ireland: even if a problem, not convinced this is the solution
 - Austria: does not address all aspects of legal relations
 - Hungary, Sweden and ors: concerned by differing interpretations and time to refer to ECJ
 - Czech Republic: undermines consumer rights
- (Based on responses to original green paper as summarised by Law Commission in its advice of November to UK Government)

The political support

- UK Ministry of Justice ✕
 - "[an] 'Esperanto fallacy' ... 'a utopian belief that a perceived problem of diversity of languages can be solved by creating an extra one'" (Ken Clarke)
 - Law Commission
 - "there is a case for a new optional code to cover distance selling across the EU"
 - "we are not convinced that developing a CESL for commercial parties should be seen as a priority"
- SMEs?
 - "...It is astonishing that the results of this consultation [to the original green paper] haven't been comprehensively taken into account by the European Commission because most of the responses had been critical towards the general need of a European Contract Law" (UEAPME)
 - UK Federation of Small Businesses very supportive of proposal
- Consumer lobby ✕
 - "a pointless proposal" (Which?)

The controversies: is there a proper legal basis?

- Currently **Article 114** TFEU "... measures for the approximation of the provisions laid down by law ...which have as their object the establishment and functioning of the internal market" (**Qualified Majority Voting**)
- Commission needs to be able to point to objective justification
- Can an optional law, limited to cross border contracts, ever have harmonisation as its object?
- **Article 352** "If action by the Union should prove necessary, within the framework of the policies defined in the Treaties, to attain one of the objectives set out in the Treaties, and the Treaties have not provided the necessary powers, the Council, acting **unanimously** on a proposal from the Commission and after obtaining the consent of the European Parliament, shall adopt the appropriate measures."

The controversies: consumers may lose protection

- Rome I Article 6(2) choice of law "...may not, however, have the result of depriving the consumer of the protection afforded to him by provisions that cannot be derogated from by agreement by virtue of the law which, in the absence of choice, would have been applicable"
- Article 11 CESL "Where the parties have validly agreed to use [CESL] for a contract, only [CESL] shall govern the matters addressed in its rules..."
- Recital (12) CESL "Since [CESL] contains a complete set of fully harmonised mandatory consumer protection rules, there will be no disparities between the laws of the Member States in this area, where the parties have chosen to use [CESL]. Consequently, Article 6(2) [Rome I], which is predicated on the existence of differing levels of consumer protection in the Member States, has no practical importance for the issues covered by the Common European Sales Law"
- So by choosing CESL a consumer may lose national protection

The controversies: will consumers give informed consent and is the choice practical?

- Article 8(2) CESL "the agreement on the use of [CESL] shall be valid only if the consumer's consent is given by an explicit statement which is separate from the statement indicating the agreement to conclude a contract"
- Standard Information Notice in Annex II
 - But is this "informed" consent under EU law?
 - Will traders be dissuaded from offering CESL for fear of losing sales because of the extra steps?
 - What about telephone sales? Law Commission: "cumbersome"

Key concepts in CESL: good faith, fair dealing & reasonableness

- Good faith and fair dealing (Article 2)
 - Overriding duty
 - Breach may lead to loss of other rights or remedies (by the party in breach)
 - Non-derogable
- "'good faith and fair dealing' means a standard of conduct characterised by honesty, openness [was "loyalty"] and consideration for the interests of the other party to the transaction or relationship in question"
- "Reasonableness is to be objectively ascertained, having regard to the nature and purpose of the contract, to the circumstances of the case and to the usages and practices of the trades or professions involved" (Article 5)

The code: reversal of caveat emptor?

- "Before the conclusion of a contract ...the supplier has a duty to disclose by any appropriate means to the other trader any information concerning the main characteristics of the goods, digital content or related services to be supplied which the supplier has or can be expected to have and which it would be contrary to good faith and fair dealing not to disclose to the other party" (Article 23)

The code: modified acceptance

- "A reply which gives a definite assent to an offer is an acceptance even if it states or implies additional or different contract terms, **provided that these do not materially alter the terms of the offer**. The additional or different terms then become part of the contract." (Article 38(3))
- What is material and what is not?

