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An Optional Common European Sales Law: Advantages and Problems

Advice to the UK Government



November 2011

**The Law Commission
and
The Scottish Law Commission**

**AN OPTIONAL COMMON EUROPEAN SALES LAW:
ADVANTAGES AND PROBLEMS**

Advice to the UK Government

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AN OPTIONAL EUROPEAN COMMON SALES LAW: ADVANTAGES AND PROBLEMS

Advice to the UK Government from the Law Commission
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AN OPTIONAL COMMON EUROPEAN SALES LAW: ADVANTAGES AND PROBLEMS

Advice to the UK Government from the Law Commission
and the Scottish Law Commission

SUMMARY

- S.1 On 11 October 2011, the European Commission published a proposal for a “Common European Sales Law” (or CESL),¹ which traders may choose to use to govern their cross-border contracts. It covers the sale of goods, the supply of digital content and some related services.
- S.2 The Law Commission and Scottish Law Commission have been asked to advise the UK Government on the potential advantages and disadvantages of the proposal. Our aim is to promote discussion and debate. The European Commission’s draft is a complex document, which is not always easy to understand. We hope this paper will explain the contents of the proposed Regulation and highlight the policy choices which have been made.
- S.3 To inform the debate, we were keen to publish within a month of the European Commission’s proposal. This means that we have concentrated solely on sales contracts and have not had time to consider the supply of digital content.
- S.4 Effectively, the European Commission has made two separate proposals: one law for traders to use when selling to consumers; and one law for businesses selling to other businesses. The two proposals will operate in different ways, and we look at them separately.

CONSUMER SALES: THE CURRENT LAW²

- S.5 Under the current law, as set out in the Rome I Regulation, a trader which directs its activities to an EU member state must comply with the mandatory consumer protection laws of that state. This may be a problem in internet and other distance selling where traders are dealing with consumers from many different states at once.

¹ European Commission, Proposal for a Regulation on a Common European Sales Law, 11.10.2011, Com (2011) 635 final.

² See Part 2.

- S.6 If an English business merely sets up a website offering items for sale which can be accessed from France (for example), there is no reason why the contract should not be subject to English law. However, if a business “directs” activities to France it must comply with the mandatory provisions of French law. The concept of “directing activities” is fluid and uncertain. If an English website regularly accepts orders from France, and starts to make changes to facilitate those orders, then it risks being found to be directing its activities to France.³ The changes do not need to be large or dramatic. They may include quoting reviews from French customers, or spending money on an internet referencing service in France.
- S.7 Businesses are concerned that at some indefinite point they will tip from operating a website accessible from France to operating a website directed at France. At this stage, the contracts may remain under English law but become subject to the additional mandatory provisions of French law.
- S.8 A mandatory provision is one which may not be excluded by contract. In consumer law, many provisions cannot be excluded, including remedies for non-conformity and unfair terms protection. These provisions are not necessarily very different across member states: many follow the basic structure of the EU Consumer Sales Directive and Unfair Terms Directive. However, these directives are minimum harmonisation measures: member states may add to them. Without legal advice, businesses will probably not be aware of what these additions are.
- S.9 This may discourage businesses from selling across borders. An EU-wide survey asked businesses about the impact of cross-border contract law obstacles. Of the businesses which sold to consumers across borders or were planning to do so, 9% reported that consumer contract law obstacles had a major impact and always or often deterred them from selling cross-border; 23% reported that although these factors had some impact on them, they were “not very often” deterred; and 68% said they were never deterred.⁴

THE PROPOSED SOLUTION

- S.10 Under the proposal, in cross-border sales, the trader could offer to contract under the new system of consumer contract law set out in the CESL.
- S.11 The trader would state that the goods were offered under the CESL and would provide a short information leaflet about it (around a page and a half long). If the consumer explicitly agreed, the law governing the contract would then be the CESL rather than a national system. The CESL would effectively be a separate legal regime which, if chosen, would take precedence over the mandatory rules of domestic law.
- S.12 Traders are unlikely to allow consumers to choose whether to contract under the CESL or their own national law. That would simply add another legal system to the current confusion. Thus consumer choice would usually be limited: either to accept the CESL or not to buy from the trader.

³ See paras 2.21 – 2.27.

IS THE CESL SUITABLE FOR DISTANCE SALES?

- S.13 We think there is a case for a new optional code to cover distance selling across the EU.
- S.14 We are not sure, however, that the current text always strikes the right balance. Distance selling needs its own clear rules, designed around automated processes. The CESL is based on more general contract law principles and we think that it would benefit from greater focus on distance sales. More could be done to clarify when the contract is formed;⁵ the effect of a change of circumstances;⁶ and unfair terms protection.⁷ Provisions on the transfer of property could also usefully be inserted.⁸
- S.15 There are three main problems with the text as currently drafted:
- (1) It is not always easy to understand. It would be a more accessible document if:
 - (a) there were separate codes for business-to-consumer contracts and business-to-business contracts;
 - (b) notes and internal references were provided;
 - (c) it was accompanied by an authoritative guide.
 - (2) From the trader's point of view, the proposal is limited in the following ways:
 - (a) Unless member states exercise an option to extend the CESL to domestic sales, traders must use one contract law system for domestic sales and one for cross-border sales.
 - (b) It is cumbersome to use for telephone sales. This is a problem where traders use both online and telephone methods alongside each other.
 - (c) Traders must still find out about and comply with the linguistic requirements of any member state to which they direct activities.
 - (d) The CESL provides consumers with an extended right to reject, for up to two years from the date the consumer could be expected to be aware of the fault. This may discourage traders from using the CESL at all.

⁴ The Gallup Organization, Flash Eurobarometer No 321, *European contract law in consumer transactions*, accessible at: http://ec.europa.eu/public_opinion/flash/fl_321_en.pdf.

⁵ See paras 4.48 to 4.71.

⁶ See paras 4.105 to 4.111.

⁷ See paras 4.91 to 4.104.

⁸ See paras 4.41 to 4.44.

- (3) From the consumer's point of view,
 - (a) The uncertainty of the provisions on allowance for use may lead to difficult arguments, which disadvantage consumers.
 - (b) The lack of damages for distress and inconvenience may reduce the level of consumer protection in some circumstances.

S.16 We hope these issues can be addressed in the forthcoming EU legislative process on the proposed Regulation.

PROBLEMATIC ISSUES

S.17 Below we list the most problematic issues. These are whether the CESL should be confined to cross-border sales; language; the right to terminate; damages for distress and inconvenience; telephone selling; and doorstep selling.

Should the CESL be confined to cross-border sales?⁹

S.18 Most internet traders wish to use only one system of law for all their sales. If the CESL is confined to cross-border sales, they will need to use two: one for domestic sales, and one for cross-border sales. On the other hand, consumer groups fear that if the CESL may be used domestically, it could undermine consumer protection in member states.

S.19 Article 4 of the proposed Regulation provides that the CESL may be used for cross-border contracts. However, under Article 13, member states may also decide to make the CESL available for domestic sales if they wish. Article 4 defines a "cross-border" sale: the consumer must provide an address in one country (which may be a billing address or delivery address) and the trader must be habitually resident in another country. At least one country must be an EU member state.

S.20 As we discuss in Part 3, it is not always clear where a multi-national internet trader is "habitually resident". We think one needs to look at the operation centre that receives the consumer's agreement to use the CESL, rather than the location of the warehouse that dispatches the goods. But if it is acceptable for a firm based in Luxembourg to use the CESL for its considerable UK trade, why should it be unacceptable for a firm based in Leicester to do the same? If a multi-national retailer based abroad is entitled to use the CESL in the UK while a retailer based in the UK is not, the CESL might become a factor discouraging multi-national traders from basing their internet operations in the UK.

S.21 If the CESL is adopted, and becomes successful, we think the UK Government should consider exercising its option to extend the CESL to domestic distance sales. Unfortunately, under Article 13 of the proposed Regulation, the option would require the CESL to be extended to all consumer sales, not just distance selling. This has the potential to undermine a member state's ability to respond to specific abuses in problematic areas, such as doorstep or other off-premises selling.

⁹ See paras 3.19 to 3.47

Language¹⁰

- S.22 Difficult questions arise about how far traders who sell across the EU should be obliged to translate information into the language of the different states. The CESL, like the Consumer Rights Directive, leaves the issue of language to the discretion of the member state. If a state wishes, it may require that contractual information is given in a particular language. For example, French law currently requires that certain contractual information be in French.
- S.23 Even if an internet trader uses the CESL it must still comply with each member state's linguistic requirements. A small business trading across borders must find out what language requirements are imposed in the 27 member states. Where language requirements exist, it must either comply with them or ensure that it does not direct its activities to that state.
- S.24 This protects consumers. When people are dealing in unfamiliar languages, they will be less able to absorb information. On the other hand, traders wishing to start a pan-European business are unlikely to start by translating their sites into all Community languages. A small British company selling its products abroad will probably start with a site only in English, to test the market, and add a few more languages slowly, over time, as sales start to take off. Linguistic requirements may limit small business start-ups and prove a barrier to trade.

The right to terminate for faulty goods¹¹

The current law

- S.25 The current EU Consumer Sales Directive sets out minimum remedies for faulty goods. The Directive provides a fairly low level of protection. Where goods are faulty, consumers must first ask for a repair or replacement. Consumers are only entitled to rescind the contract if a repair or replacement cannot be provided without unreasonable delay or significant inconvenience. Where consumers do rescind the contract, traders may retain a proportion of the price to allow for the use the consumer has had from the product.
- S.26 Member states may add to this minimum level of protection. In the UK, the consumer also has a long-established "right to reject". The consumer may require the seller to take the goods back and return the price straight away (without first seeking repair or replacement), provided rejection is made within "a reasonable time".
- S.27 In 2009 the two Law Commissions published a report on remedies for faulty goods.¹² We concluded that this right to reject was particularly valuable to consumers. However, we thought that the right should be time-limited: in normal circumstances the consumer should only be able to exercise the right to reject for 30 days following the sale. After 30 days, if the goods proved to be faulty, the consumer should start by seeking a repair or replacement.

¹⁰ See paras 4.14 to 4.29.

¹¹ See paras 4.112 to 4.139.

¹² (2009) Law Commission and Scottish Law Commission, Consumer Remedies for Faulty Goods, Law Com No 317, Scot Law Com No 216.

S.28 We argued that where consumers did reject goods, they should receive their money back in full. Our focus groups with consumers found that the allowance for use was extremely unpopular: consumers felt that no reputable trader should sell them a faulty product, fail to repair it, and then require them to pay for whatever use they may have had from it.

The right to terminate in the CESL

S.29 Under the CESL, consumers have a right to terminate. At first sight, this is similar to the right to reject. The consumer may return the faulty goods and receive their money back, without first asking for a repair or replacement.

S.30 Unlike the UK position, however, this right is not time-limited. At first sight, the only time limit is the prescription period. The consumer must act within two years from the time they knew or could be expected to know of the fault, or within ten years of the sale, if this is a shorter period.

S.31 That said, it is possible that prolonged delay by a consumer may constitute a lack of good faith. Article 2 provides that a consumer who breaches the duty to act in accordance with “good faith and fair dealing” may not be able to exercise a remedy which they would otherwise have under the CESL. A consumer may also have to give an allowance for use, if they were “aware of the ground for avoidance or termination” but delayed taking action, or if “it would be inequitable to allow the recipient the free use” of the goods.

S.32 We are pleased that that the CESL recognises a right to terminate, but we have two concerns about how it operates:

- (1) It is too long. Retailers may be discouraged from using the CESL for fear that such an extended right could be abused.
- (2) It is too uncertain. Consumers and traders need quick, simple solutions to resolve problems. Too much scope for argument may disadvantage the weaker party, who is often the consumer. Under the CESL as currently drafted, there is too much scope to argue over whether the consumer has acted in good faith or should give an allowance for their use of the product.

Damages for distress and inconvenience¹³

S.33 In English and Scots law, damages for distress and inconvenience are allowed only in exceptional circumstances. One exception is where the main purpose of the contract is to provide pleasure or to avoid distress.¹⁴ Damages are also available where the consumer has suffered some physical inconvenience and discomfort, for example where they have been prevented from using their home for a prolonged period.

¹³ See paras 4.140 to 4.147.

¹⁴ See para 4.143. we give the example of a wedding dress that falls apart during the wedding.

- S.34 Under the CESL, damages for “non-economic loss” such as distress and inconvenience are not allowed in any circumstances. This represents a reduction in consumer protection in some cases.

Telephone selling¹⁵

- S.35 As presently drafted, the CESL is difficult to use for quick telephone sales. This may cause difficulties for website traders who use online selling and telephone selling alongside each other.
- S.36 As discussed in Part 5, it may be cumbersome for the trader to send an information notice to the consumer before obtaining agreement to use the CESL. The CESL also includes a provision that a contract concluded by telephone is valid only if the consumer has signed the offer or has sent written consent. We think this provision needs to be looked at again.

Doorstep selling¹⁶

- S.37 Consumers are particularly vulnerable to doorstep selling. Member states need to be able to retain the power to reform their laws to provide consumers with clear, simple remedies. We think that initially the use of the CESL should be confined to distance selling. It should be permitted for off-premises sales only once it has become established.
- S.38 If the CESL were introduced for doorstep selling, further changes would be needed. In particular, Article 50 (on threats) should be clarified to include aggressive practices within the meaning of the Unfair Commercial Practices Directive. We would also welcome a clear remedy where Article 50 is breached; and the inclusion of negotiated terms within unfair terms protection.

BUSINESS TO BUSINESS CONTRACTS

The case for a new system¹⁷

- S.39 At present, for business contracts, the Rome I Regulation allows a free choice of law. Parties to a commercial contract may choose any of the legal systems in the EU, or a national legal system outside the EU (such as New York law).
- S.40 For most businesses within the EU, the default regime for international sales contracts is the UN Convention on Contracts for the International Sale of Goods (CISG), also known as the “Vienna Convention”. This has been ratified by 76 countries, including most EU member states.¹⁸ Where parties have places of business in two different states, and both states have ratified the CISG, the CISG becomes the default regime for international sales of goods contracts. It applies unless the parties expressly choose another regime.

¹⁵ See paras 5.2 to 5.27.

¹⁶ See paras 5.28 to 5.44.

¹⁷ See paras 6.1 to 6.36.

¹⁸ The exceptions are the UK, Malta, Portugal and the Republic of Ireland.

- S.41 For most businesses, contract law is rarely a high priority. The overwhelming majority of contracts simply work. Even when problems arise, most are resolved without recourse to law or lawyers. Where businesses do worry about choice of law, however, they are faced with a confusing array of possibilities.
- S.42 The main problem appears to be that businesses have too much choice. It is difficult for small and medium enterprises to find out about different legal systems, as this usually involves expensive legal advice. Businesses tend to favour their own legal system, making it difficult to negotiate on choice of law with businesses from other states.
- S.43 The CESL would provide another possible choice. If the CESL provides such obvious benefits that everyone would agree to use it without difficult negotiations, it would remove a source of business stress. It is supported by many small business organisations on this basis. On the other hand, if the CESL is just one more choice, it would add to the current complexity.

The content of the CESL¹⁹

- S.44 All systems of commercial contract law must grapple with the tension between certainty and fairness. English and Scots law have a reputation for leaning towards the certainty end of the scale. By contrast, the CESL is firmly towards the fairness end. It sets high standards of good faith and fair dealing and provides many discretionary remedies to a party who has suffered from a lack of good faith.
- S.45 This may protect a weaker party in negotiations – though this is less helpful in an optional regime, where a weaker party may have a choice of law imposed on them. The open ended nature of the discretion may also disadvantage the party least able to litigate.
- S.46 There may be a market for the CESL, but we are unsure whether the market would be sufficiently large or significant for the CESL to develop the critical mass it needs. Those who would most benefit from it are the least likely to use it. Where a weaker party contracts with a stronger party, the choice of law is likely to be dictated by the stronger party.
- S.47 Trade associations drafting standard term contracts may use the CESL as the governing law for the contracts. There may also be interest from small and medium sized enterprises dealing with other small or medium sized enterprises, but those who contract without legal advice are unlikely to give much thought to choice of law. And where they do, they will be naturally risk averse. They will be wary about using an untried legal system, unfamiliar to lawyers and judges alike.

Restrictions on the use of the CESL²⁰

- S.48 Under the proposed Regulation, two restrictions are placed on the use of the CESL. The first is that the CESL could not be chosen by a large business contracting with another large business: at least one business must be a small or medium sized enterprise. We have three concerns about this restriction:

¹⁹ See part 7.

²⁰ See paras 6.37 to 6.65.

- (1) It conflicts with the principle that businesses should be given a free choice of law.
 - (2) We are not sure it is feasible to restrict choice of law without amending the Rome I Regulation.
 - (3) The definition of an SME adds unnecessary complexity to the process.
- S.49 Member states are given the option to remove this restriction, and we think that the UK Government should consider exercising its option.
- S.50 Secondly, the CESL may not be used for “mixed-use” contracts, which include any elements other than the sale of goods, the supply of digital content or the provision of related services. This would make the CESL difficult to use in cases where (for example) one party provides training, or loans, or supplies equipment on hire. This exclusion may cause problems.

Conclusion

- S.51 The CESL offers the parties a free choice – which we welcome. Even if the CESL is hardly ever used, no harm would be done. On the other hand, we are not convinced that developing a CESL for commercial parties should be seen as a priority. We think efforts would be better spent on developing a European code for consumer sales over the internet, where there is stronger evidence that the current variety of contract laws inhibits the single market.

TABLE OF ABBREVIATIONS

Brussels I	Regulation (EC) No 44 of 2001 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CONSLEG:2001R0044:20100514:EN:PDF
CESL	Proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law, COM (2011) 635 final, Annex I. http://ec.europa.eu/justice/contract/files/common_sales_law/regulation_sales_law_en.pdf
CISG	The United Nations Convention on Contracts for the International Sale of Goods 1980. http://www.uncitral.org/pdf/english/texts/sales/cisg/CISG.pdf
CFR	Common Frame of Reference. http://ec.europa.eu/consumers/rights/contract_law_en.htm
CJEU	The Court of Justice of the European Union (referred to as the European Court of Justice in this document).
CRD	EU Directive on Consumer Rights (adopted 10 October 2011). http://register.consilium.europa.eu/pdf/en/11/pe00/pe00026.en11.pdf
CSD	Directive No 44 of 1999 on certain aspects of the sale of consumer goods and associated guarantees. http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31999L0044:EN:HTML
DCFR	Draft Common Frame of Reference: Principles, Definitions and Model Rules of European Private Law, Full Edition: Christian von Bar, Eric Clive (eds), 6 vols, 2009; Outline Edition: Christian von Bar, Eric Clive and Hans Schulte-Nölke (eds), 2009. http://ec.europa.eu/justice/contract/files/european-private-law_en.pdf
ESCP	European Small Claims Procedure. A procedure intended to simplify the process of cross-border litigation of a low monetary value. Discussed in more depth in the Appendix. http://europa.eu/legislation_summaries/consumers/protection_of_consumers/116028_en.htm
Feasibility Study	A work published in May 2011 by the expert group advising the European Commission containing the first draft of what was then known as the “Optional Instrument”: http://ec.europa.eu/justice/contract/files/feasibility_study_final.pdf Further draft rules of contract law were developed. The first working draft was referred to as the 8 July 2011 draft. The second was made public on 6 September 2011 and was entitled “Contract Law, Work in Progress, Version of 19 August 2011”: http://ec.europa.eu/justice/contract/files/feasibility-study_en.pdf

OI	Optional Instrument – depending on context, the forerunner to the proposed Common European Sales Law or a reference to the optionality of this proposal for companies.
Rome I	Regulation (EC) No 593 of 2008 on the law applicable to contractual obligations). http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:177:0006:01:EN:HTML
SME	Small and medium sized enterprise (as defined by Article 7.2 of the proposed Regulation).
TFEU	Treaty on the Functioning of the European Union. http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:0047:0200:en:PDF
UNIDROIT	International Institute for the Unification of Private Law.
UTCCR	Unfair Terms in Consumer Contracts Regulations, SI 1999 No 2083. http://www.legislation.gov.uk/ukxi/1999/2083/contents/made
UTD	Directive No 13 of 1993 on unfair terms in consumer contracts. http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31993L0013:EN:HTML

Note: all URLs specified in this document were accessible as of 8 November 2011.

PART 1

INTRODUCTION

THE PROPOSAL FOR AN OPTIONAL COMMON EUROPEAN SALES LAW

- 1.1 On 11 October 2011, the European Commission published a proposal for a common system of European sales law, which contracting parties could choose to use if they wished.¹ The proposal is aimed at removing the barriers to cross-border trade which may be produced by divergence between different systems of contract law across Europe.
- 1.2 The European Union currently comprises 27 member states. Each EU member state has its own legal system, and some have more than one system. The United Kingdom has three separate systems.² The diversity of contract laws poses challenges for those trading across EU borders and may inhibit free trade within the internal market.
- 1.3 One possible solution is an optional “Common European Sales Law” (CESL). This, it is thought, would benefit two particular groups.
- 1.4 The first group is internet traders, selling across borders to consumers in different member states. At present, under the Rome I Regulation,³ where a business directs its activities to a state, it must abide by that state’s mandatory provisions of consumer protection law.⁴ This means that an internet trader needs to be aware of the mandatory provisions of all the states to which it directs activities. The idea is that traders who choose the CESL will no longer be subject to another state’s mandatory consumer law provisions. The trader will only need to be familiar with the CESL (and, possibly, the law of its home state).⁵ If the CESL offers a high level of consumer protection, consumers will be confident that their rights are protected.

¹ European Commission, Proposal for a Regulation on a Common European Sales Law, , Com (2011) 635 final (11.10.2011).

² England and Wales; Scotland; Northern Ireland. With Welsh devolution a separate Welsh system of law may also develop over time.

³ Explained in Part 2.

⁴ Mandatory provisions are statutory provisions which the parties to a contract cannot disapply.

⁵ In Part 3 we discuss whether the CESL would be confined to cross-border sales or would also be available for use in domestic sales.

