

RESPONSE OF ALLEN & OVERY LLP, LONDON
TO
THE CALL FOR EVIDENCE ISSUED JOINTLY BY THE MINISTRY OF JUSTICE AND THE
DEPARTMENT FOR BUSINESS INNOVATION AND SKILLS
IN RELATION TO
"A COMMON EUROPEAN SALES LAW FOR THE EUROPEAN UNION – A PROPOSAL FOR A
REGULATION FROM THE EUROPEAN COMMISSION"

PART I: THE COMMISSION'S PROPOSAL – THE PROPOSED REGULATION

The principle of a Common European Sales Law

1. Do you support the principle of a Common European Sales Law (CESL) as proposed by the Commission? Please give evidence and reasons for your answer.

We have not seen compelling evidence of a need for CESL (or equivalent) for either business-to-business or business-to-consumer contracts. Nor are we aware of any groundswell of support for such a proposal from our clients.

The Commission has said that differences in contract law between Member States deter trade across borders, especially online trade, and suggest CESL would address this problem. In fact, in the online consumer sector, the evidence Ipsos MORI collected on our behalf suggests that other factors, such as concerns about payment security and shipping costs, are a far greater deterrent to cross-border online trade than the absence of a uniform governing law.¹ A copy of this report is attached. Additionally, the evidence from this survey indicates that younger consumers buy goods and services from other Member States online more frequently than older consumers. This suggests that, over time, the population as a whole across Member States will make more cross-border online sales, and to that extent the Commission's objective will be met.

We note that a survey by Boston Consulting Group² earlier this year suggests that the internet economy is in good health and indeed growing in the UK: it predicts UK growth of 11% per year. It also highlights that the internet economy in the UK accounted for the highest percentage of national GDP, when compared with other G20 countries.

We note that the Consumer Rights Directive³ will come into force next year and that its impact on business-to-consumer transactions will not be properly ascertainable for some time. Any further initiatives in the area of a harmonisation of consumer contract law would therefore be premature (and potentially damaging) prior to any assessment of the impact of this new legislation across Member States.

Parties choosing CESL cannot ignore national law. As the explanatory memorandum to the proposed Regulation makes clear⁴ it will still be necessary to determine the applicable law for cross-border contracts (either by choice of the parties or by the default rules). Moreover, a number of areas of law fall outside CESL (see Recital 27); for example: illegality, the law of tort, set off and assignment. It may also be necessary to refer to national law to determine how the two regimes (national and/or CESL) interrelate. Further, in business-to-business contracts, a party may also opt out of certain CESL provisions. Many of the efficiencies outlined by the Commission by the

¹ We commissioned an online consumer research study from Ipsos MORI. Our study asked online shoppers across Europe to select two or three issues that most concern them when purchasing goods from abroad. One issue stands out from the rest: the security of the website/payment. A second tier of issues is also apparent, which might be grouped under two headings: those relating to the goods (such as ease of return and sorting out problems) and those relating to prices, (shipping costs and the actual price) <http://www.allenoverly.com/AOWeb/binaries/59807.PDF>.

² Please see <http://www.bcg.com/media/PressReleaseDetails.aspx?id=tcm:12-100468>.

³ Directive 2011/83/EU of the European Parliament and of the Council of 25 October 2011.

⁴ See page 6.

introduction of CESL would therefore not be made. These factors do not appear to have been considered fully as part of the Impact Assessment (which suggests for example "a single body of rules, would remove the necessity for judges to investigate foreign law and compare several laws decreasing litigation costs compared to the BS ([baseline scenario – ie no policy change])".⁵

We also note that there are other cross border approaches in existence eg the UN Convention on Contracts for the International Sale of Goods (the Vienna Convention). It is our experience these provisions are not widely used in international business contracts, suggesting they are either not needed or that parties value the certainty of a particular choice of national law (eg English law) above all else.

As to boosting trade with countries outside the EU, CESL is likely to be largely irrelevant to such cross-border sales as it is unlikely to be chosen for such contracts. Indeed, if it is chosen, it may simply add a layer of uncertainty. The Commission states that CESL "should not be limited to cross border situations involving only Member States, but should also be available to facilitate trade between Member States and third countries"⁶. However, complex issues arise in this context. First, it is unclear how the combination of CESL and a choice of third state (non-EU) would work. Secondly, it is unclear if CESL would be considered a "choice of law" by non-EU courts. If it is not, then parties face uncertainty as to which law will govern their obligations. The approach of third state (non-EU) courts to CESL is particularly important given disputes relating to sales to consumers outside Europe are likely to be resolved before a consumer's local courts. Thirdly, it is perhaps unrealistic to expect third state (non-EU) consumers to select not only CESL to govern their contracts, but also a national law when entering a contract (and, in the case of consumers, for such a choice to be "informed" and meet with the formalities described in CESL – see further below).

CESL does not address dispute resolution. Even if there is a uniform sales law across Member States, there may still be a need for SMEs⁷ and others contracting under CESL to hire local lawyers in the jurisdictions in which they are trading because disputes under these contracts may be resolved before those local courts. Consumers remain entitled under Article 16 of the Brussels Regulation⁸ to be sued in the court of their domicile.⁹ Commercial parties may still need to resolve disputes in foreign courts if they are bringing proceedings against that foreign purchaser¹⁰. These risks do not disappear because of the introduction of CESL. This is a further point which the Impact Assessment did not appear to have considered properly (see below).

Impact Assessment

As noted in the Call for Evidence, the Green Paper¹¹ started from the premise that the current divergence in national laws was a hindrance to the proper functioning of the single market and suggested a number of options to address this. We disagree with this premise.

We have concerns about the reliability and thoroughness of the Impact Assessment, including:

- (1) The Assessment was not comprehensive as we have been led to believe that the study conducted by IBF International Consulting did not involve interviews with representatives from all Member States.

⁵ Impact Assessment, p. 39.