The code: conflicting standard contract terms

- "Where the parties have reached agreement except that the offer and acceptance refer to conflicting standard contract terms, a contract is nonetheless concluded. **The standard contract terms are part of the contract to the extent that they are common in substance.**" (Article 39)

The code: unfair exploitation

- "A party may avoid a contract if, at the time of the conclusion of the contract: (a) that party was dependent on, or had a relationship of trust with, the other party, was in economic distress or had **urgent needs**, was improvident, ignorant, or inexperienced; and (b) the other party knew or could be expected to have known this and, in the light of the circumstances and purpose of the contract, exploited the first party's situation by taking an excessive benefit or unfair advantage." (Article 51)
- Known, eg, to German law but anathema to English law

The code: interpretation

- "A contract is to be interpreted according to the **common intention** of the parties even if this differs from the normal meaning of the expressions used in it." (Article 58)
- Subjective
- "In interpreting a contract, regard may be had, in particular, to: (a) the circumstances in which it was concluded, including the preliminary negotiations; (b) the **conduct of the parties, even subsequent** to the conclusion of the contract" (Article 59)

The code: determination of price

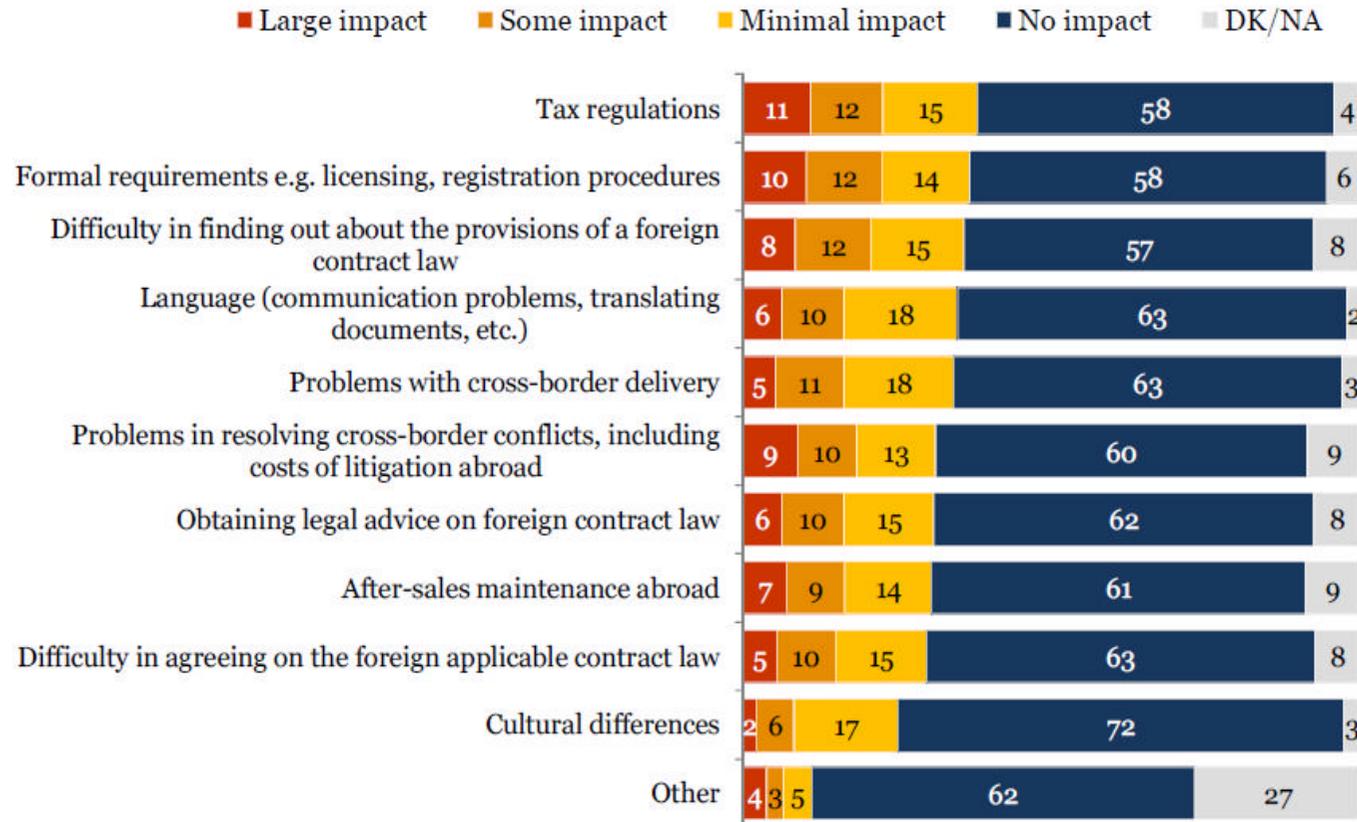
- "Where the amount of the price payable under a contract cannot be otherwise determined, the price payable is, in the absence of any indication to the contrary, the price normally charged in comparable circumstances at the time of the conclusion of the contract or, if no such price is available, a reasonable price" (Article 73)

A worked B2B example (from the Law Commission)