- 1.5 The second group is small and medium-sized enterprises (SMEs), who find it difficult to hire specialist lawyers, or to spend many hours researching the contract law of another country. As the EU Justice Commissioner Viviane Reding put it, “time and money are precious commodities that companies – especially small and medium-sized businesses – cannot afford to waste”.⁶ The hope is that if SMEs have the option of using a single pan-European system of contract which fully meets their needs, they will not need to consider other legal systems, thereby saving time and trouble.

OUR TERMS OF REFERENCE

- 1.6 In May 2011, the Law Commission and Scottish Law Commission were asked to advise the UK Government on the advantages and disadvantages of an optional system of European contract law focusing on the sale of goods.
- 1.7 The request was made jointly by the Department for Business, Innovation and Skills and the Ministry of Justice. Our terms of reference were to advise on the potential advantages of and problems with an optional system of European contract law in relation to:
- (1) business-to-consumer contracts, with particular reference to consumer protection and the desirability of combating barriers to trade; and
 - (2) business-to-business contracts, with particular reference to SMEs.
- 1.8 At the same time (May 2011), the European Commission published a “Feasibility Study” to demonstrate what an optional system of European contract law might look like. It contained a draft of a system of contract law principles, focusing on sales contracts and related services (such as installation, maintenance and repair). The document was the basis for what has now become the CESL.
- 1.9 The Commission sought views on the Feasibility Study by 1 July 2011. Following the consultation, the Commission placed two further “working drafts” on its webpage, featuring deletions, re-ordering and some changes of wording, though they were not accompanied by a discussion of the policy issues involved.⁷
- 1.10 The Feasibility Study did not include provisions for the supply of digital content. The decision to include digital content was made later, and provisions were added into the working drafts. We have not had time to consider the provisions on the supply of digital content and we do not address them in this advice.

⁶ Speech, “Opening trade opportunities: from the Hanseatic League to European contract law”, 19 July 2011

⁷ The first working draft was referred to as the 8 July 2011 draft. The second was made public on 6 September 2011, and was entitled “work in progress, version of 19 August 2011”.

THE BACKGROUND TO THE DRAFT CESL

- 1.11 The proposed CESL follows considerable academic and policy work over many years. Here we describe the background to the draft, looking at previous initiatives and the academic project to draft a “Common Frame of Reference” (CFR). We also summarise the European Commission’s 2010 Green Paper on policy options for a European contract law, and the responses to it.

Previous initiatives

- 1.12 Work on common principles of European contract law began 30 years ago. In 1982, the Lando Commission was established to bring together contract law specialists from different member states. Following comparative studies of member states’ contract laws, the Lando Commission published its “Principles of European Contract Law”.⁸ Those principles have already been an influential resource for some east European states when formulating new civil codes.⁹
- 1.13 Over the years there have been several calls from the European Parliament for the harmonisation of contract law. For example, in 1999 the European Parliament and the Council called for measures to harmonise certain aspects of member states’ civil (non-criminal) laws.¹⁰ In July 2001 the European Commission responded by publishing a Communication in which it raised the possibility of a European contract law and undertook to support further research in this area.¹¹
- 1.14 The Commission was keen to improve the existing body of EU law, often referred to as the “*acquis*” (from the French, meaning “that which has been acquired”). EU directives are interpreted against a background of member states’ laws, and this can lead to inconsistencies across the EU.

⁸ Published in three volumes between 1995 and 2003 (the second volume subsuming the content of and so replacing the first).

⁹ Stefan Vogenauer, Professor of Comparative Law, University of Oxford, evidence to the House of Lords’ European Union Committee for its Twelfth Report, European Contract Law: the Draft Common Frame of Reference, in response to question 24: www.publications.parliament.uk/pa/ld200809/ldselect/ldcom/95/8112604.htm.

¹⁰ The European Parliament encouraged work towards a European Code of Private Law, or greater harmonisation of civil law, and the Council, meeting in Tampere in 1999, called for a study on the desirability of harmonising the civil legislation of member states.

¹¹ Communication from the Commission to the Council and the European Parliament on European Contract Law, COM (2001) 398 (11 July 2001).

- 1.15 In 2003 the Commission therefore set out an Action Plan to develop a “Common Frame of Reference”. The Commission argued that, by “establishing common principles and terminology”, it would help in “ensuring greater coherence of existing and future *acquis* in the area of European contract law”.¹² In 2004, the Commission explained in a further Communication that, whilst improving the existing *acquis* should be the principal purpose behind the CFR, it could also provide a basis for an optional system of European contract law.¹³

The Draft Common Frame of Reference

- 1.16 A Joint Network on European Private Law was established to deliver a CFR, with funding from the European Commission. A Draft Common Frame of Reference (DCFR) was published in 2009 with, amongst other things, rules and principles of European contract law derived in a modified form from the Principles of European Contract Law.
- 1.17 The DCFR is an academic text, which has been described as “nothing less than the draft of the central components of a European Civil Code”.¹⁴ It is a substantial document, in six volumes, containing draft articles, commentary and background notes. It is divided into ten books, covering a wide range of subjects, including a book on sales, lease of goods and service contracts.
- 1.18 The DCFR has provided a valuable resource for drafting a CESL. There are many similarities between the DCFR and the European Commission’s proposal. The CESL, however, is much more limited than the DCFR. It only covers contracts for the sale of goods, for the supply of digital content and for related services, where the seller undertakes to perform a service for the buyer in relation to the goods.

The European Commission’s 2010 Green Paper

- 1.19 On 1 July 2010 the European Commission published a “Green Paper ... on policy options for progress towards a European Contract Law for consumers and businesses”.¹⁵ As the title shows, the Commission believed that a new European contract law would be desirable.

¹² Communication from the Commission to the European Parliament and the Council – A more coherent European contract law – an Action Plan, COM (2003) 68 (12 February 2003), p 16.

¹³ Communication from the Commission to the European Parliament and the Council – European Contract Law and the revision of the *acquis*: the way forward, COM (2004) 651 (11 October 2004), pp 5, 8, 9 and Annex II.

¹⁴ *Atiyah’s Sale of Goods* (12th ed, 2010) p 6.

¹⁵ COM (2010) 348.

- 1.20 The Commission argued that the single market was inhibited by the many different national contract laws in the EU and the unavailability of translations. Consumers and SMEs “may be reluctant to engage in cross-border transactions”, thereby hindering cross-border competition.¹⁶ The Commission thought that more must be done to ease cross-border transactions by “making progress in the area of European Contract Law”.¹⁷ It set out seven possible options by which this could be achieved.
- 1.21 Option 4 was an optional instrument of European contract law.¹⁸ The instrument would be introduced into EU law by a regulation. The regulation would:
- insert into the national laws of the 27 Member States a comprehensive and, as much as possible, self-standing set of contract law rules which could be chosen by the parties as the law regulating their contracts.¹⁹
- 1.22 The Commission recognised that this optional, self-standing set of contract law rules would need to be “sufficiently clear to the average user” and provide “legal certainty”. Moreover, to ensure that consumers would be willing to conclude contracts with businesses under the instrument, the Commission stressed that it “would need to offer a manifestly high level of consumer protection”.²⁰
- 1.23 The Commission explained that it had set up an Expert Group “to study the feasibility of a user-friendly instrument of European Contract law”. The Group would “assist the Commission in selecting those parts of the DCFR which are directly or indirectly related to contract law, and in restructuring, revising and supplementing the selected provisions”.²¹ The Commission added that the Expert Group would also “take into consideration other relevant sources in this area, as well as contributions to the present consultation”.²² The Feasibility Study was based on this work.

Responses to the Green Paper

- 1.24 The Green Paper consultation closed on 31 January 2011 and resulted in 320 responses. The subsequent Feasibility Study explains that there was considerable interest in the subject, with many views expressed. It comments that:

¹⁶ COM (2010) 348, p 2.

¹⁷ Above, p 2.

¹⁸ Above, pp 9 and 10.

¹⁹ Above, p 9.

²⁰ Above, p 10.

²¹ Above, p 4. Information about the Group, including minutes of its meetings, can be seen at http://ec.europa.eu/justice/contract/expert-group/index_en.htm.

²² Above, p 4.

The opinions on option 4 (the introduction of an optional instrument) were more varied. Several Member States and a large number of other respondents said they could support an optional instrument, provided that it fulfilled certain conditions (for example: had a high level of consumer protection, a clear and user-friendly nature, was clear about its link with the proposed Consumer Rights Directive and other EU-legislation).

- 1.25 As this paragraph implies, although some member states supported an optional instrument (OI), many did not.

Support for an Optional Instrument

- 1.26 The main benefit put forward for an OI was that it would combat legal fragmentation while still allowing party choice. Estonia argued that the OI “would be suitable for reducing the legal fragmentation in order to enliven the internal market of the European Union”. It added:

The reason why Estonia is supporting this solution the most is that this contract law instrument does not require replacing of the domestic contract law with the European Contract law, i.e. it allows the Member States to preserve their current legal system and legal culture.²³

- 1.27 Luxembourg pointed out that it has a long tradition of cross-border contracts, but the barriers to electronic distance sales posed by legal divergences were becoming more and more visible. It favoured an OI. Although Poland expected a detailed impact assessment before they could reach a definitive conclusion, they appeared in favour of an OI because it would help:

facilitate the development of a common market by eliminating legal barriers and divergences between national legal systems.²⁴

- 1.28 Germany thought that an OI “could be advantageous especially for small and medium-sized enterprises”.²⁵ However they wished to conduct further detailed scrutiny before any final views were reached. The Netherlands also supported the idea, subject to it being shown to be of real benefit to legal practice.

Concerns about an Optional Instrument

- 1.29 Not all member states were convinced that differences in contract law posed a barrier to trade. There were widespread calls for an impact assessment on this issue:

²³ Estonian views, p 2.

²⁴ Reply of the Government of the Republic of Poland, p 2.

²⁵ Reply of the Government of the Federal Republic of Germany, p 5.

[F]or the French delegation, it seems the Commission is essentially proceeding by way of affirmations without producing any empirical evidence to support the assumptions underpinning its argument. **[France]**²⁶

It is important that a thorough problem analysis is undertaken before any overly ambitious project is initiated. The creation of a European contract law instrument is so complicated that there must be clear evidence that national contract law actually causes considerable problems for the internal market. **[Sweden]**²⁷

- 1.30 Even if differences in contract law are a problem, several member states were not convinced that an OI would provide a satisfactory solution. For example:

It does not seem that the capacity of a contract law instrument to induce a real change in this field has been established ... **[Belgium]**²⁸

Even if it is accepted that reducing differences in contract law regimes among Member States would contribute to greater cross-border trade, it is far from self-evident that an optional instrument of the kind proposed would contribute materially to this end. **[Ireland]**²⁹

- 1.31 The Irish Government pointed out that parties to commercial contracts may already use transnational legal systems, including the United Nations Convention on Contracts for the International Sale of Goods, and the UNIDROIT Principles.³⁰ The Republic of Austria echoed this when it said:

International Private Law already provides absolutely appropriate solutions in cases where it is necessary to decide which regime of law should be chosen for the solving of a specific case, when due to the circumstances of the case different national laws may be applicable.³¹

- 1.32 Member states were concerned that an OI would not be sufficiently comprehensive to deal with all the issues involved in a contractual dispute. As the Government of the Republic of Austria said:

²⁶ Our translation of the original French “[P]our la délégation française, il semble que la Commission procède essentiellement par voie d’affirmations mais ne produit aucun résultat d’enquêtes pour soutenir les postulats qui constituent les fondements de son raisonnement.”

²⁷ Swedish Government’s views on the Green Paper, p 2.

²⁸ Answer of the Belgian Delegation to the Green Paper on Contract law, p 1.

²⁹ Response of Ireland, p 5.

³⁰ Above, p 5, referring in particular to the United Nations Convention on Contracts for the International Sale of Goods 1980 (the Vienna Convention), the UNIDROIT Principles of International Commercial Contracts (2nd edn, 2004) and the standard form contracts formulated by trade associations. A similar point was made by the Swedish Government in its response.

³¹ Opinion of the Republic of Austria, p 3.

Another major weakness of an optional instrument lies in the fact that it would not be capable of fully regulating all legal questions in connection with a contractual relationship.... An optional European contract law would unavoidably cause the emergence of significant distortions and contradictions at the interface between this instrument and the complementarily applied national contract law.³²

- 1.33 Several states such as Hungary thought that an OI might be interpreted differently by the courts of member states, leading to uncertainty. Eventually, disputes would be referred to the European Court of Justice, but this would take time. The Swedish Government commented:

Parties must be assured that legal disputes would be resolved uniformly throughout the EU immediately, not in a few decades' time ... The European Court of Justice already has long processing times, to which are often added long processing times in the national courts as well. The business sector cannot wait for years for disputes in such a key area as contract law to be resolved.³³

- 1.34 Finally, some member states were concerned that the OI would be used to evade mandatory consumer protection rules. According to the Czech Republic:

[the] parties opting for [the OI] could in purely domestic situations evade mandatory rules of the [relevant] Member State. This situation would entail [a] reduction in the importance of national regulations.

- 1.35 It is clear that many member states have concerns about the idea of an OI. On the other hand, the desirability of some kind of European contract law was endorsed by the European Parliament. On 8 June 2011 the Parliament, by a large majority,³⁴ acknowledged the need for further progress in the area of European contract law and favoured (amongst other options) an OI to be introduced by way of a regulation for business-to-business and business-to-consumer contracts.³⁵

THE FORM OF THE PROPOSAL

- 1.36 The proposal takes the form of a Regulation some 100 pages long.³⁶ The Regulation itself consists of just 16 articles but it also has two Annexes, the first of which is the CESL itself, which contains a further 186 articles and two appendices. As the proposal is in the form of a regulation rather than a directive, once it has been passed by the appropriate majority it would become part of the domestic law of all member states simultaneously.

³² Above, p 4. This concern was also raised in the Netherlands' response.

³³ The Swedish Government's views on the Green Paper on European contract law, p 6.

³⁴ The votes were 521 in favour, 145 against and 8 abstentions.

³⁵ Resolution of 8 June 2011 available at: <http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P7-TA-2011-0262&format=XML&language=EN>.

³⁶ The proposal is preceded by a short Explanatory Memorandum of about a dozen pages.

- 1.37 The Commission proposes that the Regulation be adopted under Article 114 of the Treaty on the Functioning of the European Union (TFEU). This would mean that no member state could veto the proposal as it could be passed by qualified majority voting. We discuss these issues further in Part 8.

THIS PAPER

- 1.38 A CESL could have an important effect on consumer protection and sales law, and we think it is important to promote debate on the issue as soon as possible. We are therefore publishing this advice within a month of the October 2011 proposal.
- 1.39 In this short time, we have not been able to give a final, considered view on the CESL. Instead, our aim is to promote further discussion and debate. The proposed draft CESL is a dense document which is not always easy to read or understand. We try to explain the contents and highlight the policy choices which have been made. The pressure to publish quickly means however that it has not been possible to consider the effect of the proposal on contracts for the supply of digital content.
- 1.40 We look first at consumer sales contracts (between businesses and consumers) and then at commercial sales contracts between two businesses. We have considered the areas where differences in contract law constitute barriers to trade, asking who would use the CESL and how well the current draft would meet their needs.
- 1.41 Our advice is in seven further Parts. Parts 2 to 5 discuss consumer contracts, Parts 6 and 7 discuss commercial contracts, while Part 8 considers the form of the Regulation and its Treaty Base. The structure is as follows:
- (1) Part 2 describes the current legal regime on cross-border consumer sales, as set out in the Rome I Regulation. It analyses the problems with the current rules, from the point of view of traders and consumers.
 - (2) Part 3 considers how the CESL would take effect in consumer sales contracts, looking at the provisions of the proposed Regulation. The most difficult question is whether the CESL should apply only to cross-border sales or should also be available for domestic sales.
 - (3) Part 4 looks at the CESL itself. It asks how appropriate the provisions would be for consumer internet sales. It considers whether the text is accessible and how it deals with language issues. It then considers each element of the transaction, from pre-contract negotiations and contract formation, through non-conformity and unfair terms, to remedies.
 - (4) Part 5 examines how the CESL would work in other forms of consumer sales contracts, including telephone sales and off-premises sales.

- (5) Part 6 looks at how the CESL would apply in business-to-business contracts. We explain that, under the Rome I Regulation, commercial parties are given a choice of law and this would be another choice available to them. We discuss two restrictions on the use of CESL namely that large businesses could not use the CESL between themselves, and that it would not apply to mixed use contracts.
 - (6) Part 7 focuses on the substance of the CESL, as it applies to commercial contracts. For most businesses selling goods to other businesses across EU borders, the default regime is currently the UN Convention on Contracts for the International Sale of Goods. We start by comparing the two regimes. We then summarise the most distinctive provisions of the CESL. We ask how well these provisions would meet the needs of the SMEs for which it is intended.
 - (7) Part 8 briefly considers the form the proposal takes (as a regulation rather than a directive) and its Treaty Base.
- 1.42 Finally, the Appendix outlines three initiatives to improve the enforcement of contract rights across EU borders. It looks at legal aid, the European Small Claims Procedure and possible revisions to the Brussels I Regulation.

PART 2

CONSUMER CONTRACTS: PROBLEMS WITH THE CURRENT LAW ON CROSS-BORDER SALES

- 2.1 In this Part we give a brief description of the Rome I and Brussels I Regulations, which set out the rules on applicable law and jurisdiction for cross-border contracts within the EU. Consumers are granted special protections. Where a business pursues or directs its activities to the state of a consumer's habitual residence, the consumer is protected by the mandatory rules of the consumer's home state. An understanding of this is essential to appreciate what the proposed Common European Sales Law (CESL) seeks to do for cross-border consumer sales.
- 2.2 We identify the main problems with these rules. For shop sales, it is generally accepted that a retailer should abide by the state's mandatory consumer protection rules. The problems arise for distance sales, especially sales over the internet. If (for example) a Scottish retailer simply accepts online orders from France, it may continue to sell the goods under Scots law. At some indeterminate point, however, it may be said to be "directing" its activities to France. At this point it must abide by the mandatory consumer protection measures of French law. Internet traders who wish to sell goods cross-border are left with uncomfortable choices. They must either pay for legal advice about the national laws of all the states to which they direct activities, or take a gamble and hope that consumers do not complain. Some traders play safe by blocking orders from particular states.
- 2.3 The CESL would address this problem. A trader using the CESL would be exempt from the mandatory consumer protection provisions of other states. As we explain, this is primarily an advantage for businesses rather than for consumers. Consumer groups have expressed concern about allowing businesses to avoid consumer protection measures in this way. Nevertheless, if the CESL provides a sufficiently high level of consumer protection, the advantages for consumers may outweigh the loss of some rights. Consumers would gain access to more websites, with more choices, and more competition.

THE CURRENT LAW

- 2.4 A party seeking a legal resolution to a dispute about a cross-border contract faces three questions:
- (1) What system of law must be used to resolve a dispute under the contract? (The "applicable law" question);
 - (2) Which courts are entitled to resolve the case? (The "jurisdiction" question); and
 - (3) What practical problems will be faced in serving documents and enforcing judgments across borders?

- 2.5 In EU law, the applicable law question is dealt with under Rome I Regulation, and the other two questions are dealt with under the Brussels I Regulation. Below we provide a brief summary of each. We look only at consumer sales contracts – that is, contracts where a business transfers ownership of goods to a consumer in exchange for money. Furthermore, we are only concerned with transactions which take place solely within the EU.

APPLICABLE LAW

- 2.6 The Rome I Regulation (Rome I) sets out the rules governing the law applicable to cross-border contractual obligations.¹ For most contracts, Rome I permits the parties a free choice of law.²
- 2.7 If the parties fail to choose a legal regime, Rome I provides default rules. Normally, a contract for the sale of goods is governed by the law of the country where the seller has its habitual residence.³ If, however, circumstances indicate that the contract is “manifestly more closely connected” with a country different from that of the seller, then the law of that country applies.⁴

Article 6: rules to protect consumers

- 2.8 Article 6 provides specific rules to protect consumers. These rules apply if:
- (1) the business
 - (a) pursues commercial or professional activities in the country where the consumer has his habitual residence, or
 - (b) by any means, directs such activities to that country or to several countries including that country; and
 - (2) the contract falls within the scope of such activities.
- 2.9 In such cases, there are two possibilities:
- (1) the contract is governed by the law of the country where the consumer has his or her habitual residence;⁵ or
 - (2) the contract is governed by the law chosen by the parties.

¹ Regulation No 593/2008.

² Above, art 3.

³ Above, art 4(1)(a).

⁴ Above, art 4(3).

⁵ Above, art 6(1).

- 2.10 In the second case, the consumer is still protected by the mandatory rules of the law of the country of their habitual residence.⁶ A mandatory rule for these purposes means one which the parties may not contract out of (or as Rome I puts it, cannot “be derogated from by agreement”). Most consumer protection measures are mandatory in this sense.
- 2.11 To appreciate the effect of Article 6, one needs to understand two relatively open-ended concepts. The first is what it means for a consumer to be “habitually resident” in a country. The second is what is involved in “pursuing” or “directing activities”. We look at each concept in turn.

“Habitual residence”

- 2.12 Rome I defines the “habitual residence” of a company as the place of its central administration. If, however, the contract is concluded by a branch or agency, then one looks at the place of that branch or agency.⁷ The habitual residence of a natural person acting in the course of business is his or her principal place of business.⁸
- 2.13 The Regulation does not define the consumer’s “habitual residence”. One therefore needs to look at how the concept has been defined in EU case law.⁹
- 2.14 The European Court of Justice provided a definition of “habitual residence” in *Swaddling v Adjudication Officer*,¹⁰ which concerned social security benefits.¹¹ The court described habitual residence as the habitual centre of a person’s interests.¹² It laid down some factors which may have a bearing on this issue:
- (1) the person's family situation;
 - (2) the reasons which have led the person to move;
 - (3) the length and continuity of the person’s residence;
 - (4) where the person is in employment, the stability of that employment; and
 - (5) the person’s intention as it appears from all the circumstances.

⁶ Above, art 6(2).

⁷ Above, art 19(2).

⁸ Above, art 19(1).

⁹ The UK courts have recognised that the term “habitual residence” has an autonomous meaning under EU law, which may differ from the meaning assigned to it under domestic law: see *Marinos v Marinos* [2007] EWHC 3315 (Fam), [2007] 2 FLR 1018.