⁶ CESL is available for cross-border sales between traders where parties have their habitual residence in different countries of which one is a Member State and between a trader and a consumer where one is a Member State – Article 4.

⁷ Small or Medium sized Enterprises defined in Article 7 of CESL.

⁸ Council Regulation (EC) No 44/2001.

⁹ We know the Commission has proposals for ADR and ODR for consumers (COM(2011) 793/2 and COM (2011) 794/2) which are outside the scope of this Call for Evidence but as we understand the proposals, these initiatives do not remove parties' rights to go to court to have their disputes resolved.

¹⁰ The general rule under the Brussels Regulation is that proceedings are to be brought in the place of defendant's domicile – Article 2.

¹¹ COM(2010)348 final.

- (2) The Assessment does not appear to have properly taken into account that legal advice on national law may still be required notwithstanding a choice of CESL (see above).
- (3) The Assessment does not include a detailed examination of the costs involved in training lawyers, judges and students on the new law (both initial and continuing costs).
- (4) No questions were asked about existing alternatives eg the Vienna Convention.
- (5) There are also a number of questionable assumptions adopted in the Assessment and no or insufficient weight has been placed on Option 1 (do nothing). See further our response to question 11 below.
- (6) The Assessment assumes that there will only be a "limited" number of cases referred to the Court of Justice of the European Union (**ECJ**) on CESL. In fact, it seems likely given the uncertainties surrounding CESL that there will be a high number of references.
- (7) The Assessment assumes a new database of decisions on CESL will "ensure transparency and de facto convergence of relevant case law".¹² This fails to take into account, *inter alia*, of the fact that decisions of one Member State are not binding on another.
- (8) Parties contracting under CESL may still have to have their disputes resolved before the courts where their counterparties are based and therefore require local law advice. The Assessment does not properly consider this issue.
- (9) When we were interviewed by the authors for the purposes of gathering data for the Impact Assessment, we were told that *the draft report had already been prepared*.

We are concerned that the Impact Assessment lacked the objective and statistical rigour required for such an important survey.¹³ We expand upon these concerns in our response to Question 11 below.

We support the Commission's desire to boost cross-border trade within the EU but consider that other, less ambitious and potentially disruptive, initiatives should be pursued at this stage. For example, a set of Commission sanctioned model contract terms (based on existing national laws and with guidance notes explaining any local variations) may be a more proportionate response to the perceived problem.

2. Do you see any major strengths, weaknesses, opportunities or threats associated with the proposal? If so, what are they and who do they affect?

We anticipate that there is a risk that the costs of litigating a dispute under a CESL contract may be greater than a contract under national law. This is principally for two reasons. First, because there will be more references to the ECJ, as parties seek to resolve unfamiliar concepts under the new law. These references will take a great deal of time to resolve – currently the average time for an ECJ reference to be resolved is 16 months. Secondly, litigation involving a CESL contract may also take longer to resolve and be more costly than a dispute involving a contract under national law, because of the nature of the new law. CESL may increase the breadth of admissible evidence, thereby increasing costs on disclosure and lengthening hearings. For example, it may involve parties arguing over what was disclosed in pre-contractual negotiations (such evidence would generally not be admissible under English law). It may also increase the amount of admissible evidence in relation to

¹² The database would apparently be set up and funded by the Commission and provide translated summaries of the cases in English, French and German (see page 38 of the Impact Assessment).

¹³ The Commission note at page 2 of its response to the feedback on the feasibility study that "A large number of respondents also stressed the importance of a comprehensive and sound impact assessment".

post-contract behaviour (to determine issues such as whether or not there had been a change of circumstances such that the counterparty has a duty to negotiate).

As noted, there are numerous complexities and uncertainties surrounding CESL, including conflict of law issues (in particular the interplay with Rome I),¹⁴ uncertainties arising from the text itself and the legal basis of the proposed instrument. Further, by using a consumer protection model to seek to protect certain businesses (who arguably do not need such protection), CESL undermines legal certainty.

Please also see our responses elsewhere in this document which are also relevant to the SWOT analysis.

3. The proposed Common European Sales Law is an optional instrument. Is it, as drafted, something you would choose to use or advise others to use? Please outline the nature of your interest in the Common European Sales Law and give reasons for your answer.

Whilst we acknowledge that in its current form CESL is an optional instrument, there is concern about potential "mission creep" meaning that, at some point in the future, it becomes mandatory.

As currently drafted, we would not advise our clients (which are predominately corporates and financial institutions and may include some SMEs as defined at Article 7), to choose CESL. The reasons for this advice include: the lack of a clear legal basis (whether on grounds of proportionality, subsidiarity, the reliance on Article 114 of the Treaty on the Functioning of the European Union (TFEU), the interaction with Rome I or otherwise) the uncertainty associated with choosing any new legal system, uncertainty on the substance of the new law, uncertainty on the scope of CESL, uncertainty surrounding the given scope for the courts to rewrite contracts made under CESL, the absence of case law on or any explanatory memorandum of new or autonomous legal concepts, the consequent risk of costs and delay associated with resolving all these uncertainties by reference to the ECJ. In addition, the concept of "freedom of contract" is diminished as a result of the restrictions placed by the terms of CESL as to what parties can agree.

It would be desirable for the Government to seek a formal legal opinion on the question of legal basis.¹⁵ There are three main provisions of the TFEU which could be the legal basis for CESL: Article 81 (which was used for Rome I), Article 114 (on which the Commission relies) and Article 352 (the fallback provision if no other legal basis is appropriate). In relation to Article 81, it remains unclear why, if this was the proper basis for Rome I, it should not also be the proper basis for CESL. Article 114 is for "measures for the approximation of the provisions laid down by law ... which have as their object the establishment and functioning of the internal market". It is unclear how an optional second regime which explicitly preserves the existing 27 national regimes can be said to be a measure for "approximation". Even if it can, is it the most proportionate measure? Finally, even if both these concerns can be met, for the reasons set out elsewhere in this response,¹⁶ we have concerns that the evidence that the Commission relies on in support of this initiative does not appear to show clearly that CESL will contribute to the removal of obstacles to the free movement of goods.