- Let's return to Mr Kowalski
- Imagine he has entered into a 5 year exclusive licence to sell beds to Italian retailer, Letti.
- There is a provision permitting him to terminate after 1 year if less than 100 beds are sold.
- Mr Kowalski does not mention to Letti, poor sales by Spanish retailer, Camas
- On and off Mr Kowalski has been in secret discussions with a rival Italian firm about becoming exclusive licensee
- In fact Letti only sells 90 beds.
- **English law:** Mr Kowalski can terminate using break clause
- **CESL:**
 - Art 2 breach of good faith?
 - Article 59 interpreting the term? Only meant best endeavours not an absolute obligation (based on pre/post contract discussions)?
 - Art 23 failure to disclose?

The statistical basis: business to business

Impact of potential obstacles on companies' decision to sell or purchase cross-border



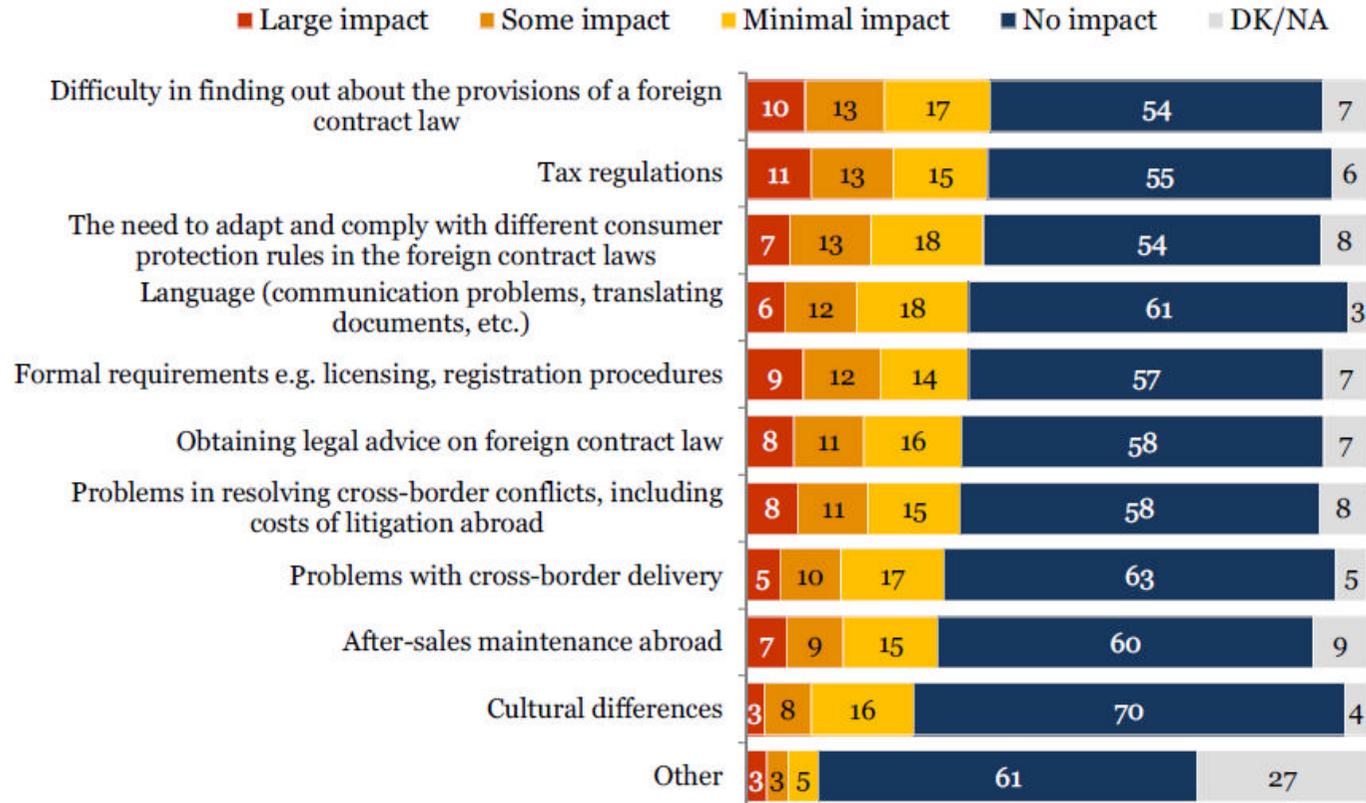
Q2. What impact do the following potential obstacles have on your decision to sell / purchase across border to / from businesses from other EU countries?