¹⁰ Case C – 90/97 *Robin Swaddling v Adjudication Officer* [1999] ECR I-1075, [1999] 2 CMLR 679.

¹¹ Peter Stone, “The concept of habitual residence in private international law” 29 (2000) *Anglo-American Law Review* 342, 347; *Dicey, Morris & Collins, The Conflict of Laws* (2006) para 6.127. In case C-497/10 PPU *Mercredi v Chaffe* the ECJ gave a definition of “habitual residence” of children for the purposes of Regulation No 2201/2003.

¹² Case C – 90/97 *Robin Swaddling v Adjudication Officer* [1999] ECR I-1075, [1999] 2 CMLR 679, at [29].

The court held that the duration of the residence is not an intrinsic element of the notion of “habitual residence”.¹³

2.15 Paul Vlas explains that habitual residence refers to:

a country with which a person has the closest bonds, where the centre of his social life is situated. Hence, the habitual residence is factual and depends on the circumstances of the case.¹⁴

2.16 In a world where people move freely across EU borders,¹⁵ consumers often ask internet traders to deliver goods to countries in which they are not habitually resident. Some UK websites are targeted specifically at “expatriate” consumers living in other member states. In these circumstances, the trader cannot be sure whether the consumer remains habitually resident in the UK or has adopted the new country as their social centre. The test is too open-ended and subjective to apply in an automatic way.

“Pursuing” or “directing activities”

2.17 Article 6(1) of Rome I asks whether the business pursues or directs its commercial activities in the country where the consumer has his or her habitual residence. There is considerable debate over what these words mean.

2.18 We know that the phrase must be interpreted consistently with Article 15(1)(c) of the Brussels I Regulation, which deals with issues of jurisdiction.¹⁶ Both Rome I and Brussels I use almost identical words, except that Brussels I refers to the consumer’s “domicile” rather than “habitual residence”. We know too that the provisions must be interpreted in a purposive way, to achieve the objective of the two Regulations. As Recital 13 of Brussels I recognises, “in relation to ... consumer contracts ... the weaker party should be protected by rules of jurisdiction more favourable to his interests”.¹⁷

¹³ Case C – 90/97 *Robin Swaddling v Adjudication Officer* 1999] ECR I-1075, [1999] 2 CMLR 679, at [30].

¹⁴ Ulrich Magnus and Peter Mankowski (eds), “Brussels I Regulation”. *European Commentaries on Private International Law* (2007) Art 59, para 3, p 700. See also Francisco J Garcimartín Alférez, “The Rome I Regulation: Much ado about nothing?” March/April 2008 *The European Legal Forum* pp 1-69.

¹⁵ The ONS estimates suggest that nearly 1.7 million UK residents are nationals of other EU states; meanwhile 1 in 12 UK pensioners live overseas. Office for National Statistics, *National Statistician’s Annual Article on the Population: a demographic review* (December 2009), p 3. An IPPR study estimates that over 760,000 UK citizens live full-time in Spain, around 300,000 in Ireland, around 200,000 in France and around 115,000 in Germany. Institute for Public Policy Research, *Brits Abroad: Mapping the scale and nature of British emigration* (December 2006).

¹⁶ Regulation No 44/2001. See recital 24 of Rome I and more generally recitals 7 and 17.

¹⁷ See also Case C-180/06 *Renate IIsinger v Martin Dreschers* [2009] ECR I-3961 at [41].

“PURSUING” ACTIVITIES

- 2.19 The Rome I Regulation does not define what is meant by “pursuing” activities. However, the concept presupposes the physical presence of the trader in the consumer’s country.¹⁸ The notion seems to include:

suppliers who actually cross a border to carry out commercial activities in the consumer state, those who set up a branch or other establishment there, as well as those who physically carry on business in the consumer’s state by other means such as agents, door-to-door salesmen or other intermediaries.¹⁹

- 2.20 The activity pursued must be conducted in a “continuous and systematic way”, and must involve “a certain minimum of business arrangements”.²⁰

“DIRECTING” ACTIVITIES

- 2.21 This is an ambiguous term. The Rome I Regulation does not define what it means. Clearly, “directing” is wider than “pursuing” and does not require a physical presence.²¹ It covers e-commerce, although it is not limited to it.²²

- 2.22 The European Court of Justice has shed light on the meaning of “directing” in the *Pammer* case.²³ In December 2010 the Grand Chamber delivered a judgment interpreting the notion of “directing” activities in the context of Article 15(1)(c) of Brussels I.

- 2.23 The decision involved two separate cases. In the first case, a consumer domiciled in Austria booked a cruise trip from a company domiciled in Germany. The booking was made online through the website of an intermediary company. The consumer brought proceedings before an Austrian court, and the business argued that the Austrian courts lacked jurisdiction. In the second case, a consumer domiciled in Germany reserved rooms at a hotel run by a company domiciled in Austria. After spending time at the hotel, the consumer refused to pay the bill and the company brought proceedings in Austria. The consumer pleaded that the court lacked jurisdiction.

¹⁸ Paul Cachia, “Consumer contracts in European private international law: the sphere of operation of the consumer contract rules in Brussels I and Rome I Regulations” 2009 *European Law Review* 476, 483; Joakim St Øren, “International jurisdiction over consumer contracts in E-Europe” vol 52, July 2003 *International and Comparative Law Quarterly* 665, 676.

¹⁹ Paul Cachia, “Consumer contracts in European private international law: the sphere of operation of the consumer contract rules in Brussels I and Rome I Regulations” 2009 *European Law Review* 476, at p 482. See also p 489.

²⁰ Joakim St Øren, “International jurisdiction over consumer contracts in E-Europe” vol 52, July 2003 *International and Comparative Law Quarterly* 665, at p 676.

²¹ Above at p 676.

²² Jonathan Hill, *Cross-border consumer contracts*, 2008, para 4.20; Joakim St Øren, “International jurisdiction over consumer contracts in E-Europe” vol 52, July 2003 *International and Comparative Law Quarterly* 665, at 666; Youseph Farah, “Jurisdictional rules applicable to electronic consumer contracts”, 21st *BILETA Conference on Globalisation and Harmonisation in Technology Law* (April 2006), 7.

²³ Joined Cases C – 585/08 and C – 144/09 *Peter Pammer v Reederei Karl Schlüter GmbH 7 Co KG, Hotel Alpenhof GesmbH v Oliver Heller* (7 December 2010) (unreported).

2.24 The Court of Justice held that the main issue was whether, looking at the website and other activities, it was apparent that the business envisaged doing business in another member state:

In order to determine whether a trader whose activity is presented on its website or on that of an intermediary can be considered to be 'directing' its activity to the Member State of the consumer's domicile, ... it should be ascertained whether, before the conclusion of any contract with the consumer, it is apparent from those websites and the trader's overall activity that the trader was envisaging doing business with consumers domiciled in one or more Member States, including the Member State of that consumer's domicile, in the sense that it was minded to conclude a contract with them.²⁴

2.25 The court formulated a list of elements which may provide evidence of the trader's intention to direct commercial activities to the consumer's home state. The list, which is not exhaustive, is as follows.²⁵

- (1) the international nature of the activity;
- (2) mention of itineraries from other Member States for going to the place where the trader is established;
- (3) use of a language or a currency other than the language or currency generally used in the Member State in which the trader is established with the possibility of making and confirming the reservation in that other language;
- (4) mention of telephone numbers with an international code;
- (5) outlay of expenditure on an internet referencing service in order to facilitate access to the trader's site or that of its intermediary by consumers domiciled in other Member States;
- (6) use of a top-level domain name other than that of the Member State in which the trader is established; and
- (7) mention of an international clientele composed of customers domiciled in various Member States.

2.26 The court also explained that:

²⁴ Above at [92]. See also [75].

²⁵ Above at [93].

The mere accessibility of the trader's or the intermediary's website in the Member State in which the consumer is domiciled is insufficient. The same is true of mention of an email address and of other contact details, or of use of a language or a currency which are the language and/or currency generally used in the Member State in which the trader is established.²⁶

- 2.27 This is an important point. The Rome I Regulation does not provide consumers with the mandatory protections of their home state whenever they buy from a website. There is no need for traders to bar access. Traders are only subject to home state mandatory provisions if they do more than simply accept orders, and start to direct activities to the state in question.

THE "SCOPE" OF THE ACTIVITIES

- 2.28 For Article 6(1) of Rome I to apply, the contract must fall within the scope of the activities that the trader pursues in the consumer's country, or directs to that country.²⁷ So if, for example, a French business advertises sofas in the UK, a UK consumer who buys one of its sofas is protected by UK mandatory provisions. If, however, the consumer buys a different piece of furniture which is not advertised in the UK, then it appears that the consumer is not protected by any mandatory provisions which might otherwise apply.²⁸

- 2.29 The contract need not be concluded in the member state where the consumer is habitually resident. Thus a consumer might take advantage of the Article 6 protection if the parties concluded the contract while the consumer was on a trip abroad. For example, if a German consumer buys a digital product from an Italian website while on a short flight transit in Italy, the consumer is protected provided the website is directed at consumers in Germany.²⁹

THE EFFECT ON SHOP SALES

- 2.30 It is worth noting that Article 6(1) applies if the activities are directed at a country. It does not apply if activities are merely directed at residents of a country.

²⁶ Above at [94].

²⁷ Paul Cachia, "Consumer contracts in European private international law: the sphere of operation of the consumer contract rules in Brussels I and Rome I Regulations" 2009 *European Law Review* 476, at p 488.

²⁸ Ulrich Magnus and Peter Mankowski (eds), "Brussels I Regulation", *European Commentaries on Private International Law* (2007) Art 15, para 37, page 318. Øren Joakim ST, "International jurisdiction over consumer contracts in E-Europe", vol 52 July 2003 *International and Comparative Law Quarterly* 665, at 694 and 695.

²⁹ For this example, see Joakim St Øren, "International jurisdiction over consumer contracts in E-Europe", vol 52 July 2003 *International and Comparative Law Quarterly* 665, at 675. See also Paul Cachia, "Consumer contracts in European private international law: the sphere of operation of the consumer contract rules in Brussels I and Rome I Regulations" 2009 *European Law Review* 476 at 486.

- 2.31 Take an example of a “Scots Tartan” shop in the Royal Mile in Edinburgh, targeted at tourists, which prices goods in euros, places signs in German and employs German-speaking shop assistants. We do not think that Article 6(1) applies. Although the shop is directing its activities to those habitually resident in Germany, it is not directing activities to Germany: all the events in question take place in Scotland. Thus the goods can be sold under Scots law, and German mandatory provisions would not apply.
- 2.32 This means that Rome I has little effect on shop sales. As we discuss below, its main impact will be on distance sales.

JURISDICTION

- 2.33 Having decided the applicable law, the next question is jurisdiction: which state’s courts may the parties use to bring proceedings? This is often a contentious issue, as each party will naturally wish to bring proceedings in the courts of its home state. The issue is decided by the Brussels I Regulation³⁰, which replaced the Brussels Convention. It sets out the rules relating to jurisdiction, recognition and enforcement of judgments in cross-border disputes.
- 2.34 The general rule is that a person domiciled in a member state will be sued in the courts of that member state.³¹ However, there are exceptions.
- 2.35 For our purposes, the most important exception is the one for the sale of goods. Article 5(1)(b) states that a defendant may be sued in the member state where, under the contract, the goods were delivered or should have been delivered. In addition, as with Rome I, there are also special provisions to protect consumers. The consumer may take advantage of either provision.
- 2.36 Thus Article 15(1)(c) mirrors the wording of Rome I, and protects consumers:

If they contract with a business which:

- (1) pursues commercial or professional activities in the member state where the consumer is domiciled, or
- (2) by any means directs such activities to that member state or to several member states including that member state; and

the contract falls within the scope of such activities.³²

³⁰ Regulation No 44/2001.

³¹ Above, art 2.

³² Above, art 15(1)(c).

2.37 In such cases a consumer may bring proceedings against a business either in the courts of the member state where the business is domiciled or in the courts where the consumer is domiciled.³³ By contrast, consumers may be sued only in the member state where they are domiciled.³⁴

“Domicile”

2.38 While Rome I talks about “habitual residence”, Brussels I uses the concept of “domicile”. The definition of a consumer’s domicile is not uniform,³⁵ but is a matter for national laws. Under Brussels I, a court must apply its domestic law in deciding whether a party is domiciled in that member state.³⁶ If a party is not domiciled in the member state of the court, then the court will decide whether that party is domiciled in another member state by applying the internal law of that state.³⁷

2.39 In the UK the definition of domicile is set out in the Civil Jurisdiction and Judgments Act 1982. An individual is domiciled in the UK if and only if:

- (1) he or she is resident in the UK; and
- (2) the nature and circumstances of his or her residence indicate a substantial connection with the UK.³⁸

2.40 Brussels I does, however, provide a specific definition of domicile for legal persons. A business is domiciled where it has its statutory seat, or central administration, or principal place of business.³⁹

2.41 Ultimately the question whether a consumer is domiciled in the UK is a question of fact. As with the question of habitual residence, it is to be determined following consideration of all relevant circumstances.

Jurisdiction: conclusion

2.42 The European rules on jurisdiction mean that a consumer with a legal dispute over an internet sales contract is usually able to sue in the courts of the country in which he or she is domiciled. The consumer may do this on two alternative bases:

- (1) the goods were delivered, or should have been delivered, to the consumer’s home state,⁴⁰ or

³³ Above, art 16(1).

³⁴ Above, art 16(2).

³⁵ Ulrich Magnus and Peter Mankowski (eds), Brussels I Regulation. European Commentaries on Private International Law (2007) Art 59; Youseph Farah, Jurisdictional rules applicable to electronic consumer contracts, 21st BILETA Conference on Globalisation and Harmonisation in Technology Law (April 2006), 3.

³⁶ Regulation No 44/2001 of 22 December 2000, art 59(1).

³⁷ Above, art 59(2).

³⁸ Civil Jurisdiction and Judgments Act 1982, s 41(2).

³⁹ Regulation No 44/2001 of 22 December 2000, art 60(1).

- (2) the business directed its activities to the consumer's home state.⁴¹
- 2.43 It is only where the consumer uses a foreign website which is not directed at his or her home state, to have goods delivered to another country, that the right to sue in a local court is lost.
- 2.44 That said, taking action against a foreign defendant is far from easy. The most significant practical problems will be serving documents and enforcing the judgment, as we discuss below.

THE PRACTICAL PROBLEMS

Service of documents

- 2.45 A consumer who sues a foreign business in his or her domestic courts will need to serve the court documents out of the jurisdiction. A court will "stay" (halt) the proceedings unless it can be shown that the defendant business has received the documents in sufficient time to enable it to arrange its defence, or that all necessary steps have been taken to do so.⁴² This may not be easy.
- 2.46 An EU Regulation provides for the transmission and the service of documents between member states through designated transmitting and receiving agencies.⁴³ One problem is that the addressee may refuse to accept a document if it is not written in, or translated into, a language which the addressee understands or the official language of the receiving country.⁴⁴ The applicant bears any costs of translation before the transmission of the document.⁴⁵

Enforcing the judgment

- 2.47 If the defendant business refuses to comply with the judgment, the consumer will need to enforce the judgment. Enforcement is now governed by the Brussels I Regulation.

⁴⁰ Above, art 5(1)(b).

⁴¹ Above, art 15(1)(c).

⁴² Above, art 26(2). See also Ulrich Magnus and Peter Mankowski (eds), "Brussels I Regulation", *European Commentaries on Private International Law* (2007) Art 26, paras 19 to 26, pp 467 to 470.

⁴³ Regulation No 1393/2007, art 2.

⁴⁴ Above, art 8.

⁴⁵ Above, art 5.

- 2.48 A judgment will be enforced in another member state if an interested party makes an application, and a court declares it enforceable.⁴⁶ The procedure for making the application is governed by the law of the country where enforcement is sought.⁴⁷ Usually, the applicant must present a copy of the judgment, a certificate issued by the court which gave the judgment, and (if required) a translation of the documents.⁴⁸
- 2.49 In 2007, a group of German academics published a study of the application of the Brussels I Regulation across the EU.⁴⁹ For declarations of enforceability, they found that the courts tend to require a translation of the foreign decision.⁵⁰ Declarations were then made reasonably quickly, usually within a few days or weeks.⁵¹
- 2.50 The declaration of enforceability is only one step along the path. If the business still refuses to pay, the next step is the enforcement itself, which must be done under the laws and procedures of the member state in which enforcement takes place.
- 2.51 The European Union has taken a series of initiatives to help people in these circumstances, which we summarise in the Appendix. First, Brussels I provides an entitlement to legal aid. Under Article 50, a person who seeks recognition and enforcement of a judgment is entitled to receive legal aid under the law of the member state addressed, if that person received complete or partial legal aid, or exemption from costs, in the member state of origin.⁵²
- 2.52 Secondly, if the value of a claim does not exceed €2,000, the consumer can resort to the European Small Claims Procedure.⁵³ The procedure is designed to be simple. For example, matters are usually dealt with on the papers, so an oral hearing will be held only if necessary.⁵⁴ Importantly, no declaration of enforceability is required to have a judgment enforced in another member state.⁵⁵ The Appendix gives further details of this welcome initiative. Unfortunately, however, it may not (yet) be as well used as it could be.

⁴⁶ Regulation No 44/2001, art 38(1). This procedure is sometimes referred to by its Latin name *exequatur* (literally, "let it be executed").

⁴⁷ Above, art 40(1).

⁴⁸ Above, arts 40(3), 53, 54, 55.

⁴⁹ Burkhard Hess, Thomas Pfeiffer, Peter Schlosser, *Report on the Application of Regulation Brussels I in the Member States*, (2007) Study JLS/C4/2005/03 Ruprecht-Karls-Universität Heidelberg.

⁵⁰ Above, at para 505.

⁵¹ Above, at para 506.

⁵² Regulation No 44/2001, art 50.

⁵³ This came into operation in 2009 through Regulation No 861/2007.

⁵⁴ Regulation No 861/2007, art 5(1).

⁵⁵ Above, art 20.

- 2.53 Thirdly, the European Commission is reviewing the Brussels I Regulation. As part of the consultation it has proposed, in line with the European Small Claims Procedure, to abolish the intermediate procedure for the recognition and enforcement of judgments, with a few exceptions.⁵⁶

PROBLEMS WITH THE CURRENT LAW

- 2.54 It is clear from our brief overview of the current law that cross-border consumer sales carry legal risks for both businesses and consumers. Here we highlight the main problems, first from the point of view of businesses and then from the point of view of consumers.

THE RISKS FOR BUSINESS

- 2.55 The current law does not appear to pose a problem for shop sales. As we have seen, if a shop in Scotland targets sales at German tourists, it is entitled to contract under Scots law. Naturally, if the business opens a branch in Germany, it will need to contract under German law, but most retailers accept that if they establish premises in a country they need to abide by that country's laws. This does not appear to be controversial.
- 2.56 The main problems come with distance selling – particularly distance selling over the internet. Websites may be accessed by anyone: the trader may be dealing with consumers from many different states. There may also be problems when traders trade across borders by telephone and post.

Barring access?

- 2.57 It has been reported that some businesses prevent consumers from accessing their websites because they are concerned about differences in contract law.⁵⁷ The EU Justice Commissioner, Viviane Reding, comments that many companies refuse to offer their products abroad:

You may be aware of this notably if you want to make an online purchase from abroad of certain products and services and if you are a resident here in Belgium, in my home country Luxembourg, in Denmark, in the Baltic States or in Poland. There, you often get the following message on the website of the company: *“Sorry, the product you have requested cannot be purchased by you as you are a non-resident.”*

⁵⁶ See Appendix 1.

⁵⁷ The European Parliament quotes research in which testers attempted to make 10,964 cross-border purchases over the internet: 61% of orders failed, either because the retailer refused to serve the consumer's country or for some other reason. See Communication for the Commission of 22 October 2009 on Cross-Border Business to Consumer e-Commerce in the EU (COM(2009)0557), quoted in European Parliament, *Report on Policy Option for Progress towards a European Contract Law*, Rapporteur Diana Wallis, 18 April 2011, p 14. In the most recent research, it was found that around 9% of businesses declined to trade across borders while 22% declined to deliver to certain countries within the EU. The European Consumer Centres' Network, *Online cross-border mystery shopping – state of the e-union*, September 2011 at p42. http://ec.europa.eu/consumers/ecc/docs/mystery_shopping_report_en.pdf

2.58 The European Commission's explanatory memorandum states that:

When consumers try to place orders with a business from another Member State, they are often faced with the business practice of refusal to sell which is often due to differences in contract law.⁵⁸

2.59 Under Rome I, there is no reason for businesses to bar access. Businesses are only required to comply with the mandatory provisions of the consumer's home state if they direct activities to that state. The *Pammer* case clarifies that "mere accessibility" of the website does not amount to directing activities.⁵⁹ Thus if a Scottish business sets up a website which can be accessed from Germany, there is no reason why the contract should not be subject to Scots law.

2.60 Research conducted by the European Consumer Centres' Network suggests that there may be a variety of practical reasons why businesses do not trade across borders, and thus bar trade with individual countries:

- (1) They do not sell online at all;
- (2) They are unable to deliver to the purchaser's country; or
- (3) They are unable to accept payment from the purchaser, for example because their bank declines payments from that region.⁶⁰

2.61 It is possible that some businesses also bar access because they misunderstand the effect of Rome I. The European Commission and others could usefully give publicity to this point, to remove this misunderstanding.

When does a website "direct activities" to another state?

2.62 The problem is that the concept of "directing activities" is fluid and uncertain. If a Scottish website regularly accepts orders from Germany, and starts to make changes to facilitate those orders, then it risks being found to be directing its activities to Germany. The changes do not need to be large or dramatic. Relevant indications may include:

- (1) a telephone number with an international code;
- (2) a domain name ending in ".com";
- (3) quoting prices in Euros;
- (4) quoting reviews from German customers;
- (5) spending money on an internet referencing service in Germany.⁶¹

⁵⁸ Proposal for a Regulation on a Common European Sales Law, Com (2011) 635 Final, p 4,

⁵⁹ Joined Cases C – 585/08 and C – 144/09 *Peter Pammer v Reederei Karl Schlüter GmbH 7 Co KG, Hotel Alpenhof GesmbH v Oliver Heller* (7 December 2010) (unreported), [94].