The position in relation to Rome I is nuanced and any legal opinion should explore this in detail. The Regulation which contains CESL is directly applicable. But so too is Rome I. How is CESL to be directly applicable while Article 6(2) of Rome I (which emphasises the consumer's national law) is preserved? Further, given that national laws are preserved there would appear to be two sets of consumer protection for the purposes of Article 6(2) of Rome I: that under the national law and that

¹⁴ Regulation (EC) No 593/2008.

¹⁵ We note the conclusion of the Bar Council of England and Wales that "the Commission not merely should not have chosen Article 114 as the legal basis for this proposal, but cannot do so." (See Bar Council of England and Wales paper "Proposed Common European Sales Law: Preliminary position paper on Legal Basis", 12 January 2012: http://www.barcouncil.org.uk/media/112927/bar_council_of_e_w_preliminary_views_on_cesl_legal_basis_-_january_2012.pdf).

¹⁶ See in particular our responses to questions 1 and 11.

under CESL. According to Article 6(2) of Rome I a choice of law may not "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 on the basis of paragraph 1." So if, to borrow an example from Professor Simon Whittaker¹⁷, French law and CESL are chosen by the parties where the consumer is resident in Germany, the basis on which CESL can extend the "power of the parties to agree to apply the CESL under French law to the designation of the relevant regime of German law for the purposes of Article 6 Rome I" is "... open to considerable doubt". In the case where the parties are silent on national law (and it would be the law of a Member State) and have merely chosen CESL, as has been pointed out by Giesela Rühl¹⁸ (and others), "... the law that would apply in the absence of a choice on the basis of Article 6(1) Rome I-Regulation is clearly not the CESL but the national contract law of the state of the consumer's habitual residence. What is the basis on which CESL overrides the national law?"¹⁹ Finally, in the case where the applicable law would be that of a third state (ie not a Member State) then most commentators are agreed that there is a risk that the default rules under Rome I will designate a law which does not contain CESL.²⁰

A failure to address questions of the correct legal basis properly may lead to challenges before national courts and ultimately the ECJ.

The scope of the Common European Sales Law

4. What are your views on the proposed scope of the draft Regulation, including [the points listed below (a)-(d)]:

Our primary position is that the Commission has not demonstrated a need for CESL at all. Nonetheless, we have sought to respond to the questions posed on scope.

- (a) the kind of transactions it can be used for; sale of goods or digital content and related services?

It should be limited to the sale of goods. The addition of digital content raises complex intellectual property issues since digital content requires a licence where the sale of a physical good does not. Whilst we support the aspirations of Digital Single Market we are concerned that digital content has just been tacked onto CESL at the eleventh hour. Examples of some of the difficulties that may be faced by using CESL for digital content are the inclusion of software and the complex obligation under Article 102 to ensure digital content is cleared of any right or not obviously unfounded claim of a third party. We believe, therefore, that the sale of digital content should be dealt with, if at all, alongside copyright and related rights and not under CESL.

We can see a case for harmonising insurance law across the EU but this does not have to be founded on the adoption of CESL.

- (b) the availability for distance, off-premises and on-premises contracts?

We have no comment.

- (c) the limitation of the draft Regulation to cross-border contracts?

¹⁷ Whittaker, Simon, The Proposed Common European Sales Law: Legal Framework and the Agreement of the Parties (17 February 2012). Modern Law Review, Forthcoming; Oxford Legal Studies Research Paper No. 10/2012. Available at SSRN: <http://ssrn.com/abstract=2006786>.

¹⁸ Rühl, Giesela, The Common European Sales Law: 28th Regime, 2nd Regime or 1st Regime? (19 March 2012). Maastricht Faculty of Law Working Paper. Available at SSRN: <http://ssrn.com/abstract=2025879> or <http://dx.doi.org/10.2139/ssrn.2025879>.

¹⁹ We acknowledge that some, including Simon Whittaker (reference at fn 17 above), believe that in this scenario "the parties' agreement to apply the CESL would take effect under this law without reference to any mandatory provisions in its own '1st contract law regime' [and that] ... therefore, the envisaged avoidance of differences between consumer protection laws in Member States would be achieved." However this disagreement between commentators serves only to highlight the uncertainty.

²⁰ See for example Simon Whittaker (reference at fn 17 above).

This limitation makes sense given the framing of the "problem" by the Commission, namely a lack of cross-border trade. At least initially, we do not think it should be made available for national contracts where national law is more than adequate. However, we do recognise that disputes may arise about whether a contract is within/outside of scope and therefore allowing CESL to apply to national contracts may help reduce the grounds for argument in this particular area.

In any event, overall we consider this issue should be left to Member States.

The fact that CESL is only available for cross-border sales means many internet traders will still need to refer to two contract laws, because for domestic sales it will have to continue to use national law. Many of the efficiencies anticipated by the Commission (and referred to in the Impact Assessment) thus fall away. We also agree with the Law Commission's observation that it is sometimes difficult to identify where an internet trader is habitually resident, therefore making the distinction between cross-border and domestic a difficult one to establish.

- (d) the requirement that at least one party to a business-to-business contract must be a Small [or] Medium Enterprise?

We believe that if CESL is to be introduced it should be limited to business-to-consumer contracts and not extend to business-to-business contracts. First, because we do not consider it necessary (national law is adequate). Secondly, CESL currently contains something akin to consumer protection for SMEs. We do not believe this is appropriate. Businesses (of whatever size) should retain the freedom to be bound by the bargain they strike.

If CESL is made available for business-to-business contracts we believe there are difficulties associated with the current proposal. In particular, how is the non-SME party to judge whether the other party is an SME or not? At what point does this judgment need to be made and what are the consequences of the other party turning out not to be an SME? We note that the Commission has given its view orally on some of these questions but that does not eliminate the concern that, by virtue of a misjudgement as to the character of the other party, a party could be faced with an agreement governed by a law other than the one it intended.