Base: all companies, % EU27

Graph sorted by 'any impact'

The statistical basis: business to consumer

Impact of potential obstacles on companies' decision to sell cross-border to final consumers



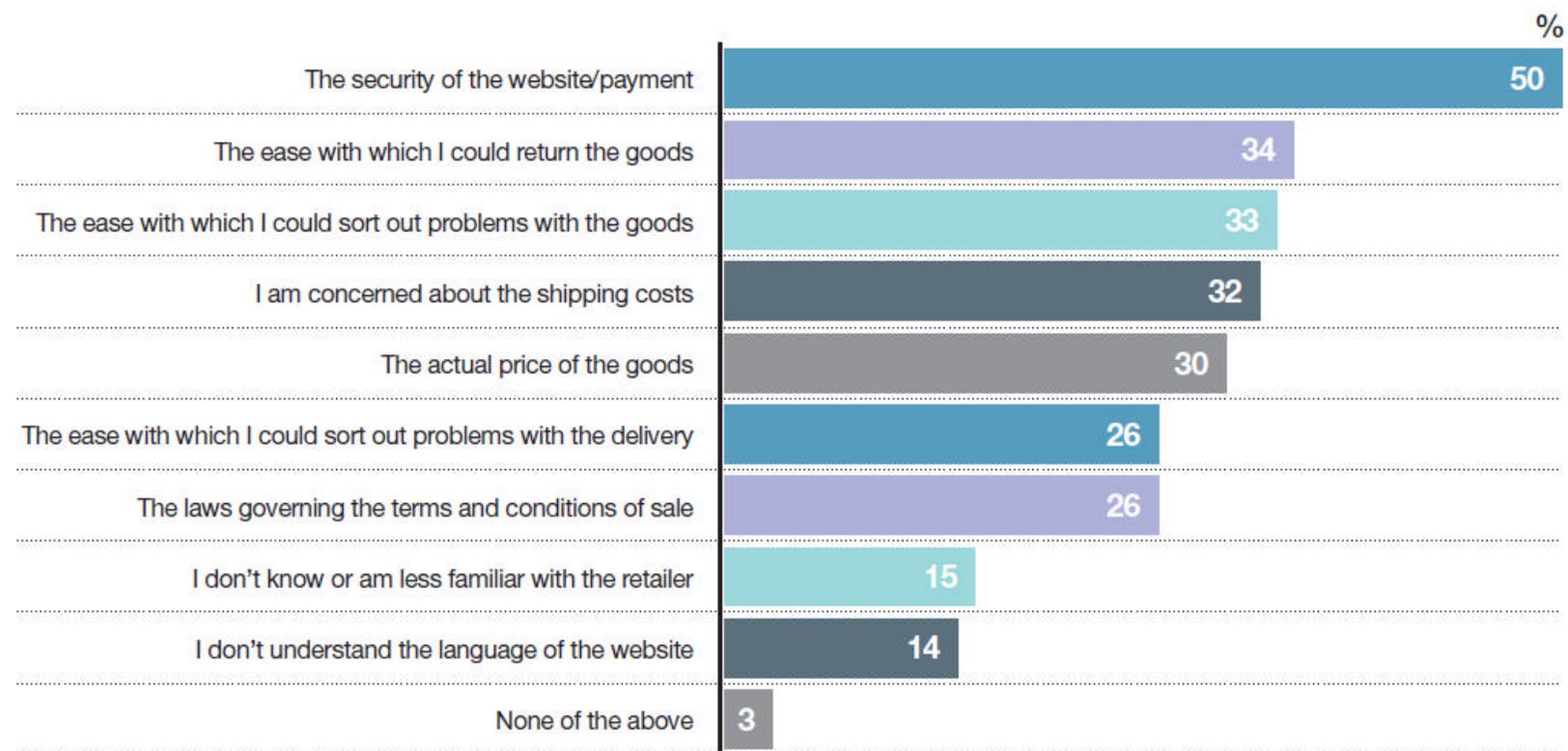
Q2. What impact do the following potential obstacles have on your decision to sell across border to consumers from other EU countries?

Base: all companies, % EU27
Graph sorted by 'any impact'

A&O Ipsos MORI research

CONCERNS OVER BUYING GOODS/SERVICES FROM ABROAD

Q: Which two or three of the following would concern you most about buying goods or services online from companies based abroad?



Next steps



Opportunities for comment?

- Formal consultation closed but:
 - Respond to MoJ call for evidence?
 - Write to European Commission, MEPs and MPs
 - Talk to Law Society
 - All, potentially, before the end of the year

Conclusions

- We may well see a Common European Sales Law
- Keep on your radar
- Provide comments
- Watch out for insurance / financial services

For more commentary please see
www.allenoverly.com/eucontractlaw

Questions?

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