⁶⁰ The European Consumer Centres' Network, *Online cross-border mystery shopping – state of the e-union*, September 2011.
http://ec.europa.eu/consumers/ecc/docs/mystery_shopping_report_en.pdf

- 2.63 Businesses are clearly concerned that at some indefinite point they tip over from being a website accessible from Germany to being a website directed at Germany. At this stage, the contracts may remain under Scots law but become subject to the mandatory provisions of German law.
- 2.64 Once the “directing activities” test is met, German mandatory provisions apply even if a consumer habitually resident in Germany placed the order while on holiday in the UK, and asked for the goods to be delivered to a UK friend. The business may not be aware of the consumer’s habitual residence, and may not realise that the contract is subject to provisions of German law.
- 2.65 A mandatory provision is one which may not be excluded by contract. In consumer law, many provisions cannot be excluded, including the definition of non-conformity with the contract, unfair terms provisions and remedies. These provisions are not necessarily very different across member states: many follow the basic structure of the Consumer Sales Directive and Unfair Terms Directive. However, these directives are minimum harmonisation measures: member states may add to them. Without legal advice, the businesses will not be aware of what these additions are.

Other forms of cross-border selling

- 2.66 In some cases, retailers may pursue activities in a member state without establishing premises. A French cheese maker may, for example, open a stall in a Kent Farmer’s market, or sell door-to-door in Maidstone. A German model-maker may attend a science fiction convention in Birmingham. Under Rome I, these businesses must comply with the mandatory consumer protection laws of the UK.
- 2.67 We do not know whether this is a real problem in practice. In Part 3 we consider, briefly, how the CESL would apply to this form of selling.

Jurisdiction

- 2.68 Even if the business does not direct its activities to the consumer’s home state, it still faces the possibility of being sued before the courts of the state into which it agrees to deliver the goods. Non-lawyers rarely distinguish between applicable law and jurisdiction. A small English business, with little access to legal advice, may be concerned about a court hearing in Germany, irrespective of whether the German courts apply German or English law.
- 2.69 The proposed CESL makes no changes to the rules on jurisdiction, though (as discussed above) the European Commission is reviewing Brussels I as part of a separate project.

⁶¹ Joined Cases C – 585/08 and C – 144/09 *Peter Pammer v Reederei Karl Schlüter GmbH 7 Co KG, Hotel Alpenhof GesmbH v Oliver Heller* (7 December 2010) (unreported). See our discussion of this case above at para 2.22 – 2.27

The views of businesses selling cross-border to consumers

- 2.70 Alongside the proposal, the European Commission published the results of an EU-wide survey.⁶² The survey questioning 6,465 businesses who indicated that they either sell to consumers across borders or were planning to do so. Most (92%) were already involved with business to consumer cross-border trade.
- 2.71 Interviewers presented businesses with a list of 11 potential obstacles, and asked if each one had a large impact; some impact; minimal impact; or no impact. Four of these questions were said to relate to contract law, and the results are set out below.

Table 1: The impact of contract-related obstacles on businesses' decisions to sell cross-border to consumers from other EU countries

	Large impact	Some impact	Minimal impact	No impact
Difficulty in finding out about the provisions of a foreign contract law	10%	13%	17%	54%
The need to adapt and comply with different consumer protection rules in the foreign contract laws	7%	13%	18%	54%
Obtaining legal advice on foreign contract laws	8%	11%	16%	58%
Problems in resolving cross-border conflicts, including costs of litigation abroad	8%	11%	15%	58%

Source: Flash Eurobarometer, European contract law in consumer transactions, page 19.

- 2.72 Overall, 55% of businesses reported at least a minimal impact for at least one factor. These businesses were then asked: "How often did these obstacles deter you from conducting cross-border transactions?" Four answers were provided: always; often; not very often; never. The results are shown below – first as a proportion of those who answered the question (the 55%) and then as a proportion of all the businesses in the sample.

Table 2: How often do contract law obstacles deter businesses from conducting B2C cross-border transactions?

	% of those reporting some impact	% of all businesses conducting cross-border sales or with an interest them
Always	2	1
Often	14	8
Not very often	41	23
Never/no impact/don't know	43	68
<i>Total</i>	<i>100%</i>	<i>100%</i>

Source: Flash Eurobarometer, European contract law in consumer transactions, page 28.

⁶² The Gallup Organization, Flash Eurobarometer No 321, *European contract law in consumer transactions*, accessible at: http://ec.europa.eu/justice/newsroom/news/20111011_en.htm.

- 2.73 In other words, out of all the businesses in the study, 9% reported a major impact: that they were always or often deterred; 23% reported that although these factors had some impact on them, they were “not very often” deterred; and 68% said they were never deterred.
- 2.74 A similar picture emerges from the answer to Question 4, which asked businesses “how often have you refused to sell to foreign consumers because of differences in consumer protection rules in the contract laws of other EU countries?” In all, 23% said they had refused to serve a customer, at least occasionally, because of differences in contract laws.
- 2.75 The need to comply with the consumer protection provisions of states to which traders direct activities is clearly an issue for businesses. This is a problem which could usefully be addressed.
- 2.76 On the other hand, it is important not to over-state the problem. The opening paragraph of the European Commission’s document “An optional Common European Sales Law: frequently asked questions” states:
- A new Eurobarometer survey published today has found that 55% of exporting businesses say that differences between contract laws are one of the major obstacles for trading across borders to consumers.⁶³
- 2.77 A more detailed consideration of the survey suggests that 55% of enterprises indicated that at least one of four potential contract law problems presented to them had some – even if minimal – impact on their decision to sell across borders.
- 2.78 Furthermore, it is important to be realistic about the problems that a CESL can solve. As we discuss in Part 3, the CESL is most likely to be used in internet selling. For telephone or market sales, the obligation on traders to provide information sheets and gain explicit agreement is likely to be unduly cumbersome. Finally, the problem of cross-border litigation will not be solved by the proposal for a CESL.

THE RISKS FOR CONSUMERS

- 2.79 Online shopping is increasingly important. It is estimated that 40% of EU consumers already buy goods online. However, only 9% of those shop across borders.⁶⁴
- 2.80 According to the European Consumer Centres’ Network the major barrier to increasing cross-border online sales is consumer perception. The biggest concerns include:
- (1) The risk of fraud (62%);

⁶³ Memo/11/680, Brussels, 11 October 2011.
http://ec.europa.eu/justice/contract/files/common_sales_law/m11_680_en.pdf

⁶⁴ European Commission, *Consumer Conditions Scoreboard – Consumers at home in the single market*, 5th Edn, March 2011 at p 11.
http://ec.europa.eu/consumers/strategy/docs/5th_edition_scoreboard_en.pdf

- (2) Concern about what to do if problems arise in a cross-border sales contract (59%);⁶⁵
 - (3) Potential problems with delivery (49%).⁶⁶
- 2.81 These are more problems of perception than reality. Where consumers have actually shopped across borders, concern reduces.⁶⁷ Moreover, the same study shows that online cross-border sales are no less reliable or troublesome than domestic sales.

Concerns about applicable law

- 2.82 As we have seen, where consumers buy from websites directed to their home state, they do not need to consider foreign laws. They continue to be entitled to the mandatory consumer protection of their home state.
- 2.83 In its introduction to the Feasibility Study, the European Commission gave an example in which a consumer considers buying from a website which is not directed to their home state.

Mrs Korhonen lives in Turku, Finland. Her daughter Taru works in Paris. When returning to Finland, Taru is always shocked by the prices she has to pay for the same products in Turku compared to Paris. For example, clothing and footwear are about 30% more expensive in Finland than in France. Taru tries to encourage her mother to start shopping online and buy products like shoes of her favourite brand from France online ... Her mother however, is sceptical and asks "what if the delivered shoes are of a different size than I ordered? Can I send them back? ... Mrs Korhonen is uncertain if she would have the same rights that she enjoys in Finland and is confident about.

- 2.84 In this example, we assume that the French website has taken no steps to direct its activities to Finland. Mrs Korhonen only visited the site because her daughter told her about it. She would not therefore be protected by the mandatory provisions of Finnish law. Instead, the French website is likely to offer a contract under French law, and this would be binding on her.

⁶⁵ European Commission, *Consumer Conditions Scoreboard – Consumers at home in the single market*, 5th Edn, March 2011 as mentioned in the European Consumer Centres' Network, *Online cross-border mystery shopping – state of the e-union*, September 2011 at p 5. http://ec.europa.eu/consumers/ecc/docs/mystery_shopping_report_en.pdf.

⁶⁶ The European Consumer Centres' Network, *Online cross-border mystery shopping – state of the e-union*, September 2011 at p 5. http://ec.europa.eu/consumers/ecc/docs/mystery_shopping_report_en.pdf

⁶⁷ Above at p 5.

2.85 In fact, Mrs Korhonen need not be too concerned about her basic rights, as EU directives have established minimum standards. Once the Consumer Rights Directive becomes law, for example, she would be entitled to withdraw from the contract within 14 days and receive her money back. Under the Consumer Sales Directive, if the goods proved to be faulty, she would be entitled to a repair or a replacement. But there are differences between member states, particularly over how far the consumer may terminate the contract for faulty goods after the first 14 days without first asking for a repair or replacement. Mrs Korhonen will not be entitled to rely on any specific additions to the minimum rules provided by Finnish law.

Concerns about obtaining redress

2.86 In practice, Mrs Korhonen is more likely to be concerned about the practicalities of obtaining redress. A 2009 report by the European Commission on e-commerce found that:

cross-border enforcement and redress is perceived as a major inhibiting factor. 71% of consumers think that it is harder to resolve problems such as complaints, returns, price reductions, or guarantees when purchasing from providers located in other EU countries.⁶⁸

2.87 Mrs Korhonen will be worried that, if her French is poor, she may not have understood the full details of the product. She will also be concerned about how to make complaints, possibly in French, to the French website, and what to do if they ignore her concerns.

2.88 Under Brussels I, Mrs Korhonen is entitled to use the Finnish courts, provided that she asked for the goods to be delivered to Finland. However, this is likely to be a difficult process. She will have to serve court documents in France, translated into French. She may also need to pay for an expert to give the Finnish courts evidence about French law. And if the business still refuses to pay, she will face the long struggle to enforce the debt.

2.89 These considerable expenses are not justified by a dispute over a pair of shoes worth only €110. Recent research on consumer attitudes across the EU shows that:

the reasons most often given for not complaining about a problem were the amount of money being too small to be concerned about (29%) and a lack of confidence in getting a satisfactory resolution to the problem (27%).⁶⁹

⁶⁸ Commission of the European Communities, Commission Staff Working Document, Report on cross-border e-commerce in the EU, Brussels SEC (2009) 283 final para 5.3 (5/3/2009).

⁶⁹ European Commission, *Consumer attitudes towards cross-border trade and consumer protection*. Flash Eurobarometer (March 2010). The research covered the 12 months before publication.

2.90 Thus very few disputes actually go to court. In England, we have found only three reported cases on cross-border consumer disputes, all for expensive items: works of art, financial services and yachts.⁷⁰ The same paucity of reported cases on cross-border disputes is registered abroad. A 2007 study on the application of Brussels I among member states observed:

published case law of national courts ... is not as frequent as one would be inclined to consider due to the extent of cross-border consumer-direct marketing. Most national reporters state that there is none in their countries.⁷¹

2.91 Only cases involving considerable sums of money end up in court.⁷² In *Pammer v Reederei Karl Schlüter GmbH & Co KG*,⁷³ for example, one consumer had spent around €8,500 on a holiday package.

2.92 When buying from an unknown website, consumers undertake an informal risk assessment. Do the benefits in terms of price and quality outweigh the risks that the retailer will fail to deliver or the product will not be as promised? The more unfamiliar and foreign the website, the greater the potential risks.

2.93 Consumers may make small purchases, where they are prepared to lose the purchase price – or make large purchases where there are significant savings. In the UK, they are also encouraged to buy abroad by the protection offered by section 75 of the Consumer Credit Act 1974, which gives them the right to claim against the credit card company for any breach by the supplier.⁷⁴ In the absence of such protection they will however naturally be cautious.

2.94 We welcome the initiatives set out in the Appendix to help consumers enforce their rights across borders. From the consumer's point of view, these are more important than changes in the applicable law.

An indirect rather than direct benefit

2.95 The Rome I Regulation already protects consumers. Consumers are entitled to the mandatory protections of their home state where a trader directs its activities to their state.

⁷⁰ Jonathan Hill, *Cross-border consumer contracts* (2008), at para 2.55.

⁷¹ Burkhard Hess, Thomas Pfeiffer, Peter Schlosser, *Report on the Application of Regulation Brussels I in the Member States*, (2007) Study JLS/C4/2005/03 Ruprecht-Karls-Universität Heidelberg, para 339.

⁷² Jonathan Hill, *Cross-border consumer contracts* (2008), at para 3.142.

⁷³ Joined Cases C – 585/08 and C – 144/09 *Peter Pammer v Reederei Karl Schlüter GmbH & Co KG, Hotel Alpenhof GesmbH v Oliver Heller* (7 December 2010) (unreported).

⁷⁴ For further discussion of this provision, see Part 4, paras 4.37 to 4.40.

- 2.96 Thus the main benefits of a CESL to consumers would be indirect ones. If more businesses offer goods across borders, consumers would benefit from better access and improved competition. These indirect benefits are important to consumers in smaller member states. In a study quoted by the European Parliament, testers searched for a list of 100 popular products online. It found that at least half the products were not available domestically in 10 states. In 13 states, even where a domestic product was available, a foreign alternative was at least 10% cheaper at least half the time.⁷⁵
- 2.97 Clearly if the CESL is to be acceptable to consumers it needs to provide a high level of consumer protection. But achieving the right level of protection will be difficult: it must not be so high as to dissuade businesses from using the CESL at all. In Part 4 we discuss whether the draft CESL achieves this balance.

CONCLUSION

- 2.98 As we have seen, the Rome I Regulation provides good protection to consumers, but at a cost. Traders who sell to consumers across borders need to find out about foreign contract law and comply with the different consumer protection rules in other countries. In some cases they may need to pay for legal advice about different laws. Around one in ten traders who sell (or wish to sell) across border describe this as a major obstacle, and just over half say that it has at least a minimal impact on them.
- 2.99 We do not think that the need to comply with consumer protection provisions is a problem for shop sales. If a trader takes the decision to establish a shop in a different country, it must comply with foreign laws in all its operations: taking premises, employing staff, paying tax. The need to comply with consumer protection law is a minor issue in comparison. On the other hand, it appears to be a problem for distance sales, where traders are selling to a range of different member states. With the growing importance of internet sales, this issue has come to the fore.
- 2.100 The key feature of the CESL is that it would allow a trader to contract under only one or two systems of law across the whole of the EU, bypassing the mandatory provisions of the consumer's national consumer protection law. The CESL has the potential to extend internet trading across national boundaries in the EU. It will make it easier for businesses to set up pan-EU websites, which start to direct activities to many member states. It therefore has the potential to extend the online internal market and give consumers a greater choice of products.
- 2.101 On the other hand, it is important to look carefully at the details of how the CESL would apply (discussed in Part 3). The UK Government will need to ensure that it does not undermine member states' ability to protect consumers in domestic sales. It is also important that the CESL offers an appropriate level of consumer protection. The level must be high enough to protect consumers, without being so high that it dissuades businesses from using the CESL.

⁷⁵ See Communication for the Commission of 22 October 2009 on *Cross-Border Business to Consumer e-Commerce in the EU* (COM (2009) 0557), quoted in European Parliament, *Report on Policy Option for Progress towards a European Contract Law*, Rapporteur Diana Wallis, 18 April 2011, p 14.

PART 3

CONSUMER CONTRACTS: HOW WOULD THE CESL APPLY?

- 3.1 Here we consider how an optional Common European Sales Law (CESL) would take effect. The European Commission's proposal is in two parts. A proposed Regulation with 16 articles sets out the circumstances in which the CESL may be used. This is followed by Annex 1, with 186 articles, which contains the substance of the CESL.
- 3.2 In this Part we consider the Regulation, looking at how the CESL would apply to business to consumer sales. It is in four sections.
- (1) We start by setting out the central idea. Where the parties agree to use the CESL, a state's mandatory consumer contract protection would not apply. Instead, the CESL consumer protection provisions would apply.
 - (2) We then consider how agreement would be obtained. Article 8 requires a consumer to give explicit agreement to use the CESL, while Article 9 states that the trader must give the consumer an information notice before seeking agreement. This is designed for internet sales, but it presents more of a problem in telephone and face-to-face sales.
 - (3) Article 4 states that the CESL may be used for "cross-border" sales. This may be a problem for cross-border internet traders, who would be required to use two systems of contract law: one for cross-border sales and one for home sales. Internet traders have told us that it would be more convenient to use only one system. We discuss how "cross-border" has been defined, and consider whether the definition would be a factor in encouraging firms to base themselves outside the UK.
 - (4) Article 13 gives member states the option to extend the use of the CESL to all domestic consumer contracts. However, member states would not be permitted to extend the CESL to domestic distance sales only. Therefore if the option were used, the CESL would be available to all traders. This has the potential to undermine a member state's ability to introduce new consumer protection laws going further than CESL.

THE CENTRAL IDEA

- 3.3 Where the parties agree to use the CESL, this will render inapplicable the provisions of Article 6 of Rome I. The CESL will effectively be a separate legal regime which, if chosen, will take precedence over the mandatory rules of any domestic legal system. The Rome I Regulation foreshadows this possibility. The European Commission explains that:

The Common European Sales Law will be a second contract law regime within the national law of each Member State. Where the parties have agreed to use the Common European Sales Law, its rules will be the only national rules applicable for matters falling within its scope. Where a matter falls within the scope of the Common European Sales Law, there is thus no scope for the application of any other national rules.¹

Thus, where the CESL is used, the mandatory provisions of member states' consumer protection law would be disapplied.

- 3.4 This is a benefit to businesses, but consumer groups have expressed concern about it. Consumers would exchange their existing consumer protection systems for a different contract law regime. There would be consumer disadvantage if the CESL protection is less than the existing domestic regime.
- 3.5 The CESL would not affect most forms of consumer protection. It has no effect on service contracts, utility contracts or sales of land. Nor does it affect criminal or regulatory provisions or liability under the law of tort or delict. On the other hand, contracts for the sale of goods are important in consumer law and any proposal for change must be considered carefully.

OBTAINING AGREEMENT

- 3.6 Although the CESL is explained in terms of choice, consumers' choice would be limited: to either accept the CESL or not to buy from the trader. It would make little sense for a trader to allow consumers to choose to contract under the CESL or their own law. That would simply add another legal system to the current confusion.
- 3.7 To provide some protection, however, the consumer must specifically agree to use the CESL. In June 2011, Viviane Reding, the EU Justice Commissioner, suggested that e-commerce websites might display a "blue button" (that is, a clickable icon based on the EU flag). This would be very visible to the consumer and would include the following explanation:

"If you click here, then you contract under European Contract Law, not your national law."

- 3.8 Commissioner Reding commented:

I find this a very good idea, but believe it needs to be complemented by a further measure: a legal requirement to inform the consumer about the most important features of the European Contract Law System in layman's terms.... The objective is clear: the optional instrument can only apply on the basis of a conscious decision by the consumer – and an explicit statement to that effect – that the consumer agrees to contract on the basis of the optional instrument.²

¹ Proposal for a Regulation on a Common European Sales Law, COM (2011) 635 final, Explanatory Memorandum p 6.

² Speech to Conference "Towards a European Contract Law", Leuven. 3 June 2011, p 8.

- 3.9 The proposed Regulation therefore requires the consumer to consent explicitly. Article 8.2 states that:

In relations between a trader and a consumer the agreement on the use of the Common European Sales Law 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. The trader shall provide the consumer with a confirmation of that agreement on a durable medium.

- 3.10 Under Article 9 of the proposed Regulation, the trader is required to provide the consumer with the information notice set out in Annex II. This is around a page and a half long, and is designed to cover the core rights.

Internet sales

- 3.11 The provisions just mentioned are clearly drafted with internet contracts primarily in mind. The information notice will be available on the website, and will include a hyperlink to the 186 articles of the CESL. The consumer will then click a button to indicate assent.
- 3.12 However, explicit agreement becomes more of a problem with telephone and other sales.

Telephone sales

- 3.13 For telephone sales, Article 9.1 suggests that traders should send the consumer the information notice and then obtain the consumer's consent to use the CESL. This is a complex provision with the potential to cause practical difficulties in telephone sales contracts. We explore its effects in detail in Part 5.

Off-premises and other sales

- 3.14 In the Flashbarometer Research quoted in Part 2, 19% of firms said they were engaged in off-premises sales, either door-to-door or through fairs or markets. This was much more common in Latvia and Hungary (where over a third of firms were engaged in off-premises sales), than in the UK (where only 16% of firms mentioned it).
- 3.15 The requirements for information notices and explicit consent could be met in door-step selling, especially for larger items, where it is usual to ask the consumer to sign paperwork. Our concern, based upon our research on consumer redress for unfair commercial practices,³ is that consumers are particularly vulnerable to doorstep selling. In Part 5 we consider whether the CESL provides sufficient protection in these circumstances.

³ Law Commission and Scottish Law Commission, Consumer Redress for Misrepresentation and Aggressive Practices (April 2011) Law Commission Consultation Paper 199 / Scottish Law Commission Discussion Paper 149.

- 3.16 In Part 2 we also gave examples of other forms of cross-premises sales. A French cheese maker may open a stall in a farmer's market, or a German model-maker may attend a science fiction convention in Birmingham. This type of sale has less scope for abuse, but it may be difficult for the trader to comply with Articles 8 and 9.
- 3.17 To use the CESL in a market stall, the market trader would need to hand out information notices to all customers and gain their explicit agreement to use the CESL. The trader must then "provide the consumer with a confirmation of that agreement in a durable medium", presumably handing the customer a till receipt or another slip of paper. It is not absolutely necessary for the trader to retain a record of the agreement, but some traders may feel that they need to do so, for example, recording the name of the consumer with their initials.
- 3.18 This may generate more paperwork than would be justified by a quick cash sale in an open-air market. The trader may find it easier to read a leaflet explaining UK consumer protection law and then take a no-quibble approach to complaints. If there is a problem over market trading across borders, the solution may require further thought.