5. The proposed Regulation purports to be a "stand alone" code of contract law rules. Does the proposal achieve this objective? Is there anything currently excluded that ought to be brought into scope or is there anything that ought to be removed?

The list of exclusions in Recital 27 of the proposed Regulation is extensive. Parties choosing CESL will continue to have to address (by choice or default) the question of the national applicable law. There will be several layers of complexities. Parties may need to navigate the interaction between CESL, national law, as well as EU law, to help determine issues as to scope.

Please also see our comments that CESL should not apply to business-to-business contracts.

As we have suggested above, the more proportionate approach to the perceived problem is a set of Commission sanctioned model contract terms based on existing national laws. Alternatively, rather than introducing an entirely new set of contract rules, the Commission might tackle certain identifiable problems in the area of sales. Such an approach is likely to be less disruptive.

The content of the Common European Sales Law

6. Will the proposal, as drafted, provide benefits for businesses, particularly Small Medium Enterprises, wishing to sell to consumers in other Member States? Please give reasons for your answer.

We are not in a position to comment specifically on any claimed benefits to SMEs but for the reasons outlined elsewhere in this response we do not believe that CESL will benefit the majority of our clients.

7. Does the proposal, as drafted, provide an appropriate level of consumer protection? Is it set too low or too high? Are there any particular changes you would like to see made?

We advise businesses (rather than consumers), but make the following general observations. CESL appears to include an inconsistent level of protections for consumers – some very high, whilst others may be considered to be low. For example, provisions such as the ten-year prescription period (Article 179) offer a very high level of protection to consumers (and, such a term will act as a major disincentive to businesses contemplating CESL). On the other hand, the requirement to pay for use (Article 174) would seem to offer a lower level of consumer protection than currently enjoyed.

We also have concerns about the validity of a consumer's choice of CESL (on which we would have to advise businesses when considering whether to contract under CESL with consumers). How is the consumer properly to evaluate whether or not the law of its Member State affords greater or lesser protection than CESL?²¹ As EU law currently stands a consumer must make an "informed choice". To address this CESL seeks to impose various formalities. However, the standard information notice contained in Annex II does not require the provision of a full comparative analysis as to which is the better law (CESL or the relevant national law) and our understanding from oral statements by the Commission is that there is no intention for it to do so. As Simon Whittaker concludes "... as regards consumer contracts, it [CESL] puts far too much reliance on the agreement of the consumer as a justification for their loss of protection as intended by existing EU private international law rules."²² We also have concerns about the complexity of the mechanisms by which a consumer chooses CESL (under Article 8 of the Regulation) and the draconian consequences of getting these wrong (which act as a further disincentive to a business to contracting under CESL).

8. What do you believe will be the impact on UK consumers if the Common European Sales Law is available for cross-border business-to-consumer contracts?

We have no additional comment. Plainly UK consumers (like all others) may lose some hard won protections and certainty.

9. Do you support the approach taken towards digital content in the Common European Sales Law, including the use of a specific digital content category, the scope of digital content covered and the application of rights and remedies that are identical to those for goods? Please give reasons.

No, please see our comments in relation to question 4(a) above.

Impact Assessment

10. What, in your view, would be the impact of the Common European Sales Law? We are interested to hear from all affected sectors; consumers, business, advisory groups and the legal sector.

Introducing CESL will involve training judges, lawyers (private practice and in-house) and law students in the new law. There will be initial training costs and also continuing costs. These costs will fall on businesses whose in-house lawyers will need to be trained, legal firms, barristers, the Government (training of judges and also responsible for some of funding of universities) and law

²¹ Simon Whittaker notes these concerns in his response to the Green Paper:
http://ec.europa.eu/justice/news/consulting_public/0052/contributions/333_en.pdf.

²² Reference at fn 17 above.

students. There would also be costs associated with the amount of business lost while lawyers were training on the new law.

The Impact Assessment²³ does not attempt to estimate these costs. We are aware of the work done in this regard by the Commercial Court Users' Committee and would refer the Ministry of Justice to those submissions.

The Commission indicates that certain public funding may be available for training, however few details have been provided about this. In any event, it appears such funding may be restricted to judges and Government lawyers. It is thought that in the present economic climate these training costs to be met out of public funds may be unwelcome.

We anticipate that there are also likely to be additional costs for businesses in referring issues ultimately to the ECJ in the absence of a body of case law on the meaning of CESL. The Impact Assessment is slightly muddled on this point, stating on the one hand that "The uniform application would be ensured firstly by the ultimate interpretation of the optional Common European Sales Law through the ECJ"²⁴ but, on the other hand that "There may be a limited number of cases which may need to be referred to the ECJ"²⁵. Our view is that at least in the short to medium term, parties may have to make references to the ECJ and that this will result in a significant increase in the caseload of the ECJ and mean further costs and delays in achieving a resolution of disputes.

A further consequence of the introduction of CESL in the business-to-business concept is that standard legal opinions given on transactions governed in whole or part by CESL may be more expensive because the law is new and position more complex and uncertain. Inevitably these legal opinions need to be heavily caveated until a body of case law has been settled.

Businesses will have to adapt their internal policies to cope with an additional legal regime. As the proposal only applies to cross-border contracts, they will be faced with the possibility of an increasingly fragmented position. A business could potentially be contracting under (i) its national law in its domestic agreements, (ii) CESL and national law in cross-border transactions where the parties agree to use it and subject to certain other requirements set out in CESL, (iii) under national law of other Member States and (iv) under the law of a non-EU third party states.

11. Do you believe it would provide the benefits identified in the Commission's Impact Assessment?

No. We are not in a position to provide an in-depth analysis of the Impact Assessment or the survey data. However we make the following observations which suggest there is not the wholesale support for CESL that the Commission asserts.