SHOULD THE CESL ONLY APPLY TO CROSS-BORDER SALES?

- 3.19 One of the most difficult questions is whether the CESL should be limited to cross-border transactions, or whether it should also be available for domestic sales. In June 2011, Commissioner Reding summed up the debate in the following terms:

The Commission will need to decide whether the optional instrument should be only made available for **cross-border transactions**. Or whether it should also apply to **domestic transactions** if chosen by the parties to the contract. Many contributions to the public consultation tell us that it would be unwise to make a distinction between cross-border and domestic transactions as it is the very essence of the single market that both situations are treated alike. Others are urging the Commission to limit the scope of the optional instrument to cross-border contracts in order not to disturb at all national legal systems.⁴

- 3.20 She concluded:

I can understand both camps of this argument, and I will continue to listen to both of them. Perhaps the best solution for the Commission is to choose a middle way: to limit the scope of the optional instrument to cross-border contracts; but to allow Member States to extend the application of the optional instrument also to domestic contracts.⁵

⁴ Speech to the Conference, "Towards a European Contract Law", Leuven, 3 June 2011.

⁵ Above.

- 3.21 Most internet traders wish to use only one system of law for all their sales. If the CESL is confined to cross-border sales, they will need to use two: one for domestic sales, and one for cross-border sales. On the other hand, if the CESL can be used domestically, it could be used to undermine the consumer protections currently available in member states.
- 3.22 The proposed Regulation follows Commissioner Reding's "middle way". Article 4 provides that the CESL may be used for cross-border contracts. However, under Article 13, Member States may decide to make the CESL available for domestic sales if they wish.

The definition of cross-border sales

- 3.23 The main difficulty is defining cross-border sales. Article 4.3 defines a cross-border consumer contract in the following terms:

For the purposes of this Regulation, a contract between a trader and a consumer is a cross-border contract if:

(a) either the address indicated by the consumer, the delivery address for goods or the billing address are located in a country other than the country of the trader's habitual residence; and

(b) at least one of these countries is a Member State.⁶

- 3.24 Thus at least one address provided by the consumer must be in a different member state from the habitual residence of the trader. This leads to difficult questions about where a multi-national internet trader is "habitually resident".
- 3.25 Article 4.4 states that the habitual residence of a company is normally the place of central administration. This term has two competing conceptions in the EU. The first ("the incorporation doctrine") prevails in the UK, Ireland, Denmark and Spain and holds that a company is habitually resident in the country in which it is incorporated, even if the substance of its business is conducted in another country. The second ("the real seat theory") prevails in France, Germany and Italy and seeks to identify where the company has its actual head office or is really undertaking its business.⁷ This issue has been explored by the European Court of Justice in the context of the free movement of businesses, but the court has dealt with each case on its facts.⁸ The issue therefore remains live.
- 3.26 Article 4.4 must be read subject to Article 4.5, which states:

⁶ A contract between England and Scotland would not be a cross-border contract within Regulation 4. However, only one country needs to be a member state. A contract between a US trader and a Scottish consumer would qualify.

⁷ In Germany this will be where fundamental management decisions are put into practice. See Kilian Baelz & Teresa Baldwin "The End of the Real Seat Theory (*Sitztheorie*): the European Court of Justice Decision in *Ueberseering* of 5 November 2002 and its Impact on German and European Company Law" <http://www.germanlawjournal.com/print.php?id=214>. Also Stephen Rammeloo, *Corporations in Private International Law a European Perspective* (2001) Ch 2 and 4.

⁸ For example, Case C-212/97 *Centros Ltd v Erhervs-og Selskabsstyrelsen* [1999] ECR I-1459; Case C-208/00 *Uberseering BV v Nordic Construction Co Baumanagement GmbH* [2002] ECR I-9919, [2005] 1 WLR 315.

Where the contract is concluded in the course of the operations of a branch, agency or any other establishment, the place where the branch, agency or any other establishment is located shall be treated as the place of the trader's habitual residence.

Article 4.5 repeats the substance of Rome I, Art 19(2), but it is an uncertain test, which to date has not been clarified by case law.

3.27 Finally Article 4.6 states:

For the purposes of determining whether a contract is a cross-border contract the relevant point in time is the time of the agreement on the use of the Common European Sales Law.

3.28 This would suggest that the relevant issue for the purposes of 4.5 is not the where "the contract is concluded", but where the agreement to use the CESL is concluded. As we discuss below, the joint effect of these provisions may be quite complicated.

Applying the habitual residence test to internet sales

3.29 The habitual residence test is particularly difficult test to apply to internet contracts, where offers and acceptances may be bounced around cyber-space, through a variety of establishments. It may be helpful to illustrate this point with a hypothetical example. Suppose, for example, a major multi-national internet retailer has:

- (1) A head office in Luxembourg;
- (2) A server in Sweden;
- (3) A major operation in Jersey, which stores data, inputs material and keeps the website up-to-date;
- (4) A warehouse in Swindon, which dispatches goods to the UK market.

3.30 A UK consumer looks at the website, and clicks the blue button. The click is "received" by the Swedish server, and the data is transmitted to Jersey. The consumer then places an offer for the goods, which is transmitted (via Sweden) to Swindon. The Swindon staff dispatch the goods, and send notification confirming dispatch. The dispatch data is monitored in Jersey. Has the contract been concluded "in the course of operations of a branch, agency or other establishment of the retailer" – and if so, which one?

3.31 As we discuss in Part 4, there is an argument that the contract was concluded when the staff in Swindon confirmed dispatch, as this probably constitutes the acceptance required to conclude a contract. This would suggest that "the contract was concluded in the course of the operations" of an establishment in the UK. If so, then the CESL could not apply.

3.32 However, under Article 4.6, the relevant point is not the conclusion of the contract, but when the consumer clicked the blue button. At this point, the Swindon warehouse had not been notified of the sale: the establishment in contact with the consumer was in Jersey. On this basis, the trader was habitually resident outside the UK, and the CESL could be used.

3.33 We think that the UK warehouse is probably irrelevant. A large international trader will deal with warehouses all over the EU. Yet at the time of the agreement to use the CESL it may not have located the relevant warehouse. If the applicability of the CESL were dependent on the location of the warehouse, it would make the system unusable. In this example, we think that the trader would probably be said to be habitually resident in Jersey, but the issue could usefully be clarified.

Problems with the definition of cross-border sales

3.34 There appear to be three problems with a definition of cross-border sales that depends on the habitual residence of the trader.

- (1) It is uncertain and fact-specific.
- (2) The consumer will not know the full intricacies of where the trader's various operations are located.
- (3) An international internet retailer may base their operations where they wish: the availability of the CESL may be one factor influencing their choice of operations. Thus retailers may prefer to base themselves in small jurisdictions (Luxembourg, Jersey) rather than larger jurisdictions. The advantage of Luxembourg is that traders can use the CESL in all EU states except the relatively tiny market of Luxembourg. In Jersey, traders could use the CESL in *all* member states. The provision might thus become a factor discouraging multi-national traders from basing their internet operations in the UK.

3.35 As we discuss below, these problems might be factors encouraging the UK Government to exercise the option to extend the CESL to domestic sales.

Internet platforms

3.36 We have also considered how the definition would apply where a product is sold through an international internet platform, but the goods are supplied by a range of smaller suppliers. Take an example where the platform is a well-known brand which has a place of central administration in Luxembourg, but the supplier is a small firm based in Swindon.

3.37 As before, the UK consumer looks at the website, and clicks the blue button. The data is transmitted to Luxembourg. The consumer then places an offer for the goods, which is transmitted to Swindon. The Swindon staff dispatch the goods, and send notification confirming dispatch.

- 3.38 Despite the superficial similarity in the two arrangements, the result would appear to be different. As the contract is between the Swindon firm and the consumer, the contract would with a UK firm, whose central administration (and indeed only place of establishment) is in Swindon. If so, the CESL could not be used to sell to UK consumers.
- 3.39 If an internet platform were designed around the blue button, the prohibition on using the CESL domestically could possibly discourage traders from allowing small locally-based companies from using the platform. We would suggest that the UK Government consults on this point before agreeing to Article 4.

Why just cross-border sales?

- 3.40 This leads to an obvious question: if it is acceptable for a firm based in Luxembourg to use the CESL for all its considerable UK trade, why should it be unacceptable for a firm based in Leicester to do the same? The logic of the argument drives one to the conclusion that if the Luxembourg firm and the Leicester firm are doing the same sort of business in the same way, they should be given the same choice of contract rules, meaning that the CESL should be available for domestic business-to-consumer sales.

MEMBER STATES' OPTIONS

- 3.41 Under Article 13, member states may extend the CESL to domestic sales. It provides that a member state may decide to make the CESL available where the trader and consumer are in the same state.
- 3.42 This is an all or nothing option. The UK could make the CESL available for all domestic sales (including shop and doorstep sales). This could, however, limit the ability of the UK to introduce new consumer protections into their law. If traders did not wish to abide by any mandatory new rules, they could avoid them by using the CESL instead.
- 3.43 For example, the two Law Commissions have proposed new contract law protections to cover misleading and aggressive selling, particularly on the doorstep.⁹ We found that consumers need much simpler, clearer protection against aggressive practices, such as salespeople who stay for hours, ignoring requests to leave. Vulnerable consumers are easily deterred from claiming their rights by legal uncertainty and complexity. The CESL might permit traders to avoid the new protections. There is also danger that unscrupulous traders could use the CESL simply to avoid consumers exercising their rights under the otherwise applicable domestic law.
- 3.44 We would be concerned if the UK exercised the option to allow all domestic traders to use the CESL. On the other hand, if the final version of the CESL provides an adequate level of consumer protection, there is a case for allowing it to be used in all distance sales. Distance sales are already defined in the Consumer Rights Directive, and that definition is imported into the Regulation in Article 2(p):

⁹ Law Commission and Scottish Law Commission, Consumer Redress for Misrepresentation and Aggressive Practices (April 2011) Law Commission Consultation Paper 199 / Scottish Law Commission Discussion Paper 149.

‘distance contract’ means any contract between the trader and the consumer under an organised distance sales scheme concluded without the simultaneous physical presence of the trader or, in case the trader is a legal person, a natural person representing the trader and the consumer, with the exclusive use of one or more means of distance communication up to and including the time at which the contract is concluded.

- 3.45 Distance selling relies on automated processes and is much less problematic than doorstep or other off-premises selling. As we discuss in Part 4, we think that the CESL could be adapted to meet the needs of internet and other distance selling (such as telephone selling), but this would not necessarily make it suitable for all domestic sales contracts.
- 3.46 We would recommend that the Regulation include an option to extend the CESL to all domestic distance selling, but not to other forms of selling.
- 3.47 There can be no objection to the Regulation containing two options: one option to extend the CESL to distance sales and one option to extend the CESL to all forms of sales (including shop and off-premises sales). We would not, however, advise the UK Government to exercise the second option (to all sales) at present.

CONCLUSION

- 3.48 There needs to be greater clarity about the problem the CESL is addressing. The evidence suggests that the main reason for the CESL is to facilitate distance selling, particularly on the internet. If so, there is an argument for proceeding cautiously and limiting the CESL to distance sales.
- 3.49 There may be arguments why, initially, the CESL should be confined to cross-border sales, but we do not think that the distinction can be maintained in the long term. There is no reason why the form of law should depend on where a trader chooses to place its centre of administration. Member states should not agree to the CESL unless it is considered an acceptable system for all distance consumer sales contracts, including domestic sales. On the other hand, if the CESL were extended to all domestic sales, including shop and off-premises sales, then the CESL would have the potential to undermine a member state’s ability to respond to specific abuses.
- 3.50 Next, in Part 4, we turn our attention to the content of the draft CESL. As the main purpose of the CESL is to facilitate cross-border internet shopping, we focus on how the CESL would affect the specific needs of traders and consumers in internet sales. The effect on other forms of selling is considered in Part 5.

PART 4

THE DRAFT CESL: IS IT APPROPRIATE FOR CONSUMER INTERNET SALES?

INTRODUCTION

- 4.1 In Part 2 we identified internet sales as the main problem area in the current law on cross-border sales. We concluded that for internet sales, an optional sales law has the potential to remove barriers to the internal market by encouraging retailers to provide goods to a greater range of member states. This would offer consumers greater access and choice, and improve competition.
- 4.2 In this Part we consider how the draft Common European Sales Law (CESL) deals with the problems of consumer internet sales. We ask whether it is easy to understand (particularly for non-lawyers); whether it provides clear answers to the main problems of internet shopping; and whether it is set at an appropriate level of consumer protection.
- 4.3 We start with two over-arching issues. The first is whether the text is accessible and user-friendly for non-specialist users. The next is the issue of language: would the trader need to make information available to the consumer in the consumer's language? This would be subject to the requirements imposed by different member states.
- 4.4 The next sections consider the content of the CESL. We start with the essentials of the internet transaction: the trader wishes to get paid, and the consumer wishes to receive the goods. We then consider each element in turn, from pre-contract negotiations and contract formation, through non-conformity and unfair terms, to remedies. Finally we mention two issues which are not included within the draft CESL: transfer of title and illegality rules.
- 4.5 The remedies provisions are particularly important. We are concerned that the extended right to terminate the contract may be unduly onerous on traders. Meanwhile, the exclusion of damages for distress and convenience would reduce consumer protection in some circumstances.

AN ACCESSIBLE, USER-FRIENDLY TEXT?

- 4.6 The European Commission is keen to develop a clear and user-friendly text which can be understood by non-specialists. As the Feasibility Study stated:

The Commission asked the Expert Group to develop a text which would not only be concise, but also be user-friendly, both in its language and structure so it could be understood and used by businesses and consumers who would not necessarily be specialist in the area of contract law.¹

¹ A European contract law for consumers and businesses: Publication of the results of the feasibility study carried out by the Expert Group on European contract law p 6.

- 4.7 This is an important objective. As discussed in Part 2, the overwhelming majority of consumer disputes are resolved without the intervention of lawyers.
- 4.8 The CESL is a long and complex document. As lawyers, we found the document difficult to get to grips with. Many provisions are general principles of contract law. It is not always easy to understand, for example, how the general provisions might apply to internet sales.
- 4.9 We also found the text difficult to navigate. As we discuss below, in order to describe the right to terminate, it is necessary to refer to Articles spread throughout the instrument, including Articles 2, 108, 114, 174 and 179. The joint effect of these articles only becomes clear after several hours of study. We do not think that the average consumer would be able to understand the right to terminate by reading through the text.
- 4.10 One problem is that the draft CESL attempts to cover both business-to-business and business-to-consumer contracts in a single instrument. It would become a shorter, more accessible document if the provisions applying to consumer sales contracts were brought together in a stand-alone code.
- 4.11 Another problem is that the current text does not include any notes to help explain the provisions. We have found some guidance in the commentary to the Draft Common Frame of Reference (DCFR).² However the CESL text is not the same as its DCFR counterparts. The CESL makes no explicit reference to the DCFR, and we are not sure whether the DCFR commentary is intended to have any status in interpreting the CESL provisions. Furthermore, the DCFR is not easily accessible in its annotated version. It is not available online and the full text retails in the UK for £795. Few businesses or consumers will be aware that it exists. It would be helpful if the CESL included its own interpretative notes.
- 4.12 As explained in Part 3, traders will be obliged to provide consumers with an information notice, a page and a half long. Online, this will contain a hyper-link to the text of the CESL. We fear that the information notice is not enough, while the text itself needs elaboration. We would welcome a longer guide, easily available online, which has authoritative status and provides a straightforward explanation of how the CESL applies to internet sales. As we discuss the provisions, we make suggestions on points the guide should contain.
- 4.13 Lacking notes to explain the policy choices which have been made, we fear we may have misunderstood some provisions. For this reason, in the discussion that follows, we sometimes conclude by asking for more clarification, rather than expressing a definitive view.

LANGUAGE

- 4.14 The main problem in selling across borders is language. Difficult questions arise about how far traders who sell across the EU should be obliged to translate information into the language of the different states.

² *Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference (DCFR)*, Volumes I to VI, Oxford University Press (2010).

The linguistic requirements of member states

- 4.15 The Consumer Rights Directive (CRD) leaves the issue of language to the discretion of the member state. Article 6(7), which applies to distance and off-premises contracts, states:

Member States may maintain or introduce in their national law language requirements regarding the contractual information, so as to ensure that such information is easily understood by the consumer.

- 4.16 At present, French law requires that certain contractual information be in French (with an accompanying translation, if desired).³ Under the CRD, member states such as France may maintain these requirements, while others may wish to introduce them. The penalties for failing to comply with linguistic requirements are left to member states to determine. Member states may give consumers private law rights, or the penalties may be a matter of public law, to be enforced by specified bodies.⁴

- 4.17 The question is whether internet traders using the CESL would need to comply with any mandatory linguistic requirements imposed by the consumer protection laws of the member state to which they direct their activities. The answer is to be found in Recital 27, which states that:

All matters of a contractual or non-contractual nature that are not addressed in the Common European Sales Law are governed by the pre-existing rules of the national law.

The Recital goes on to say that this includes not only issues such as capacity, illegality and non-discrimination, but also “the determination of the language of the contract”. Recital 27 does not specifically refer to the language of pre-contract information, but we think this is intended to be included in the general phrase “language of the contract”.

- 4.18 This is an important issue which merits more discussion.

Irreconcilable objectives

- 4.19 There are two irreconcilable objectives. On the one hand, the CESL is designed to provide a high level of consumer protection, based on principles of information and choice. When people are dealing in unfamiliar languages, they will be less able to absorb information.

³ Art 2 of the “Loi Toubon” (Law No 94-665 of 4 August 1994 on the use of the French language) makes the use of French mandatory “for the designation, offer, presentation, instructions for use, and description of the scope and conditions of a warranty of goods, products and services, as well as bills and receipts”. These provisions also apply to any written, spoken, radio or television advertisement.

⁴ See, for example, Consumer Rights Directive, Art 23 and 24.

- 4.20 The Feasibility Study gave the example of Mrs Korhonen, from Finland, who visits a French website. Suppose, for example, that Mrs Korhonen wishes to buy a new printer for her computer. With the help of her daughter and Babel Fish, she may be able to negotiate her way through the basics of the French site, but her understanding may be limited. She may miss the phrase “printer cable not included”; she may not be aware of her right to withdraw; and she will not even attempt to read the legal terms and conditions. She would be better protected if the website were in Finnish.
- 4.21 On the other hand, traders wishing to start a pan-European business are unlikely to start by translating their sites into all Community languages. This would be a substantial investment and they will probably wish to build up gradually. The Feasibility Study gave an example of a small British jewellery company which wishes to trade across Europe. A business like this will probably start with a site only in English, to test the market, and add a few more languages slowly, over time, as sales start to take off. Any requirement to provide translations before starting to trade would limit the number of small business start-ups and prove a substantial barrier to trade.
- 4.22 Linguistic requirements have the potential to impose barriers to the internal market. Take the example of a UK trader specialising in Indian films, which offers a website solely in Hindi and finds a market throughout Europe. Even if the website uses the CESL, it may not direct its activities to France, if France maintains its language laws.
- 4.23 This means that the CESL will not remove all need for traders to comply with different consumer protection rules. Internet traders would still need to be familiar with the linguistic requirements set by member states. In states with linguistic requirements, traders would either need to incur the costs of translation, or take steps to ensure that they do not direct activities to those states. We fear this may undermine many of the benefits of the CESL.

Language issues within the CESL

- 4.24 The CESL itself does not impose any particular language requirements, though the issue of language is often relevant to interpreting its provisions.
- 4.25 For example, under Article 70 a trader may need to take reasonable steps to bring a contract term to the consumer’s attention. Could a trader comply with this requirement if it has not translated the term into the consumer’s own language? Again, under Article 100, the goods must possess the qualities that the buyer reasonably expects. A similar question arises: does one look at the reasonable expectations of a consumer who read and understood the full description, or at the reasonable expectations of a consumer who did not understand the language used? The CESL does not give an answer to these questions.
- 4.26 We think, on balance, that a consumer who uses a website in a foreign language should take the risk that they might misunderstand the details of the product. This issue should however be discussed further and could usefully be clarified in the CESL.

What language must a consumer use when exercising a contractual right?

- 4.27 The final issue is whether a consumer is entitled to use their own language to exercise a contractual right. We think that if a French site takes orders from Finland there is a strong case to say that it should be prepared to receive complaints in Finnish. Article 76 stipulates as follows:

Where the language to be used for communications relating to the contract or the rights or obligations arising from it cannot be otherwise determined, the language to be used is that used for the conclusion of the contract.

- 4.28 This appears to say that if Mrs Korhonen concludes a contract in French and then wishes to exercise a right under it (such as the right to withdraw), she must communicate in French. This may be difficult for her. Furthermore, if Mrs Korhonen takes her dispute to court, she will end up in the Finnish courts. The court may require any relevant documents to be translated into Finnish, including her letter of complaint in (poor) French.
- 4.29 To increase consumer confidence, we think that traders should be required to accept complaints in the official language of the country of delivery. This may add some costs. An English trader, with a website in English selling to Latvia, may need to pay to translate emails received in Latvian. However, this would be much less than the capital investment required to translate the whole website into Latvian.

THE ESSENTIAL OBLIGATIONS

- 4.30 The definition of a consumer sales contract is that a business provides goods to the consumer, and in return the consumer pays money to the business.⁵ Thus the business's main interest is in getting paid; and the consumer's main interest is in receiving the promised goods. All the various legal systems within Europe recognise these two essential obligations and provide legal remedies if they are not met. Although there are legal differences in sales law across the member states, they tend to be minor variations around this central similarity.
- 4.31 Unfortunately, enforcing these obligations is often difficult. It becomes even more difficult where the parties must deal with foreign legal procedures.

⁵ Article 2(k) of the proposed Regulation defines a "sales contract" as "any contract under which a business transfers or undertakes transfer the ownership of goods to another person (the buyer), and the buyer undertakes to pay the price".

Getting paid

- 4.32 If the business is not paid, it must sue for its debt in the consumer's home state. It must be able to deal with a foreign legal system and enforcement procedures, and it takes the risk that the consumer may become bankrupt or be given other forms of legal protection against creditors. In practice, the vast majority of cross-border internet traders demand payment in advance – and will continue to do so, even under the CESL. For this reason we do not address the provisions on recovering payment in Article 132 or on interest on late payment in Articles 166 and 167.
- 4.33 There is also a market for selling internet goods on credit. The CESL, however, is not intended to apply to credit sales. Article 6.2 of the main Regulation states that the CESL may not be used for consumer contracts where the trader grants or promises to grant credit. This would not however prevent consumers from buying goods from an internet provider through a credit card, where the credit is not provided by the trader. We are not sure whether Article 6.2 also prevents traders from using the CESL where the trader arranges for the consumer to be given credit from a third party through a "linked credit" arrangement. We would welcome further clarification of this point.

Receiving the promised goods

- 4.34 A consumer who pays for goods in advance runs the risk that the goods will not be delivered, or if they are delivered, will not be as promised. Consumers therefore have the opposite problem. They must sue to enforce the obligation to deliver or for return of the contract price. As we saw in Part 2, consumers will usually be able to sue the business in their home state, but this is just the first step in a three-step process. They must next apply for a declaration of enforceability, and then use the procedures in the business's home state to enforce the debt. In Appendix 1 we describe the steps being taken to simplify this process.
- 4.35 In both domestic and cross-border sales, consumers run the risk that the business will become insolvent before the goods are delivered. The CESL does not deal with insolvency, so the priority given to the consumer's debt will continue to be governed by the law of the business's home state. Often consumers are given relatively little protection: they may rank as general creditors, below the claims of the tax authorities, employees or secured creditors such as banks.
- 4.36 These problems cannot be solved by a system of contract law. The risk of insolvency is not an argument against the CESL, but we think it is an argument for not over-selling the CESL. If there is to be a standard information notice, it may be worth mentioning that where the trader becomes insolvent, the issue will be dealt with by the law of the trader's home state. Otherwise the first major cross-border trader insolvency could provoke a reaction against the CESL and lead consumers to lose confidence in the concept.

Rights against the credit card company

- 4.37 In the UK context, consumers' main protection in buying abroad is provided by section 75 of the Consumer Credit Act 1974. This provides that where a consumer buys goods worth between £100 and £30,000 on a credit card, the consumer has a claim against the credit card company for any breach of contract or misrepresentation by the supplier.⁶ In *OFT v Lloyds TSB Bank*,⁷ the House of Lords confirmed that this applies to transactions governed by foreign law.
- 4.38 From the consumer's point of view, section 75 is an extremely valuable right. So long as the goods are within the price range, the UK consumer may make a cross-border purchase using a credit card, knowing that if the goods are not delivered, or turn out to be faulty, they have a claim against the credit card company, in the UK courts. This may partially explain why UK consumers are particularly confident internet users.⁸
- 4.39 Under EU law, consumers have a right which is similar to section 75, but more limited. Article 15 of the Consumer Credit Directive 2008⁹ gives consumers the right to claim against a creditor, but in more restricted circumstances. Currently, Article 15 is limited to "linked credit agreements", which does not extend to credit cards. Moreover, Article 15 allows a consumer to pursue the creditor only if they have first sought remedies against the supplier and failed. Extending Article 15 to include credit cards would be a powerful way of increasing consumer confidence across the EU, though we acknowledge that it would be controversial.
- 4.40 Meanwhile, in a UK context, consumer confidence would be increased if greater publicity were given to section 75. It would be useful to include details of section 75 in the UK version of the information notice, highlighting that section 75 applies to transactions governed by the CESL.

Ownership of segregated goods

- 4.41 There is one way in which the CESL could provide greater protection against trader insolvency. As a general principle, goods stored in the trader's warehouse will be considered to be the trader's property. However, questions arise about goods which have been packed and labelled with the consumer's address. At the moment of insolvency they may be waiting in the post-room or on the way to the consumer in the delivery van. This is not generally a problem with shop sales, where consumers rarely pay in advance, but it is a particular issue for internet sales.

⁶ The same provisions would also apply against any other "connected lender".

⁷ [2007] UKHL 48, [2008] 1 AC 316.

⁸ European Commission, *Consumer attitudes towards cross-border trade and consumer protection. Summary*. Flash Eurobarometer (March 2011) p 10.

⁹ Council Directive 2008/48/EC of 23 April 2008.

- 4.42 In the laws of the UK this issue is dealt with not through insolvency law but through sales law. Section 18 of the Sale of Goods Act 1979 sets out five default rules to say when property passes to the buyer, in the absence of a contrary intention. For distance sales, the relevant rule is Rule 5, which deals with “unascertained goods”. Property passes when goods are unconditionally appropriated to the contract, that is, when the seller “commits” the goods to the contract. The exact meaning of this is not as clear as it should be. It is generally not sufficient to label the goods with the consumer’s address, but it would be sufficient to hand them to the courier if the trader could not require their return.¹⁰
- 4.43 Even if the CESL does not deal with the passing of property generally, we think that a code designed to provide internet consumers with a high level of protection could usefully include a specific provision on this issue. This because internet shoppers are particularly vulnerable to trader insolvency. They pay in advance and take the risk that the goods will never be delivered.
- 4.44 We recommend that the CESL should include a specific consumer protection measure to protect consumers who have paid for goods which have not been delivered. Ideally, we think that the protection should go further than section 18 of the UK Sale of Goods Act 1979: property in the goods should pass as soon as the goods are labelled. This would mean that if a UK trader using the CESL becomes insolvent and, at that moment, its delivery van has reached the Polish border, the driver can continue to deliver the goods to the Polish consumers, rather than returning them to the UK. Labelled goods still in the business’s warehouse would be handed to the courier for onward delivery.¹¹

PRE-CONTRACT INFORMATION AND THE CONSUMER RIGHTS DIRECTIVE

- 4.45 On 23 June 2011, the European Parliament adopted the CRD, which focuses on distance and off-premises contracts.¹² The measure is fully harmonised. As Article 4 clarifies, member states can only depart from it to the extent allowed by the Directive.
- 4.46 The CRD focuses on three elements.
- (1) *Information requirements.* Internet traders must include the listed information, which includes, for example, the trader’s address and telephone number, the main characteristics of the goods, the price (including taxes), any delivery charge and a reminder of the law requiring goods to conform to contract.

¹⁰ See *Carlos Federspiel & Co SA v Charles Twigg & Co. Ltd.* [1957] 1 Lloyd’s Rep 240 and *Hendy Lennox (Industrial Engines) Ltd v Grahame Puttick Ltd* [1984] 1 WLR 485. *Hayman v McLintock* (1907 SC 936, (1907) SLT 63) is the classic Scottish case on the subject.

¹¹ Note that property may pass earlier than risk passes. The CESL follows the Consumer Rights Directive in stating that risk should pass on delivery. In the UK, s 20(4) Sale of Goods Act 1979 provides that risk only passes to the consumer when the goods are delivered,

¹² The CRD must be implemented by member states by the end of 2013.

- (2) *A right of withdrawal.* Consumers must be told that they may withdraw from the contract within 14 days, returning the goods and receiving the purchase price back.
 - (3) *Delivery.* Traders are responsible for any damage to the goods until the consumer takes possession of them.
- 4.47 As far as internet sales are concerned, the CESL follows the provisions of the CRD, using slightly different wording. As these provisions are already part of EU law, we do not comment on them here.

WHEN IS THE CONTRACT FORMED?

- 4.48 A contract is formed when the parties reach an agreement which is intended to have legal effect. The normal arrangement is that one side makes an offer and the other side accepts it. These general principles are uncontroversial, and subject to party autonomy. They are set out in Article 30 of CESL.

The consumer offers and the trader accepts

- 4.49 The difficulty lies in deciding which part of an internet sale constitutes the offer, and which the acceptance. Is the website advertisement an offer, which is accepted when the consumer puts in credit card details and presses submit? Or is the website merely an “invitation to treat”? If so, the consumer makes an offer to buy which the trader accepts through statement or conduct.¹³
- 4.50 Article 31.3 clarifies that “a proposal made to the public is not an offer, unless the circumstances indicate otherwise”. This means that a website offering goods for sale is not normally an offer in legal terms. This is a substantial change from the Feasibility Study, which stated that a proposal “made in a public advertisement or a catalogue referring to an identified stock” would normally be considered to be an offer to supply goods to members of the public at the stated price, until the stock was exhausted.¹⁴
- 4.51 Article 31.3 of the CESL draft is much more in line with internet trading as it is currently understood in the UK. The website is an “invitation to treat”; the consumer makes an offer to buy the goods by clicking the submit button; and the trader then accepts the offer.

¹³ See Art 33.

¹⁴ Feasibility Study draft, May 2011, Article 30(3)

When does acceptance take place?

Internet practice

- 4.52 Internet traders are often careful about when they accept an offer. They do not wish to be bound to supply goods if they are out-of-stock. They are also worried about possible mispricing. Suppose an internet trader made a typing error on the website and offered a £499 laptop at £4.99. It could then receive thousands of hits within the hour. If the trader were obliged to fulfil all the orders at that price it could make a substantial loss. Thus traders will be reluctant to accept consumers' offers until they have checked availability and price, and are ready to dispatch the goods.
- 4.53 Internet traders generally send at least two emails in response to the consumer's offer to purchase. The first confirms receipt of the offer and is said not to be an acceptance. The formal acceptance is delayed until the second email which confirms dispatch. The following term is used by Amazon.co.uk, though similar terms are used throughout the industry:

When you place an order to purchase a product from Amazon.co.uk, we will send you an e-mail confirming receipt of your order and containing the details of your order. Your order represents an offer to us to purchase a product which is accepted by us when we send e-mail confirmation to you that we've dispatched that product to you (the "Dispatch Confirmation E-mail"). That acceptance will be complete at the time we send the Dispatch Confirmation E-mail to you. Any products on the same order which we have not confirmed in a Dispatch Confirmation E-mail to have been dispatched do not form part of that contract.

- 4.54 The Amazon terms and conditions go on to deal with mispricing:

Despite our efforts, a small number of the millions of products in our catalogue are mispriced. Rest assured, however, that we verify prices as part of our dispatch procedures. If a product's correct price is lower than our stated price, we charge the lower amount and send you the product. If a product's correct price is higher than our stated price, we will, at our discretion, either contact you for instructions before dispatch or cancel your order and notify you of such cancellation.

- 4.55 This outcome is possible because the contract is not formed until the dispatch confirmation. Many traders may use their discretion to supply at the advertised price, but that is a matter of goodwill rather than law. Representatives of the British Retail Consortium told us that they would often supply one item at the lower price – but where a consumer has ordered ten items, traders would take a hard line.

The CESL approach

- 4.56 The most recent draft, unlike previous drafts, allows the current practice to continue. Article 33.1 states that:

Any form of statement or conduct by the offeree is an acceptance if it indicates assent to the offer.

- 4.57 Thus acceptance may either be by statement or by conduct. Under Article 35, the contract is concluded when the consumer receives the acceptance or notice of the conduct.

ACCEPTANCE BY STATEMENT

- 4.58 Under Article 33.1, the timing of the acceptance depends on the words used. Traders would be well advised to continue to draft their first response email carefully, so that it does not amount to an acceptance. For example the first email might say:

Thank you for your order. It is being processed, but will not be accepted before we have dispatched the goods.

- 4.59 A trader who uses wording of this type would not be bound to supply the goods until they have in fact been dispatched.
- 4.60 We think that this produces the right outcome. It appears to correspond to the current position under the laws of the UK, and reflects current UK market practice. We think that it is also right in policy terms. Given how easy it is to buy online, the consumer has rarely lost from the transaction, and is adequately protected by the return of any payment made. If the consumer were to be given a £499 computer for £4.99 this would represent an element of windfall profit. It would expose traders to substantial and uncontrollable losses, which might undermine the viability of this form of selling. We therefore welcome the change from the Feasibility Study.
- 4.61 It would be helpful to explain this point to traders and consumers. The new draft represents a major policy change from the DCFR and the Feasibility Study published in May.

TAKING PAYMENT AS ACCEPTANCE BY CONDUCT

- 4.62 A key issue is whether a trader's acceptance of payment amounts to acceptance by conduct. Take a case where the consumer submits an order, giving details of a credit card. The trader obtains payment from the credit card company, but fails either to send an acceptance notice or dispatch the goods. Is a contract formed?
- 4.63 Under the laws in the UK, the consumer would be entitled to the return of their money, whether or not the contract had been formed. In the absence of a contract, the consumer would have a right to the return of the payment under the law of restitution (also known as "unjustified enrichment"). Under the draft CESL, there is a clear right to the return of the payment if a contract has been formed,¹⁵ but no equivalent right to the return of payment in the absence of a contract. Part VII deals with restitution, but only where a contract is avoided or terminated. There is no right to restitution where no contract was ever formed.

¹⁵ Under Article 106.1(c) the consumer may terminate the contract for non-performance and claim the return of any price paid.

- 4.64 Even if the consumer has agreed to use the CESL, the consumer could still rely on the English law of restitution or the Scottish law of unjustified enrichment, on the grounds that restitution in the absence of a contract is outside the scope of the CESL. This would not, however, provide a simple, easy to understand remedy for a consumer seeking redress without professional legal advice.
- 4.65 Furthermore, it is easier for the consumer to obtain their money back from the credit card company if a contract has been formed. This is because section 75 of the Consumer Credit Act 1974 offers an easy straightforward remedy against the credit card company where the trader is in breach of contract.¹⁶ But section 75 does not apply to a claim for restitution in the absence of a contract.
- 4.66 This means that consumers are better protected if accepting payment is considered to be “acceptance by conduct” within the meaning of Article 34. The words used are capable of producing this result, but we think the issue could usefully be clarified.

Time of acceptance by conduct

- 4.67 A final issue is when the contract is formed through acceptance by conduct. Article 35.2 states that:

When an offer is accepted by conduct, the contract is concluded when notice of the conduct reaches the offeror.

- 4.68 In other words, if the trader takes a credit card payment but does not make a statement accepting the offer, the contract would appear to be formed when the consumer receives their credit card bill or is otherwise notified that the debit has been made. Where the trader has become insolvent, this may be too late. Article 35.2 may be difficult to reconcile with the rule we recommend above, that property passes when a trader takes payment and labels the goods. We think further thought could usefully be given to this provision.

Conclusion on contract formation

- 4.69 We think that the new provisions on contract formation are on the right lines, and represent a significant improvement upon the Feasibility Study. On the other hand, some elements remain complex and their effect is far from clear to a consumer with a problem. We think the issue could usefully be clarified, if not in the main text, at least in an authoritative guide.
- 4.70 The essential point, which consumers need to understand, is that when they order goods online, they have no legal right to receive them at the advertised price until the trader has either confirmed acceptance or taken payment. We are concerned that consumers may misunderstand the statement in the European Commission’s Factsheet for the United Kingdom published on 11 October which lists the following “improvement for UK consumers”:

¹⁶ Note that section 75 applies even if the contract was formed under a foreign law: see *OFT v Lloyds TSB Bank* [2007] UKHL 48, [2008] 1 AC 316, discussed above at para 4.37.

Under the Common European Sales Law, if a business fails to deliver the goods, a consumer can require the business to do so. Such a general right does not exist in the UK: courts will almost invariably offer a financial compensation to the consumer instead of imposing the delivery of the goods. In certain circumstances, this is less convenient and effective for the consumer as he will have to look for another seller of the same good, at the same conditions and conclude a new transaction.¹⁷

- 4.71 It is important to note that consumers can only require a business to deliver the goods once the trader has accepted their offer, and this will normally only be done once the trader has dispatched the goods. The practical effect of the right to specific performance is limited, as we discuss below.¹⁸

NON-CONFORMITY

The existing law

- 4.72 Under the Consumer Sales Directive, goods only conform to contract if they meet the listed requirements. Broadly speaking, goods must be fit for the purpose for which they are normally used, be fit for any special purpose which the consumer made known to the business, and possess the qualities which the consumer can reasonably expect.¹⁹ In substantial measure, these requirements reflect the implied terms which are already set out in the UK Sale of Goods Act 1979.²⁰
- 4.73 However, as the 1999 Directive is a minimum harmonisation measure, the Sale of Goods Act 1979 contains an additional gloss on the Directive. In particular, section 14(2) states that goods must be of satisfactory quality. Section 14(2B) specifies that in appropriate cases aspects of quality may include:

- (a) fitness for all the purposes for which goods of the kind in question are commonly supplied,
- (b) appearance and finish,
- (c) freedom from minor defects,
- (d) safety, and
- (e) durability.

¹⁷ European Commission, *A common sales law for Europe: factsheet for the United Kingdom*. http://ec.europa.eu/justice/contract/files/common_sales_law/sales_law_uk_en.pdf It should be noted that this statement more correctly reflects English than Scots law where specific performance is more readily available. See below at paras 4.148 to 4.155.

¹⁸ See paras 4.148 to 4.155.

¹⁹ 1999/44/EC, Art 2.

²⁰ In domestic contracts, the implied terms are mandatory. Under the Unfair Contract Terms Act 1977, s 26, it is technically possible to contract out of the implied terms in international contracts for the sale of goods. The Law Commissions have criticised s 26 for being inconsistent with EU law and have called for its reform: see *Unfair Terms in Contracts*, (2005) (Law Com No 292; Scot Law Com No 199) para 7.6.

4.74 These provisions were incorporated into section 14 following recommendations made by the two Law Commissions in their 1987 Report, *Sale and Supply of Goods*.²¹ We argued that consumers often put great store in the appearance of new goods, and their expectations were undermined when new household goods arrived with “dents, scratches, minor blemishes and discolourations”. We thought the issue should be addressed specifically in legislation on the subject.

4.75 In our 2009 report, *Consumer Remedies for Faulty Goods*,²² we argued that section 14(2B) continued to be appropriate and should give rise to a right to reject. Referring back to the 1987 Report we said:

Now in 2009, it is evident that the appearance of goods is as important (if not more important) to consumers. In many cases consumers spend a great deal of time selecting goods specifically because of their appearance. Therefore, it is appropriate that dents, scratches and blemishes will sometimes be breaches of the implied term as to quality. In these cases, a repair or replacement may not be practical or possible, and the consumer will not want a reduction in price because they have selected the goods for their appearance and paid for a specific appearance.²³

Article 100

4.76 In the draft CESL, the provisions on quality of goods are set out in Article 100. This follows the Draft Common Frame of Reference.²⁴ Paraphrasing slightly, it requires that the goods must:

- (a) be fit for any particular purpose made known to the seller when the contract was concluded (unless the consumer did not rely on the seller’s skill and judgement or it was unreasonable for the consumer to rely on the business’s skill and judgement);
- (b) be fit for the purposes such goods would ordinarily be used for;
- (c) possess the qualities of the sample or model which the seller held out to the consumer;
- (d) be contained or packaged in a manner adequate to preserve and protect the goods;
- (e) be accompanied by such accessories and instructions as the consumer might reasonably expect to receive;
- (f) possess the qualities and performance capabilities indicated by any pre-contractual statement which forms part of the contract; and

²¹ Law Com No 160, Scot Law Com No 104, pp 22 to 35.

²² (2009), Law Com No 317, Scot Law Com No 216, paras 3.98 to 3.110.

²³ Above, para 3.101.

²⁴ See DCFR IV.A – 2:302.

- (g) possess the qualities and performance capabilities the consumer might reasonably expect.

4.77 The basic provisions are similar to existing EU legislation and the Sale of Goods Act 1979. However, there are a few differences which are worth highlighting.

Appearance, finish and freedom from minor defects

4.78 First, Article 100 does not include any specific reference to appearance and finish. We think that the provisions along the lines of section 14(2B) of the Sale of Goods Act 1979 are useful to have for the reasons we gave in our 1987 and 2009 Reports.

4.79 There is probably not a substantive difference between UK law and Article 100. A consumer could argue that the prominent scratch on the door means that their new fridge does not possess the qualities they expected. But given the number of arguments over scratches and blemishes, it is helpful for the consumer to be able to point to a specific statement that appearance and finish are aspects of quality.

Packaging

4.80 The reference to packaging in Article 100(d) is new. It needs to be understood in the context of Article 142.1, which states that the business is responsible for any damage to goods before the goods have been delivered. So if the goods are damaged in transit, it does not matter why: there is no need to consider whether the packaging was adequate.

4.81 If the goods arrive undamaged, it is unlikely that the consumer would be able to reject them simply because of a fault in the packaging. That would probably be regarded as an insignificant lack of conformity, within the meaning of Article 114. The consumer could, however, ask for replacement packaging under Article 111.

Accessories

4.82 Article 100(e) is also new. Consumers have the full range of remedies if the goods do not arrive with the accessories and instructions a buyer may reasonably expect. In the context of internet sales, this is clearly an important issue. Do consumers reasonably expect electronic goods to arrive with plugs, batteries and cables? And should the instructions be in a language and format they can understand? Large manufacturers will translate their instruction manuals into multiple languages, but small manufacturers may be wary of the expense of providing manuals in all 23 EU languages.

4.83 The onus is on the trader to explain what is and is not included in the price. If the website clearly states, in English, "cable not included", then any consumer who reads English cannot reasonably expect to receive a cable. Where does this leave consumers who struggle with English? May their reasonable expectations be different?

4.84 Article 5 states that:

Reasonableness is to be objectively ascertained, having regard to the nature and purpose of what is being done, to the circumstances of the case and to any relevant usages and practices.

- 4.85 It will therefore be for the court to determine objectively whether in the particular circumstances, a reasonable consumer would or would not speak the language. This may depend on the perspective of the judge: a judge who speaks English may be more likely to decide that the warning was clear than with a judge who does not speak English.
- 4.86 One answer may be to develop internationally recognised symbols for what is or is not included in internet sales. This could not cover the full range of goods, but would address common issues such as cabling and batteries.