Impact Assessment (SEC(2011) 1165 final)

We were interviewed as part of the research for the Impact Assessment and have a number of concerns about the process:

- We were interviewed for the Assessment at a time when we were told the draft report *had already been prepared*.
- We note that the Impact Assessment pre-dates CESL in its current form and so was not premised on the detailed proposals now put forward by the Commission.

²³ Footnote 355 to Impact Assessment, p.109.

²⁴ Impact Assessment p.109.

²⁵ Impact Assessment p.110.

- We have been led to believe that the study carried out by IBF International Consulting did not involve interviews with representatives from all Member States.
- No or little credence was given to Option 1 (of the Commission's Green Paper), which was instead portrayed merely as the "do-nothing" base line against which any potential changes under the remaining policy options and the impacts were to be assessed. In accordance with better law-making principles, the need for a comprehensive and broader impact assessment includes that of not taking Union action and focusing on practical issues. The Impact Assessment states "The baseline scenario (BS) would not remove the additional transaction costs or reduce the level of legal complexity for businesses who wish to trade cross-border." The status quo cannot create "additional growth". Further, the status quo cannot remove "additional transaction costs" or reduce complexity. The Commission attributes no value to the baseline scenario. The worry is that the status quo option has not been properly evaluated.
- It is unclear what consideration, if any, was given to the Vienna Convention in this Assessment.
- Many of the questions prejudged the outcome by being premised on there being additional transaction costs and legal uncertainty associated with the status quo.
- The value of lost intra-EU trade as a result of companies giving up cross-border trade due to contract law only is estimated at a range between EUR 26 billion and EUR 184 billion. This is a very wide range indeed. It also seems to assume that *all* cross-border trade will be *additional* trade when it is likely that a significant proportion will be *substitute* trade (so a consumer buys goods from X instead of Y as opposed to buying more goods overall).
- No or insufficient thought was given to whether and why an EU instrument would be more widely adopted than international instruments that are already available to parties to incorporate into their contracts. We agree with the conclusions of Nicole Kornet in her recent paper that "Surveys on the impact of contract law matters on businesses' decisions to engage in cross-border trade do not adequately analyze experiences with the CISG [the Vienna Convention] and the implications thereof for the necessity and likely success of a European sales instrument. Lessons can be learnt from the CISG with respect to businesses' utilization of uniform contract rules. Due to unfamiliarity, high learning costs, routines and substantive concerns businesses often opt out of the default regime."²⁶
- The working assumption was that a single body of rules would remove the need to investigate foreign laws. For the reasons discussed elsewhere it is clear that national and EU law cannot be ignored when choosing CESL.
- The Commission suggests that CESL removes the need for translations and refers in this context to the ability to have recourse to standard terms. This is confusing. As the Law Commission highlights,²⁷ CESL, like the Consumer Rights Directive, leaves the issue of language to the discretion of the Member State. If a Member State wishes, it may require that contractual information is given in a particular language. The use of standard terms is a different point. We support the suggestion of a Commission-blessed form of standard terms for consumer trades to be prepared. This can of course be done without the need to introduce CESL.
- Of the 11 barriers to trade that are identified, it is claimed that four are "contract law related": the difficulty in finding out about the provisions of a foreign contract law; the need to adapt and

²⁶ The Common European Sales Law and the CISG – Complicating or Simplifying the Legal Environment?, Maastricht Faculty of Law Working Paper No. 2012/4, by Nicole Kornet, University of Maastricht.

²⁷ An Optional Common European Sales Law: Advantages and Problems, Advice to the UK Government by the Law Commission and the Scottish Law Commission, November 2011 (http://lawcommission.justice.gov.uk/docs/Common_European_Sales_Law_Advice.pdf) at paragraphs 4.14 to 4.29.

comply with different consumer protection rules in the foreign contract laws; obtaining legal advice on foreign contract law; and problems in resolving cross-border conflicts, including costs of litigation abroad. We do not agree that these are all truly about contract law. For example, the challenges of cross-border conflicts and litigation that can arise whatever the contract law will not be addressed by CESL and, if anything, will be increased by CESL (see further comments above on dispute resolution).

- No account seems to have been taken of the fact that contract law does not appear to pose a barrier to trade with businesses based outside the EU (eg in China).

Eurobarometer 320 on European contract law in business-to-business transactions (EB320)

- The majority – 51% – of respondents claimed that none of the obstacles proffered had any impact on their operations.²⁸ In this context, tax regulations and formalities (eg licensing/registration procedures) were seen as greater potential obstacles than those associated with foreign contract law.
- EB320 acknowledges that "contract law-related problems were typically not standalone issues" and that "Overall, only 3% of the surveyed enterprises cited contract law-related obstacles having at least a minimal impact on their cross-border trading, and at the same time reported no other problems interfering with their ability to carry out transactions with other EU countries."²⁹
- As to the anticipated effects of a single European contract law, EB320 states that "Most enterprises ... felt that the adoption of a single European contract law that could be selected to govern cross-border contracts would not change the volume of their cross-border activities (54%)."³⁰ Overall, in 18 of the 27 Member States, an absolute majority did not expect any increase in their cross-border activities, even if EU contract law would be available for them to choose for international transactions.³¹
- 71% of respondents in the UK said that the prospect of a single European contract law would have no impact on their cross-border operations.³²

Eurobarometer 321 on European contract law in consumer transactions (EB321)

- Most enterprises thought that, even if there was a single European consumer contract law for their international transactions, the volume of their cross-border activities would remain at the current level (49%); the rest could not tell.³³
- As in relation to EB320, in EB321 it is acknowledged that consumer contract law-related problems (to the extent identified) were typically not standalone burdens and "Overall, only 6% of the surveyed enterprises said that consumer contract law-related obstacles had at least a minimal impact on their cross-border trading, and reported no other problems at the same time that interfered with their ability to carry out transactions with other EU countries".³⁴
- Only 7% of respondents said that "the need to adapt and comply with different consumer protection rules in the foreign contract laws" had a "large impact" on companies' decisions to sell cross-border.³⁵ In contrast, when businesses were asked how often they had refused to sell to