Contracting out of Article 100

- 4.87 It is possible to contract out of Article 100 if the trader brings a defect to the consumer's attention before the sale. However, the CESL is more protective than the Consumer Sales Directive (CSD) on this issue.
- 4.88 The CSD provides that the business is not in breach of contract if the consumer was aware of (or could not reasonably have been unaware of) the lack of conformity at the time the contract was concluded.²⁵ Article 104 of the CESL provides a rule mirroring this provision, but only for business-to-business contracts.
- 4.89 The rule for consumers is slightly different. Article 99.3 provides that the parties cannot agree to derogate from Article 100 unless the consumer knew about the specific condition of the goods and accepted the goods on that basis. This means that it is not enough to show that the consumer knew of the defect or "could not have been unaware" of it. There needs to be some form of express or implied agreement that the buyer would buy despite the non-conformity. Thus it is not enough that the consumer should have been aware that one of the plates in the crockery set was chipped. The trader would need to show that the consumer agreed to buy despite the chipped plate.
- 4.90 The change has implications for internet traders selling second-hand or imperfect goods. It may no longer be sufficient for the internet trader to mention the defect. It may need to add a button that the consumer clicks to acknowledge that they are aware of the defect. We can see the logic of this change, but it has the potential to add to traders' costs. It may be helpful to consult further on this issue.

UNFAIR TERMS

Provisions reflecting the Unfair Terms Directive

- 4.91 Member states must provide the minimum protections set out in the Directive on Unfair Terms 1993,²⁶ and they may also add to these provisions if they wish. The UK has implemented the Directive, with very few changes, in the Unfair Terms in Consumer Contracts Regulations (UTCCR) 1999.

²⁵ For the UK, s 14(2C) Sale of Goods Act provides a similar exclusion in relation to the term implied by s 14(2).

²⁶ Council Directive 93/13/EEC of 5 April 1993.

4.92 The two Law Commissions reviewed the operation of the UTCCR in our 2005 report, *Unfair Terms in Contracts*.²⁷ We concluded that the UTCCR were too narrow. We recommended that the UK should extend unfair terms protection beyond the minimum required under the Directive in two respects.

- (1) **Negotiated terms:** we argued that consumers seldom have sufficient understanding of the possible impact of non-core terms to make any negotiation meaningful. The exclusion of negotiated terms was exploited by some unscrupulous businesses selling door-to-door: the businesses would initially offer an absurd term and then alter it to something more acceptable, but nevertheless severely disadvantageous to the consumer.
- (2) **The definition of core terms:** Under the Directive, a term is exempt from review if relates to the main subject matter of the contract or the adequacy of the price, provided it is in plain intelligible language.²⁸ It need not necessarily be accessible or brought to the consumer's attention. In *Office of Fair Trading v Abbey National plc*,²⁹ the Supreme Court held that bank charges levied on personal account holders for unauthorised overdrafts were part of the price for banking services. So, provided the term was in plain intelligible language, the courts had no jurisdiction to assess its fairness.

In our 2005 report, *Unfair Terms in Contracts*,³⁰ we argued that the way a consumer understood a term was not just about the language used, but about the way the term was presented. We recommended that a term should not be considered to be a core term unless it was presented in a clear manner and was accessible to the consumer.

4.93 The draft published in the Feasibility Study in May 2011 extended unfair terms protection in the way we had recommended.

4.94 The draft CESL published in October 2011 departs from the May 2011 draft in this regard, however. Chapter 8 of the CESL restates the principles of the Directive in slightly different words, but does not contain protection over and above minimum EU requirements. In particular:

- (1) Under Article 83, protection is restricted to terms which have not been individually negotiated.
- (2) Under Article 80.2, unfair terms protection does not apply to terms defining the main subject matter of the contract or the appropriateness of the price, provided the terms are in plain intelligible language.³¹

²⁷ Law Com No 292, Scot Law Com No 199, paras 3.62 and 3.63.

²⁸ Art 3(3), Unfair Terms Directive 1993.

²⁹ [2009] UKSC 6, [2010] 1 A.C. 696.

³⁰ Law Com No 292, Scot Law Com No 199, paras 3.62 and 3.63.

³¹ The requirement for plain intelligible language is set out in Article 82.

Reasonable steps to draw the party's attention to the term

- 4.95 In addition to the normal protections against unfair terms, the draft CESL provides that a non-negotiated term is automatically unfair if the business did not take reasonable steps to draw the consumer's attention to it. Article 70.1 provides as follows:
- Contract terms supplied by one party and not individually negotiated ... 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.
- 4.96 Article 70.2 specifies that in consumer contracts it is not sufficient merely to refer to a term in a contract document, even if the consumer signs the document.
- 4.97 This is an additional protection, over and above the Directive. The test under Article 70 is different from the unfair terms test in Articles 79 to 85. The unfair terms test is a rounded test, balancing a wide range of factors. Under Article 83 a term is only unfair if it "causes a significant imbalance in the parties' rights and obligations" and is "contrary to good faith and fair dealing". Thus the court should look both at the substance of the term and at the way it was presented. Article 83.2 sets out a wide range of factors which the court should consider, including the nature of what is to be provided and the circumstances prevailing during the conclusion of the contract. The court must take account of both presentation and substance.
- 4.98 By contrast, the Article 70 test is one-dimensional: the term does not have to be substantively unfair. Nor does the court need to balance a range of factors. If the trader failed to take reasonable steps to draw the term to the consumer's attention, it is not binding on the consumer, irrespective of its substance.
- 4.99 Article 70 goes further than the law in England or Scotland. In England, the case of *Interfoto Picture Library Ltd v Stilleto Visual Programmes Ltd*³² held that where a clause was particularly onerous or unusual, the party seeking to enforce it must show that it had been brought fairly and reasonably to the attention of the other party. This rule has also been applied in Scotland.³³ By contrast, Article 70 applies to all terms, whether or not they are onerous or unusual.
- 4.100 This next question is what constitutes reasonable steps. As Article 70.2 makes clear, it would not be enough to refer to terms and conditions which no-one actually reads, even if the consumer is required to tick a box agreeing to them before submitting an order. Some more prominent warning would be needed.
- 4.101 This brings us back to the issue of language. Would a warning in English be taking reasonable steps to bring the term to the notice of a Spanish consumer? Again, a judge who does not read English and cannot understand the warning may be unsympathetic to the argument that the warning constituted reasonable steps.

³² [1989] QB 433.

³³ *Montgomery Litho Ltd v Maxwell* 2000 SC 56

Conclusion on unfair terms

- 4.102 We are disappointed that the draft CESL does not include the extensions to unfair terms protection which we recommended in 2005, and which were included in the Feasibility Study.
- 4.103 That said, the additions we proposed are more relevant to face-to-face contracts rather than to internet sales.
- (1) Negotiated terms are important in off-premises contracts, where the parties negotiate face-to-face, but do not occur where the parties deal remotely over the internet.
 - (2) The exclusion of price terms from review is a major issue for some contracts, particularly bank accounts. In internet contracts, however, consumers are already protected by the pre-contract information provisions. Thus Article 13(b) provides that the trader has a duty to provide information on the total price and additional charges and costs “in a clear and comprehensible manner”. Under Article 14, this must be the total price, inclusive of taxes, or (where the price cannot be calculated in advance) the manner in which the price is to be calculated. Article 29 provides that where the trader has breached these requirements, the consumer is not liable to pay additional charges.
- 4.104 In some circumstances, Article 70 may provide useful additional protection. It goes further than current law, however. It may prevent traders from relying on terms which are substantively fair but which were written in a language that the consumer did not understand. Further thought needs to be given on whether this achieves the right balance for internet sales.

ADAPTING THE CONTRACT FOR AN EXCEPTIONAL CHANGE OF CIRCUMSTANCES

- 4.105 Article 89 introduces a new provision where one party is unable to perform its obligations because exceptional circumstances have made performance excessively onerous. It imposes a duty on parties to negotiate in good faith, with a view to either adapting or terminating the contract. If the parties fail to reach an agreement within a reasonable time, either party may go to court to ask the court to adapt the contract.
- 4.106 This is a controversial inclusion. It goes considerably further than the general doctrine of frustration found in English and Scots law, and introduces a more onerous duty to renegotiate. In the Feasibility Study, the European Commission asked whether it represented added value in consumer contracts.
- 4.107 We do not feel that it represents added value, particularly for consumers. Conceptually, the scheme and procedure of Article 89 are full of uncertainty and doubt. The Article is likely to produce different results across all the court systems of the EU member states because of these inherent uncertainties.
- 4.108 Moreover, as a basic concept we think the inclusion of a positive duty to renegotiate is unlikely to help consumers. All evidence indicates that consumers generally do not negotiate with suppliers. A positive duty requiring businesses and consumers to renegotiate is unduly optimistic and unlikely to be fruitful.

An example

- 4.109 In low-value internet sales, neither party will wish to become involved in litigation: the cost of asking a court to adapt a contract would be excessive.
- 4.110 We assume that Article 89 is aimed at high-value items. Take a case where a consumer orders an expensive car, to be made in accordance with their special requirements. The consumer specifies that the car must be yellow. The business, for exceptional reasons, becomes unable to supply the car in yellow. Instead, it offers one in red, blue or green, with a discount. Under Article 89, the consumer must negotiate with an open mind. If negotiations fail, the business may go to court, arguing that an objectively reasonable consumer would have agreed a different colour.
- 4.111 The problem with this provision is that it imposes a test of objective reasonableness (as defined by Article 5) on consumers who wish to spend their money to satisfy entirely subjective preferences. If the trader is unable to fulfil the terms of the contract, most consumers would prefer to get their money back, rather than having a different choice imposed on them. The provision is unlikely to encourage consumer confidence in the CESL.

REMEDIES

- 4.112 Much of the debate over consumer contract law has centred on remedies. One of the most controversial issues is whether consumers who receive faulty goods must start by asking for a repair or replacement, or whether they should be entitled to return the goods immediately and ask for their money back.
- 4.113 The Consumer Sales Directive sets out minimum requirements: initially a consumer is only entitled to a repair or replacement, but may rescind the contract if a repair or replacement cannot be provided without unreasonable delay or significant inconvenience. Under the laws in the UK the consumer also has a “right to reject”. The consumer may reject the goods and receive their money back straight away, without first seeking repair or replacement from the seller, provided rejection is made quickly, within “a reasonable time”.
- 4.114 In 2009 we published a report on remedies for faulty goods. We concluded that the right to reject outright, without a need first to seek repair or replacement of the defective goods, was particularly valuable to consumers and should be retained. However, it should be time-limited. We noted that there was considerable uncertainty over how long a reasonable time might be, and recommended that the issue should be clarified. We thought that in normal circumstances the consumer should only be able to exercise the right to reject for 30 days following the sale. Thereafter, if the goods proved to be faulty, the consumer should start by seeking a repair or replacement.

- 4.115 Another controversial issue is whether a consumer who returns goods should receive back the full purchase price or whether the trader should be given some allowance for the consumer's use of the goods. Under the Consumer Sales Directive, a consumer who rescinds the contract will not necessarily be entitled to the return of the full purchase price. The trader can retain a proportion of the price to allow for the use the consumer has had from the product. Our focus groups with consumers found this to be extremely unpopular: consumers felt that no reputable trader should sell them a faulty product, fail to repair it, and then require them to pay for the use they may have had from it.

An unlimited right to terminate

- 4.116 The CESL gives the consumer a choice of remedies, including repair or replacement, damages or "termination".
- 4.117 Termination is similar to the right to reject: the consumer returns the goods and receives the purchase price. It is set out in Article 114.2:

In a contract between a business and a consumer, the consumer may terminate for non-performance in the case of any non-conformity, unless the non-conformity is insignificant.

Under Article 108, this right cannot be excluded.

- 4.118 We are pleased that consumers are granted a right to reject the goods, without first being required to ask for a repair or replacement, as we recommended in our 2009 Report. The right to terminate under the CESL is however very different from the normal 30-day right to reject we recommended.
- 4.119 Under the CESL the right is not time-limited. Article 119 states that in contracts between businesses notice of termination must be given within a reasonable time, but this does not apply where the buyer is a consumer. At first sight, the only time limit imposed on the right to terminate is the prescription period in Articles 179 and 180. The consumer must act within two years from the time they knew or could be expected to know of the fault, or within ten years of the sale, if this is a shorter period.
- 4.120 So what happens if a consumer buys shoes which fall apart after five months? Under Article 105.1 the consumer must establish that the goods were faulty at the time they were sold. This task, however, is made easier by Article 105.2, which reflects the current law, as set out in the Consumer Sales Directive. Any fault which becomes apparent within six months is presumed to have existed at the time of the sale. It is up to the trader to show that it did not.
- 4.121 The combined effect of these provisions means that if the shoes fall apart after five months, the consumer has two years and five months from the sale to terminate the contract and ask for their money back. If the shoes fall apart after a year, the consumer may reject the shoes within a further two years (that is, within three years from the sale), but would need to produce evidence that a latent fault existed at the time the shoes were sold.

4.122 That said, it is possible that prolonged delay may constitute a lack of good faith. Article 2.2 provides that a consumer who breaches the duty to act in accordance with “good faith and fair dealing” may not be able to exercise a right or remedy which they would otherwise have under the CESL. The following example is given by the Draft Common Frame of Reference:

if a [consumer] inexcusably failed to notify the [business] of a defect for an altogether unreasonable length of time with the effect that the [business] was seriously prejudiced by the delay then ... the [consumer] might be precluded by the general rule on good faith and fair dealing from founding [a claim] on the non-conformity.³⁴

4.123 We do not know whether this observation would also apply to the CESL. Recital 31 suggests that it might not. It states:

The principle of good faith and fair dealing should provide guidance on the way the parties have to cooperate. As some rules constitute specific manifestations of the general principle of good faith and fair dealing, they should take precedence over the general principle. *The general principle should therefore not be used as a tool to amend the specific rights and obligations of parties as set out in the specific rules.* (Italics added)

4.124 The question is whether the unlimited right to reject under Article 114.2 is a specific rule which takes precedence over the duty of good faith and fair dealing. We are not sure of the answer to this, and think that the recital could usefully be clarified.

4.125 In some circumstances, a consumer who terminates a contract will be required to give an allowance for use, rather than receive the return of the full purchase price. Article 174 provides that a recipient who has made use of goods must pay the other party the monetary value of that use for any period where:

- (a) the recipient caused the ground for avoidance or termination;
- (b) the recipient, prior to the start of that period, was aware of the ground for avoidance or termination; or
- (c) having regard to the nature of the goods, the nature and amount of the use and the availability of remedies other than termination, it would be inequitable to allow the recipient the free use of the goods for that period.

4.126 Thus a consumer would be expected to give an allowance if they continued to use the goods after discovering the fault. They must also give an allowance if it would be inequitable not to do so.

4.127 We have two concerns about these provisions: first, that the right to terminate is too long; and secondly that it is too uncertain.

³⁴ DCFR, Vol 2, p 1340.

The termination right is too long

4.128 In our 2009 Report we saw some advantages to allowing an extended right to terminate a contract, especially where a latent defect comes to light several months or possibly years after purchase. But we saw two reasons against such an extension:

- (1) An extended right could be abused. Retailers felt strongly that extending the time for rejection might encourage abuse by some consumers who may use an item for a period of time, and then seek a refund when they no longer need it.³⁵
- (2) It would not be fair to allow a long-term right to reject goods without giving some form of credit for use and enjoyment. This raises difficult problems of calculation which would take away much of the force of a clear, simple right to reject.

4.129 We commented that “the right to reject is a powerful weapon which should be kept for faults that manifest themselves immediately or after a short period of use”. After the product has been used for a while, the primary remedy should be a repair or replacement.

4.130 We are concerned that internet traders may regard the extended right to reject as excessive, and decide not to use the CESL at all for fear that it would be abused. The Feasibility Study included a three year prescription period, and led to the following comment from Shop Direct:³⁶

The proposal to include a 3 year right for consumers to reject faulty goods would be a complete non-starter for our business and I suspect for any other sizeable UK business. This is because we currently operate to the short term right of rejection contained in the Sale of Goods Act 1979, which we interpret as 30 days. Accordingly, an increase from 30 days to 3 years is totally unrealistic and would be a deal breaker.

4.131 Although under the current draft, the prescription period is two years rather than three years, the right to terminate is still much longer under the CESL than under the laws of the UK. It would be regrettable if the CESL were to not to be used for this reason. We would suggest that the consumer’s right to terminate under the CESL be restricted to a period of months rather than years.

³⁵ Consumer Remedies for Faulty Goods, (2009) Law Com No 317 and Scot Law Com No 216, para 3.29.

³⁶ Shop Direct operates the brands Littlewoods, Very, Isme, K&Co and Woolworths in the UK as well as Littlewoods Europe, which trades across approximately 25 (mostly EU) European countries.

The termination right is too uncertain

- 4.132 In our 2009 report we stressed the importance of certainty in consumer law. Only a tiny minority of domestic disputes will ever be taken to court – and even fewer court cases will be brought in cross-border sales. Consumers and traders need quick, simple solutions to resolve problems with the minimum scope for dispute. The advantage of a right to reject within 30 days is that it provides minimal scope for argument.
- 4.133 We think the proposed CESL provisions on termination give the parties too many issues to argue about – particularly over whether the consumer has acted in good faith under Article 2, and whether it would be equitable to give an allowance for use under Article 174(c).
- 4.134 Where there is delay, consumers and businesses are likely to see things differently. Take an example where a consumer buys new shoes, and instead of wearing them straight away puts them in the bottom of their wardrobe for three months. They then wear them only three times in two months, and on the fourth occasion the heel falls off. The consumer falls ill, or goes on holiday, or has the stress of caring for a sick relative, so it is seven months before they manage to return the shoes to the trader. The consumer is convinced that they are completely reasonable to complain: they have spent £100 on new shoes and worn them only three times.
- 4.135 The trader may see it differently, and think that the consumer has acted unreasonably in delaying the complaint for seven months. The trader strongly suspects that the consumer is lying: that the consumer has worn them all summer and has simply grown tired of them now that the weather has changed.
- 4.136 The problem is that the CESL fails to provide any clear rules for resolving this dispute. We fear that the longer the chain of emails continues the more entrenched views will become, until a minor dispute about a broken heel escalates into “an issue of principle”, with consumer and trader at loggerheads. We think it is better to set a time limit for the right to reject, however arbitrary, rather than allow disputes to escalate in this way.

The allowance for use

- 4.137 In the Feasibility Study, the European Commission asked whether the rules set out in Article 178 on giving an allowance for use were appropriate in business to consumer transactions. We think that the rules are too uncertain and give too much scope for disputes.
- 4.138 The issue will arise frequently. Traders are likely to ask for an allowance for use whenever they consider the consumer to be acting unreasonably. The focus groups we conducted for our remedies project suggest that consumers are likely to resent it. Article 174 gives no indication of how use should be valued, and disputes are likely to escalate.
- 4.139 We think it would be preferable to limit the right to terminate to a set period. A consumer who terminates within that period should receive the return of the full purchase price.

Damages for distress and inconvenience

- 4.140 In English and Scots law, the general position is that following a breach of contract, damages are not recoverable for injured feelings.³⁷ However, this general rule is now subject to an increasing number of exceptions.³⁸
- 4.141 The most important exception is that mental distress damages are allowed where the main purpose of the contract is to provide pleasure, or to avoid distress.³⁹ The key cases in this area concern contracts for entertainment, and particularly spoiled holidays.⁴⁰ The courts have set informal tariffs, which are typically low. In a case concerning a dream-cruise-turned-nightmare, the English Court of Appeal noted that “awards in this area should be restrained and modest”.⁴¹
- 4.142 Damages are also available where the consumer has suffered some physical inconvenience and discomfort caused by the breach.⁴² Damages for physical inconvenience are common where the landlord has failed to repair the consumer’s home.⁴³ They would also be granted whenever a consumer has been prevented from using their home for a prolonged period.
- 4.143 As far as internet sales are concerned, damages for distress or inconvenience may be granted where the trader was aware that the goods would be used as part of an important occasion, where distress would be caused if the occasion was ruined. An example would be where a wedding dress fell apart at the wedding, causing distress to the bride. We also think that the CESL could apply to a contract for wedding photographs, which appear to come within the definition of “a contract for the supply of goods to be manufactured or produced”, as set out in Article 2(k). Faulty wedding photographs are a classic example where distress damages might be granted.

³⁷ *Addis v Gramophone* [1909] AC 488, 491; *Watts v Morrow* [1991] 1 WLR 1421, 1445; *Johnson Gore Wood & Co* [2000] UKHL 65, [2002] 2 AC 1, 49; followed in Scotland, but not uncritically: see W W McBryde, *The Law of Contract in Scotland* (3rd edn, 2007), paras 22-101 to 22-103.

³⁸ Even the general rule has been doubted. See Lord Millett’s comments in *Johnson v Unisys* [2001] UKHL 13, [2003] 1 AC 518, para 71, indicating that the exclusion of mental distress damages should only apply to “ordinary commercial contracts entered into by both parties with a view to making a profit”. See also *Johnson v Gore Wood* [2000] UKHL 65; [2002] 2 AC 1. For Scots law see Scottish Law Commission Report No 174 on Breach of Contract (1999), para 3.3; W W McBryde, *The Law of Contract in Scotland* (3rd edn, 2007), paras 22-98 to 22-105.

³⁹ As in *Heywood v Wellers* [1976] QB 446 where solicitors were held liable for the distress caused to their client, through their negligent failure to get a restraining order against a man who was harassing her. In Scotland, see also *Diesen v Samson* 1971 SLT (Sh Ct) 49 and *Colston v Marshall* 1993 SCLR 43; also *Gary McKay v Stakis Ltd t/a Hilton Coylumbridge*, reported in Scottish Legal News 27th January 2011.

⁴⁰ *Jarvis v Swan Tours* [1973] QB 233 CA; *Jackson v Horizon Holidays* [1975] 1 WLR 1468 CA; and *Milner v Carnival* [2010] EWCA Civ 389, [2010] 3 All ER 701.

⁴¹ *Milner v Carnival* [2010] EWCA Civ 389, [2010] 3 All ER 701, para 41 by Ward LJ, echoing the words of Lord Steyn in *Farley v Skinner* [2001] UKHL 49, [2002] 2 AC 732, para 28 and Bingham LJ in *Watts v Morrow* [1991] 1 WLR 1421, 1445.