²⁸ EB320 p.17.
²⁹ EB320 p.18.
³⁰ EB320 p.33.
³¹ EB320 p.34.
³² EB 320 p.33.
³³ EB321 p.7.
³⁴ EB321 p.21.
³⁵ EB321 p.23.

foreign consumers because of differences in consumer protection rules in the contract laws of other EU countries, an average of 88% of traders responded that this had occurred "never" or "not very often".³⁶

We also note the conclusions of Eric A Posner in his recent paper that "contrary to the general view, the introduction of an optional instrument should increase rather than reduce transaction costs."³⁷ These increased costs arise because each party has to consider not only its national law and the national law of any counterparty, but also CESL and in each transaction determine which is the optimal governing law.

12. Do you have any views on changes that could be made to the proposal to increase its potential benefits for the UK?

Please see our comments in relation to question 1.

PART II: ASSESSING THE COMMISSION'S PROPOSAL: ANNEX I

13. What is your view of the practical utility of the Common European Sales Law, as drafted?
- (a) Do you feel the provisions provide sufficient clarity and legal certainty? If not, why not, and how could the provisions be improved in this regard?
- (b) Is it sufficiently clear whether a provision is or is not mandatory?
- (c) Do you feel that the provisions strike an appropriate balance between considerations of "fairness" when things go wrong, and providing sufficient certainty to contracting parties that what they have agreed will be upheld? If not, how could the provisions be improved?
- (d) Are there any provisions that give rise to particular concerns, and why?

We do not believe that the provisions of CESL provide sufficient clarity and legal certainty. Nor do we believe the correct balance has been struck between fairness and certainty. Further difficulties arise because it is often unclear whether a provision is mandatory or not. We highlight below certain provisions that give rise to concern.

Part I 'Introductory Provisions'

Article 2: Good faith and fair dealing

1. Each party has a duty to act in accordance with good faith and fair dealing.
2. Breach of this duty may preclude the party in breach from exercising or relying on a right, remedy or defence which that party would otherwise have, or may make the party liable for any loss thereby caused to the other party.
3. The parties may not exclude the application of this Article or derogate from or vary its effects.

The introduction of requirements of "good faith" and "fair dealing" may introduce an element of uncertainty into commercial contracts. They are not concepts appropriate to arm's length business dealing, where businesses should be entitled to act in their own interests. Businesses also typically prefer clear rules over general principles since they want to know in a given circumstance that their contract will be binding. Moreover, because CESL is autonomous (Article 4), even in Member States where the concept of good faith is refined, the case law will presumably be of little assistance. This means that such concepts may develop differently to how national law developed. Finally, it is also unclear whether provisions that require good

³⁶ EB321 p.29.

³⁷ Posner, Eric A., *The Questionable Basis of the Common European Sales Law: The Role of an Optional Instrument in Jurisdictional Competition* (May 1, 2012). University of Chicago Institute for Law & Economics Olin Research Paper No. 597. Available at SSRN: <http://ssrn.com/abstract=2049594> or <http://dx.doi.org/10.2139/ssrn.2049594>.

faith and fair dealing can be excluded from business-to-business contracts. Whereas certain specific rules mentioning good faith (eg Article 23) may be excluded, the general principle under Article 2 may not and the consequences of breach under Article 2(2) are severe.

Part II 'Making a binding contract'

Article 23: Duty to disclose information about goods and related services

1. Before the conclusion of a contract for the sale of goods, supply of digital content or provision of related services by a trader to another trader, 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.
2. In determining whether paragraph 1 requires the supplier to disclose any information, regard is to be had to all the circumstances, including:
 - (a) whether the supplier had special expertise;
 - (b) the cost to the supplier of acquiring the relevant information;
 - (c) the ease with which the other trader could have acquired the information by other means;
 - (d) the nature of the information;
 - (e) the likely importance of the information to the other trader; and
 - (f) good commercial practice in the situation concerned.

This appears to reverse the common law rule of caveat emptor by requiring the pre-contract disclosure of "any information concerning the main characteristics of ... goods or services ... which it would be contrary to good faith and fair dealing not to disclose to the other party". Businesses know that they must not misrepresent their products and there exist well understood safeguards under national law but the proposed duty to disclose is likely to have uncertain consequences, particularly when judged with hindsight. With certain limited but important exceptions (eg in the sphere of consumer law), English contract law does not, and should not, intervene in the information exchange that parties are required to undergo. That is a commercial matter that should be left to them. From a practical perspective, despite the guidance in the Article, it remains unclear what the "main characteristics" will be (eg if the buyer and seller have different uses in mind for the goods) and what level of disclosure is required. This provision seems particularly unsuitable for business-to-business contracts.

Article 38: Modified acceptance

1. A reply by the offeree which states or implies additional or different contract terms which materially alter the terms of the offer is a rejection and a new offer.
2. Additional or different contract terms relating, among other things, to the price, payment, quality and quantity of the goods, place and time of delivery, extent of one party's liability to the other or the settlement of disputes are presumed to alter the terms of the offer materially.
3. 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.
4. A reply which states or implies additional or different contract terms is always a rejection of the offer if:
 - (a) the offer expressly limits acceptance to the terms of the offer;
 - (b) the offeror objects to the additional or different terms without undue delay; or
 - (c) the offeree makes the acceptance conditional upon the offeror's assent to the additional or different terms, and the assent does not reach the offeree within a reasonable time.

The concept of modified acceptance is likely to give rise to practical difficulties. How will the parties ascertain whether a suggested alteration is either a material or a non-material addition? While Article 38(2) provides some guidance, it still leaves questions unanswered: what about a change to the seat of an arbitration in a dispute resolution clause or a change to a time period (that does not relate to delivery)?

It is also not clear what a "definite assent" is as compared to a plain "assent".

Article 39: Conflicting standard contract terms

1. 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.
2. Notwithstanding paragraph 1, no contract is concluded if one party:
 - (a) has indicated in advance, explicitly, and not by way of standard contract terms, an intention not to be bound by a contract on the basis of paragraph 1; or
 - (b) without undue delay, informs the other party of such an intention.

CESL introduces the novel concept (to English law) that standard terms become part of the contract to the extent that they are "common in substance", so the contract can become binding even though there is no agreement on the terms which are not common in substance and apparently even if there is no agreement on significant terms of the contract. From an English law perspective, this seems to be a recipe for confusion and an outcome that neither party intended. It is also an example of a provision in CESL which means that it would be the court or tribunal and not the parties that determine the substance of the contract.

Article 51: 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.

This appears to mean that a contract can be avoided if one party was in "economic distress" or had "urgent needs" or is "improvident, ignorant, or inexperienced" and the other party exploits this by "taking an excessive benefit or unfair advantage". To an English lawyer, this appears to mean that, in certain cases, if you advise or educate your clients you might put them at a disadvantage. This suggests there is enormous scope for confusion and uncertainty.

We are concerned that, this provision may not be workable in the business-to-business context.

Part III 'Assessing what is in the contract'

Article 58: General rules on interpretation of contracts

1. 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.
2. Where one party intended an expression used in the contract to have a particular meaning, and at the time of the conclusion of the contract the other party was aware, or could be expected to have been aware, of that intention, the expression is to be interpreted in the way intended by the first party.
3. Unless otherwise provided in paragraphs 1 and 2, the contract is to be interpreted according to the meaning which a reasonable person would give to it.

This provides for interpretation of a contract in accordance with the common intention of the parties and, subject to this, according to the meaning which a reasonable person would give it. This appears to reverse the common law approach of starting with "... the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract ...".³⁸ The test proposed by CESL

³⁸ *Investors Compensation Scheme v West Bromwich Building Society* [1998] 1 WLR 896.

affords greater opportunities to argue over (real or actual) intention. Again, there will be uncertainty over how the courts will apply CESL. It is undesirable for the parties to be bound by a contract which is the result of a judicial interpretation of what the intention is, rather than what the words say.

Article 59: Relevant matters

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;
- (c) the interpretation which has already been given by the parties to expressions which are identical to or similar to those used in the contract;
- (d) usages which would be considered generally applicable by parties in the same situation;
- (e) practices which the parties have established between themselves;
- (f) the meaning commonly given to expressions in the branch of activity concerned;
- (g) the nature and purpose of the contract; and
- (h) good faith and fair dealing.

According to this provision, both preliminary negotiations and subsequent conduct may be taken into account when interpreting a contract. Whilst there can be debate about the extent to which negotiations should be taken into account as an aid to construction, we believe taking account of subsequent conduct to be wrong in principle. The parties' conduct subsequent to the conclusion of the contract would seem to relate to whether the parties have varied the terms of the contract by their conduct rather than adhering to what the contract meant at the time of its conclusion. This is an important distinction, particularly in relation to contracts that confer rights on third parties or where the contract has been assigned by way of security for a financing. We suggest clarifying this.

Prior statements, undertakings or agreements which are not embodied in the document can be excluded under Article 72 but this would not seem to include all negotiations (eg draft agreements).

Articles 58 and 59 appear to mean that a court is required to undertake a wide-ranging (and costly) exploration of the contractual premises and their surroundings from the parties' first discussions about the contract, through market practice, and on to the parties' performance. The parties will never feel confident that what they actually wrote down means what it says. The suggested clarifications would avoid this consequence.

Article 68: Contract terms which may be implied

1. Where it is necessary to provide for a matter which is not explicitly regulated by the agreement of the parties, any usage or practice or any rule of the Common European Sales Law, an additional contract term may be implied, having regard in particular to:
 - (a) the nature and purpose of the contract;
 - (b) the circumstances in which the contract was concluded; and
 - (c) good faith and fair dealing.
2. Any contract term implied under paragraph 1 is, as far as possible, to be such as to give effect to what the parties would probably have agreed, had they provided for the matter.
3. Paragraph 1 does not apply if the parties have deliberately left a matter unregulated, accepting that one or other party would bear the risk.

Under English law the test for implying terms into a contract is one of necessity and not reasonableness. The presumption is that the parties meant what they said. The implication of terms should usually be a matter of last resort. We are concerned that, despite the inclusion of "necessary" in Article 68(1), this will be undermined by the need to have regard to good faith and fair dealing.

Article 69: Contract terms derived from certain pre-contractual statements

1. Where the trader makes a statement before the contract is concluded, either to the other party or publicly, about the characteristics of what is to be supplied by that trader under the contract, the statement is incorporated as a term of the contract unless:
 - (a) the other party was aware, or could be expected to have been aware when the contract was concluded, that the statement was incorrect or could not otherwise be relied on as such a term; or
 - (b) the other party's decision to conclude the contract could not have been influenced by the statement.
2. For the purposes of paragraph 1, a statement made by a person engaged in advertising or marketing for the trader is regarded as being made by the trader.
3. Where the other party is a consumer then, for the purposes of paragraph 1, a public statement made by or on behalf of a producer or other person in earlier links of the chain of transactions leading to the contract is regarded as being made by the trader unless the trader, at the time of conclusion of the contract, did not know and could not be expected to have known of it.
4. In relations between a trader and a consumer the parties may not, to the detriment of the consumer, exclude the application of this Article or derogate from or vary its effects.

This provides that pre-contractual statements about the goods or services (including those in advertising and marketing materials) become terms of the contract (unless excluded). This concept may have unintended consequences. The presumption that the statements are to become part of the contract (as opposed to the onus being on the party relying on the statement). There should be a clarification that not every pre-contractual statement praising the goods or services will become a contractual term.

Article 70: Duty to raise awareness of not individually negotiated contract terms

1. Contract terms supplied by one party and not individually negotiated within the meaning of Article 7 may be invoked against the other party only if the other party was aware of them, or if the party supplying them took reasonable steps to draw the other party's attention to them, before or when the contract was concluded.
2. For the purposes of this Article, in relations between a trader and a consumer contract terms are not sufficiently brought to the consumer's attention by a mere reference to them in a contract document, even if the consumer signs the document.
3. The parties may not exclude the application of this Article or derogate from or vary its effects.

This Article is a further example of where the parties may not be able to rely on the written and agreed terms of the contract. It is unclear how a party is to know that the other party is "aware" of a particular term. Nor is it clear what a party is supposed to do to draw the term in question to the attention of the other party. The test would appear to depend heavily on the particular facts.

Article 73: 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.

To allow the court to determine what the price should have been if the price is not mutually agreed by the parties introduces uncertainty. This would not arise if the court was able to conclude that there is no contract at all since an essential element of the contract is missing.

Article 83: Meaning of "unfair" in contracts between a trader and a consumer

1. In a contract between a trader and a consumer, a contract term supplied by the trader which has not been individually negotiated within the meaning of Article 7 is unfair for the purposes of this Section if it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer, contrary to good faith and fair dealing.
2. When assessing the unfairness of a contract term for the purposes of this Section, regard is to be had to:
 - (a) whether the trader complied with the duty of transparency set out in Article 82;

- (b) the nature of what is to be provided under the contract;
- (c) the circumstances prevailing during the conclusion of the contract;
- (d) to the other contract terms; and
- (e) to the terms of any other contract on which the contract depends.

At least from an English law perspective, it is unclear whether this standard (which provides that terms in business-to-business contracts are unfair, if they are not individually negotiated, significantly disadvantage the other party and grossly deviate from good commercial practice or contrary to good faith and fair dealing) is the same in substance as the test of reasonableness under the UK Unfair Contract Terms Act 1977.

Article 86: Meaning of "unfair" in contracts between traders

1. In a contract between traders, a contract term is unfair for the purposes of this Section only if:
 - (a) it forms part of not individually negotiated terms within the meaning of Article 7; and
 - (b) it is of such a nature that its use grossly deviates from good commercial practice, contrary to good faith and fair dealing.
2. When assessing the unfairness of a contract term for the purposes of this Section, regard is to be had to:
 - (a) the nature of what is to be provided under the contract;
 - (b) the circumstances prevailing during the conclusion of the contract;
 - (c) the other contract terms; and
 - (d) the terms of any other contract on which the contract depends.

It is unclear what "good commercial practice" is and whether that might vary across business sectors or across the EU. Unlike in relation to consumers, there is no "black list" of unfair terms which, as a result, gives the court or tribunal a wide discretion and creates uncertainty.

We reiterate our general objection to the application of consumer concepts to business-to-business transactions.

Part IV 'Obligations and remedies of the parties to a sales contract or a contract for the supply of digital content'

Articles 88 (Excused non-performance) and 89 (Change of circumstances):³⁹

Business-to-business contracts often contain force majeure provisions. They are usually negotiated carefully to avoid uncertainty and any unintended consequences. CESL introduces a general concept of force majeure. Performance is excused "due to an impediment beyond that party's control". The general consequences of this are termination of the contract and no right to damages. Parties are also obliged to renegotiate the contract if there is "an exceptional change of circumstances" – which is likely to be an unattractive concept to businesses. It is very unlikely that a heavily negotiated business-to-business contract would contain such open-ended provisions as these. Again, these provisions give the court or tribunal the power to rewrite the contract (eg Article 89(2)) and, from a practical perspective, this is all supposed to take place in a situation of extreme urgency. From an English law perspective, we would rather not include these Articles.

Article 119: Loss of right to terminate

1. The buyer loses the right to terminate under this Section if notice of termination is not given within a reasonable time from when the right arose or the buyer became, or could be expected to have become, aware of the non-performance, whichever is later.
2. Paragraph 1 does not apply:
 - (a) where the buyer is a consumer; or
 - (b) where no performance at all has been tendered.

³⁹ These are too long to set out in full in here.

Having no time limit on when a consumer may exercise his right to terminate is likely, almost of itself, to dissuade businesses from choosing CESL.

Article 120: Right to reduce price

1. A buyer who accepts a performance not conforming to the contract may reduce the price. The reduction is to be proportionate to the decrease in the value of what was received in performance at the time performance was made compared to the value of what would have been received by a conforming performance.
2. A buyer who is entitled to reduce the price under paragraph 1 and who has already paid a sum exceeding the reduced price may recover the excess from the seller.
3. A buyer who reduces the price cannot also recover damages for the loss thereby compensated but remains entitled to damages for any further loss suffered.

From an English law perspective, it is unclear how in practice a buyer and a seller will agree to a reduction in price in accordance with this provision, where a buyer accepts less than full performance.

Article 132: Requiring performance of buyer's obligations

1. The seller is entitled to recover payment of the price when it is due, and to require performance of any other obligation undertaken by the buyer.
2. Where the buyer has not yet taken over the goods or the digital content and it is clear that the buyer will be unwilling to receive performance, the seller may nonetheless require the buyer to take delivery, and may recover the price, unless the seller could have made a reasonable substitute transaction without significant effort or expense.

From an English law perspective, the move towards specific performance as the default (as opposed to damages) interferes with the parties' freedom of choice and is not suitable in many commercial situations.

Parts VI-VIII 'Damages and interest, restitution and prescription'

CESL does not set out sufficient detail on how damages are to be calculated. As a result, it may take many years before the courts develop the basic principles on damages under CESL.

It is unclear to us what will happen when one of the two periods proposed expires, but the other does not. Also, a ten-year prescription period is likely to be unacceptable to businesses.

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