⁴² *Watts v Morrow* [1991] 1 WLR 1421, 1445 by Bingham LJ, cited with approval (in this respect) by the House of Lords in *Farley v Skinner* [2001] UKHL 49; [2002] 2 AC 732.

⁴³ See, for example, *Wallace v Manchester City Council* [1998] 3 EGLR 38. In Scotland see *Mack v Glasgow City Council* 2006 SC 543, Extra Division.

- 4.144 Damages for physical inconvenience might be awarded if there was damage to the consumer's home, for example where a defective water pipe burst, leaving the consumer unable to use a room of their house for several months. As the type of cases involving damages for distress or inconvenience expands, we think damages might also be granted where a boiler fails, leaving a family with young children without heating for a prolonged period of sub-zero temperatures.
- 4.145 Damages for distress and inconvenience are not available under the CESL. This is made clear by the definition of loss given in Article 2 of the Regulation. Article 2(c) states:
- 'loss' means economic loss and non-economic loss in the form of pain and suffering, excluding other forms of non-economic loss such as impairment of the quality of life and loss of enjoyment.
- 4.146 Thus the right to damages for loss in Article 159 does not include damages for "non-economic loss" such as distress and inconvenience. This is another major change from the Feasibility Study, which stated that loss included "impairment of the quality of life and loss of enjoyment".⁴⁴
- 4.147 This represents a reduction in consumer protection, which undermines the European Commission's claim that the CESL provides a high level of consumer protection. At the very least, this point must be adequately explained in the information provided to consumers. If a consumer were buying the sort of goods which are likely to cause distress or discomfort should they fail (wedding dresses, boilers, pipes etc), this may give pause for thought. We note that the point is not mentioned in the Standard Information Notice in Annex II to the Regulation.

Specific performance

- 4.148 Commissioner Reding has pointed out that under the CESL, the buyer is more likely to obtain an order for specific performance than is the case under English law. As we saw, this was noted as a particular improvement for all UK consumers in the European Commission's Factsheet for the United Kingdom, although the law on this issue differs between England and Wales on the one hand and Scotland on the other hand.
- 4.149 Under English law, specific performance may be granted to enforce the sale of "specific or ascertained goods".⁴⁵ On the other hand, such orders are made at the discretion of the judge, and are relatively rare. The English courts tend to assume that if the supplier has failed to deliver goods without the intervention of the courts, the supplier is unlikely ever to meet its obligations satisfactorily. The courts will tend to treat the contract as dead, and provide compensation instead.

⁴⁴ Feasibility Study draft, Art 2(12).

⁴⁵ See Sale of Goods Act 1979, s 52(1), which states that: "in any action for breach of contract to deliver specific or ascertained goods the court may, if it thinks fit, on the plaintiff's application, by its judgment or decree direct that the contract shall be performed specifically, without giving the defendant the option of retaining the goods on payment of damages".

- 4.150 In Scots law, such orders are referred to as “implement”. Scots law tends to grant implement more readily than English law.⁴⁶ It has been said that in sale of goods cases, implement should only be refused where the buyer has a readily available alternative source of supply.⁴⁷ Other authority, however, suggests that it should only be granted where the goods have special or sentimental value for the buyer,⁴⁸ which is closer to the English position on the subject.
- 4.151 In the CESL, the issue is dealt with by Article 110. This states that “the buyer is entitled to require performance of the seller’s obligations”. This, however, is subject to the exceptions in Article 110.3 that performance cannot be required where
- (a) Performance would be impossible or has become unlawful; or
 - (b) The burden or expense of performance would be disproportionate to the benefits that the buyer would obtain.
- 4.152 In the internet context, the right to specific performance is unlikely to have an effect before goods are dispatched. As we have seen, internet traders are usually reluctant to enter into contractual obligations before this point. Nor will this provision make a practical difference where the goods are received and turn out to be faulty. Under current law, UK consumers already have a right to a repair or a replacement, which is effectively a right to have goods re-delivered in a way that conforms to the contract.
- 4.153 The right to specific performance would arise where goods are dispatched, but never arrive (for example where goods are stolen from the lorry or destroyed in an accident). Even in these circumstances, however, we doubt that the right to specific performance would have a practical effect. Most traders would much prefer to deliver replacement goods than to give consumers their money back, if replacements are available. The problem comes where the trader does not have replacement goods and could only source them at higher price. Yet if the cost of sourcing replacement goods is disproportionate to the cost of compensating the consumer for their loss of benefit, the CESL allows the trader to refuse specific performance under Article 110.3(b).
- 4.154 There may be a difference where the consumer has entered into a continuing contract at a fixed price. For example, suppose a consumer has entered into a contract that the trader will deliver a gold coin every month for a fixed price. As the price of gold mounts, the trader loses money and tries to escape from the agreement. Under English law, the consumer would be compensated for their loss, calculated as the difference between what the gold coins are now worth and the price the consumer agreed to pay for them. Under the CESL, the trader may be compelled to deliver the coins as promised. This would be an extremely unusual contract, however, and the difference in approach between English law and the CESL is a subtle one.

⁴⁶ See in particular *Highland & Universal Stores Ltd v Safeway Properties Ltd* 2000 SC 297.

⁴⁷ *TB Seath & Co v Moore* (1886) 13 R (HL) 57.

⁴⁸ Known as “pretium affectionis”; see *Union Electric Co Ltd v Holman* 1913 SC 954.

- 4.155 In conclusion, the difference between English law and the CESL on this issue is more theoretical than real. We find it difficult to think of any circumstances where it would have a practical effect for consumers. There does not appear to be any difference with Scots law, even at a theoretical level.

ISSUES NOT DEALT WITH

- 4.156 The European Commission asked the Expert Group not to deal with topics which are less relevant for cross-border contracts, such as capacity.⁴⁹ There are two issues, however, which are not dealt with by the draft CESL but which we think may be relevant: title and illegality. We consider them below.

Title

- 4.157 It is the nature of the sales contract that the seller transfers ownership of the goods to the buyer. The CESL states explicitly, in Article 91(b), that the business must “transfer the ownership of the goods” to the consumer. Article 102 confirms that the goods must be free from third party rights and plausible third party claims. Thus if the trader sells goods which turn out to be stolen or subject to a security interest in favour of a finance company, the consumer has a remedy against the trader. That issue is unproblematic and an essential provision of sales law across the EU.
- 4.158 The difficulty is where the trader disappears, and the consumer is faced with a third party demanding the return of the goods. An example is where an unsuspecting consumer buys an expensive second-hand racing bicycle from an e-Bay trader. The bicycle turns out to be stolen; the e-Bay trader is never seen again; and the original owner discovers her bicycle in the hands of the consumer. Must the consumer return the bicycle to the true owner, and pay compensation to the owner for any use they have had from it?
- 4.159 The European Commission specifically asked the Expert Group not to address transfer of ownership, on the grounds that it was “less relevant to cross-border contracts”.⁵⁰ The CESL is therefore silent on this point.⁵¹ We assume that this means that the issue will be dealt with by the law of the member state in which the transaction takes place. In the case of stolen goods this may not be too problematic: most legal systems in the EU will recognise the rights of the true owner to the return of stolen goods.
- 4.160 The issue becomes more complex, however, when the goods are subject to a security interest in favour of a finance company. Take a case where a German consumer orders a second-hand car from a UK website. The consumer later finds that the car is subject to a security interest in favour of a finance company. Can the finance company reclaim the car? EU legal systems differ in the balance of protection they provide to the consumer and the finance company, both of whom are innocent parties.

⁴⁹ Feasibility Study p 6.

⁵⁰ Feasibility Study p 6.

⁵¹ The DCFR contains relevant rules at Books VIII.-3:101-2 and IX.-6:102.

- 4.161 In English and Scots law, special statutory protection is granted to private purchasers of motor vehicles which are subject to un-discharged hire-purchase agreements. A private purchaser who acts in good faith and is unaware of the hire-purchase, receives good title and can keep the vehicle.⁵² But the protection is limited. It applies only to motor vehicles and only to hire purchase. If, for example, the finance house had lent not under a hire purchase agreement but under a so-called “bill of sale”, the consumer would be forced to return the car to the finance company.⁵³ If the internet trader had become insolvent the consumer would also be without protection.
- 4.162 Again, this could be a problem. The German consumer would have bought the car in good faith under the CESL, assuming that they would be given a high level of legal protection, only to find that the car must be surrendered to the finance company.

Illegality

- 4.163 There are many goods which may not legally be sold across borders. The HM Revenue and Customs’ guide to internet shopping across borders lists the following banned items which may not be brought into UK in any circumstances.⁵⁴
- illicit drugs;
 - flick and gravity knives;
 - self defence sprays such as pepper and CS gas sprays;
 - stun guns;
 - indecent and obscene material; and
 - counterfeit, pirated and patent-infringing goods.
- 4.164 Furthermore, the following items are restricted, in that they need a licence or permit:
- firearms, explosives and ammunition;
 - realistic imitation firearms;
 - offensive weapons including swords with a curved blade exceeding 50cms in length;
 - live animals;
 - endangered animals or plants;

⁵² See Hire-Purchase Act 1964, s 27, as amended by Consumer Credit Act 1974, sch 4.

⁵³ The Law Commission addressed the complexities of Bills of Sale legislation in Registration of Security Interests, Consultation Paper No 164 (2002), part VIII, and argued strongly that reform is needed. It should be noted that Scots law does not contain a concept analogous to Bills of Sale.

⁵⁴ HM Revenue and Customs Guide: *Buying abroad from the internet: what to look out for*. <http://www.hmrc.gov.uk/customs/post/internet.htm>

- certain fur skins and articles made from fur skin;
- certain radio transmitters; and
- rough diamonds.

4.165 If a consumer buys alcohol or tobacco online from another EU state, it is also a criminal offence to import the goods without paying excise duty. The Guide explains:

Excise Duty is payable on goods such as alcohol or tobacco. It is the responsibility of the online seller to ensure that UK Excise Duty is paid before they send you the goods. You should therefore expect the price you pay to reflect the payment of UK duty - if the price is very low, UK duty has probably not been paid.

In addition, cigarettes and hand rolling tobacco must bear UK health warnings and fiscal marks, and containers of spirits that are larger than 35cl must bear a UK duty stamp.

If the online retailer you're buying the goods from does not pay UK Excise Duty before they send them to you, or the goods do not bear the relevant UK markings or warnings, the goods can be seized by customs on arrival in the UK, and you may not be able to get a refund on their value. It's therefore a good idea to check with the retailer that all these requirements have been met.⁵⁵

4.166 The question is what are the legal consequences if a consumer orders a banned or restricted item in a cross-border sale, which is then seized by customs on arrival?

4.167 Most European legal systems have a doctrine of illegality, which means that the civil courts will refuse to give a remedy to a party to an illegal contract. If the contract were for heroin, the outcome is clear. Civil courts would refuse to hear the dispute and the loss would lie where it fell. Thus if the buyer refused to pay, the seller could not sue for the contract price. Conversely, if the seller provided sub-standard goods (such as drugs cut with rat poison), the buyer would be without a remedy. In the case of seriously illegal products, such as heroin, that is uncontroversial, and we do not intend to suggest that the CESL should provide for such circumstances.

4.168 The difficulties come where the goods are not so obviously illegal. Some goods (such as pepper sprays) may be legal in the business's home state: a small trader who has not taken legal advice may not realise that the spray is banned in the UK. In other cases, the consumer may be genuinely unaware that the radio transmitter is restricted, or that the piano has ivory keys. In some cases, goods may legally be sold to adults but not children. Thus it may be a crime to sell pornography, tobacco, knives or glue directly to children.

⁵⁵ <http://www.hmrc.gov.uk/customs/post/internet.htm>

- 4.169 In the UK context, importing pets causes particular problems. Pet animals may only be imported into the UK if they comply with the PETS Scheme or are licensed by Animal Health and are quarantined upon arrival. If a UK consumer travels to Belgium to buy a rare breed of puppy from a small Belgian breeder, the consumer may assume that the trader has dealt with the necessary formalities, while the trader may assume that a UK consumer will be familiar with UK law.
- 4.170 European legal systems differ in how they distinguish between seriously illegal and restricted goods, and in how they deal with cases where one party is more at fault than the other. Traditionally, the English courts have taken a harsh line, so that they would not be prepared to hear a claim from a weaker party who had acted illegally.⁵⁶ The German courts on the other hand may be more prepared to entertain a claim from the weaker party to the transaction, so as to do justice between the parties.⁵⁷
- 4.171 The risk that the parties may be unaware of an illegality is greater in cross-border sales. Small enterprises may be unfamiliar with the different laws across Europe. They may even misunderstand the concept of the CESL and assume that it means they do not have to check the legality of their products in other European states.
- 4.172 It might therefore be helpful if the CESL addressed the issue.⁵⁸ The main question is what should happen where a consumer buys a product in a cross-border sale which may not lawfully be imported into their home state, where they are less at fault than the trader. In a code designed to boost consumer confidence, the best solution may be to allow the consumer their money back. However, the publicity surrounding the CESL would need to make clear that businesses (however small) would be obliged to check the legality of their products in all the states to which they were sent, taking legal advice if necessary.

CONCLUSION

- 4.173 In Part 2 we identified a need for a self-standing code to resolve consumer disputes which arise from cross-border distant sales, particularly sales made online.

⁵⁶ See for example, *Gibbs Mew v Gemmell* [1999] ECC 97. The proposition set out in that case was criticised by the Advocate-General in *Courage Ltd v Crehan* [1999] IEGLR 43 at p 49, as being unduly formalistic. For the Scottish approach to the *in pari delicto* question see W W McBryde, *The Law of Contract in Scotland* (3rd edn, 2007), para 13.31.

⁵⁷ For example, in 1982 the Federal Court, the Bundesgerichtshof (BGH), was asked to decide whether a consumer could enforce a building contract when both sides had agreed to use clandestine labour. Although both sides had acted illegally, the defendant's behaviour was the more heinous, and the claimant should not be put at "an intolerable disadvantage": see 23 September 1982, BGHZ 85.39. A partial translation is to be found in H Beale et al, *Cases, Materials and Text on Contract Law* (2nd edn, 2010) pp 640-642.

⁵⁸ We note that the issue is addressed in the DCFR, books II.-7:301-4 and VII.-6:103.

- 4.174 A code to deal with the specific problems of internet selling, however, would be very different from a set of principles of European contract or general sales law. Principles of contract law need to be general, comprehensive, fluid and flexible. Contract law provides a framework by which the parties may write their own rules, often supplemented by specific industry practices, and interpreted and developed through court decisions. By contrast, an internet code needs to be simple, certain and specific. Consumer disputes rarely go to court, and almost never to the appeal courts. Cross-border disputes are even less likely to end in court decisions. Thus it is often better to have a clear (if arbitrary) time limit, rather than an open, flexible test.
- 4.175 General principles are relatively policy neutral: they do no more than provide the framework under which the parties can make their own decisions. Drafting a general code is often a technical exercise, best done by experts, with comment and input from a panel of users. An internet code, on the other hand, encapsulates policy decisions. The most difficult element is to find the appropriate balance between the needs of businesses and consumers, which means that at its core it must reflect policy trade-offs.
- 4.176 At the start of this Part we asked whether the draft was easy to understand; whether it provided clear answers to the main problems; and whether it set an appropriate level of consumer protection.
- (1) It is not always easy to understand. It would be a shorter, more accessible document if it only applied to consumer sales. There is also a need for an authoritative guide explaining how it works. As we went through the draft, we identified many points which would need to be covered by such a guide.
 - (2) It does not always provide clear answers to problems. In particular, the open-ended discretion over whether the consumer must give an allowance for use may encourage disputes.
 - (3) In some places, the level of consumer protection may not be appropriate. In particular:
 - (a) The draft provides consumers with an extended right to reject, for up to two years from the date the consumer could be expected to be aware of the fault. This may discourage traders from using the CESL at all.
 - (b) On the other hand, the exclusion of damages for distress and inconvenience would reduce consumer rights in some circumstances.
- 4.177 We think that before proceeding further, there should be consultation on the central policy issues involved. The four most important issues we have identified are:

- (1) Language: should the CESL be subject to the linguistic requirements imposed by member states, or should businesses be entitled to trade across the EU in any language they wish? If so, who should bear the costs of any misunderstandings that result – the business or the consumer?
- (2) Where the goods are faulty, how quickly should the consumer notify the business that they wish to terminate the contract, and get their money back?
- (3) Is it better to decide this issue through fixed periods or more open-ended principles?
- (4) In what circumstances should consumers be provided with damages for distress and inconvenience?

PART 5

THE DRAFT CESL AND OTHER CONSUMER SALES CONTRACTS

- 5.1 In Part 3 we considered how the Common European Sales Law (CESL) would work in the context of internet selling. In practice, internet selling is likely to be the most important use of the CESL and we think it should be designed with the internet primarily in mind. It is not, however, confined to internet selling. Here we consider how it might apply to two other forms of selling: telephone sales and off-premises sales.

TELEPHONE SALES

- 5.2 We do not think that the CESL as currently drafted is suitable for telephone sales. Two provisions make the CESL problematic for traders doing business by telephone, which we outline below.

Agreement to use the CESL by phone

- 5.3 Recital 23 explains that consumers should only be bound by the CESL once they have received the information notice:

Where it is not possible to supply the consumer with the information notice, the agreement to use the Common European Sales Law should not be binding on the consumer until the consumer has received the information notice together with the confirmation of the agreement and has subsequently expressed consent.

- 5.4 This policy is reflected in Article 9.1 of the Regulation which states that:

Where the agreement to use the Common European Sales Law is concluded by telephone or by any other means that do not make it possible to provide the consumer with the information notice... the consumer shall not be bound by the agreement until the consumer has received the confirmation referred to in Article 8(2) accompanied by the information notice and has expressly consented subsequently to the use of the Common European Sales Law.

Telephone contracts valid only with written consent

- 5.5 The second problematic provision is Article 19.4. This is new, and was not included in the Feasibility Study. It states that:

A distance contract concluded by telephone is valid only if the consumer has signed the offer or has sent his written consent indicating the agreement to conclude a contract. The trader must provide the consumer with a confirmation of the agreement on a durable medium.

- 5.6 Under the Consumer Rights Directive (CRD) member states may add a formal requirement for telephone contracts into their national laws if they wish. Article 8.6 of the CRD states that:

Where a distance contract is to be concluded by telephone, Member States may provide that the trader has to confirm the offer to the consumer who is bound only once he has signed the offer or has sent his written consent. Member States may also provide that such confirmations have to be made on a durable medium.

- 5.7 There is a significant difference between Article 8.6 of the CRD and Article 19.4 of the draft CESL. Under the CRD, member states may provide that consumers are not bound by the contract. By contrast, Article 19.4 declares the contract to be invalid. This is a significant change. If the contract is invalid, the consumer would not be able to enforce it. The consumer would, for example, be deprived of any right to a repair or replacement if the goods prove to be faulty.

Telephone sales in practice

- 5.8 There are many different forms of telephone selling. We have considered three examples to see how these provisions would apply to telephone selling in practice. We consider:

- (1) Telephone sales through a website;
- (2) Telephone sales through a press advertisement; and
- (3) Unsolicited telephone calls.

Telephone sales through a website

- 5.9 In this example, the consumer finds a website which includes the trader's telephone number, and phones to order the goods. The trader takes the consumer's credit or debit card details on the phone and then dispatches the goods for delivery.
- 5.10 A small business may offer telephone ordering instead of online ordering because it is easier to set up. More commonly, however, traders use telephone ordering as an addition to online ordering. Telephone ordering offers personal service, and many customers are happier talking to a person rather than pressing buttons. The customer can check that the product meets their needs, as envisaged by Article 100(a). Also a telephone service allows the trader to continue to trade should the online ordering service encounter technical difficulties.
- 5.11 We assume that where a firm offers telephone sales alongside its internet sales, it will wish to use the same form of contract law to cover both. There is little point in using the CESL for online sales, and the mandatory provisions of national law for the telephone sales. This would just add another legal regime to the current complexity. If the CESL is to achieve its objective of providing a simpler system for traders, it would need to apply to the firms' telephone sales in much the same way as it applies to its online sales. As the CESL is currently drafted this may be difficult.

- 5.12 The first question is whether Article 9.1 of the Regulation would apply. Is this a contract “concluded by telephone or by any other means that do not make it possible to provide the consumer with the information notice”? On balance, we think that Article 9.1 would not apply. The information notice is available on the firm’s website, which the consumer has visited. Thus in this case, it is possible to provide the consumer with the information notice. We think that the CESL could be used if:
- (1) The trader confirms that the consumer had access to the information notice;
 - (2) The consumer makes an explicit oral statement indicating consent to the use the CESL; and
 - (3) When the trade dispatches the goods, it includes written confirmation of the agreement to use the CESL, as required by Article 8.2 of the Regulation.
- 5.13 This, however, does not deal with the problems posed by Article 19.4. In the scenario we have outlined, the consumer has not signed the offer or sent written consent indicating agreement to conclude a contract. If the draft CESL is to be taken at face value, the contract would be invalid. This would not be a problem for the trader, who has the required payment. It would, however, be a major problem for the consumer who would be deprived of all rights under the contract.
- 5.14 We do not think this can have been the drafters’ intention. We recommend that the European Commission reconsiders Article 19.4, explaining in more detail the intention behind the provision.

Telephone sales through a press advertisement

- 5.15 In this scenario, the customer telephones in response to an advertisement in a newspaper. The trader takes credit card details over the telephone and dispatches the goods immediately. We think the CESL is probably incompatible with this method of selling.
- 5.16 Take an example of a small business offering next day delivery on printer ink. It advertises in the back of a national newspaper. Like many small businesses, it can only afford a small advertisement. This advertisement includes the information listed in Article 19.3, such as the main characteristics of the goods, the identity of the trader, the total price and the right to withdraw. This leaves no space to re-print the information notice, which is a page and a half long.
- 5.17 We think that in this case Article 9.1 applies: it has not been possible to provide the consumer with the information notice. This means that the choice of CESL cannot apply until the consumer has received confirmation of the agreement in a durable agreement, together with the information notice and has then expressly consented.
- 5.18 We are puzzled that the trader is required to send “confirmation” of an agreement before an agreement has taken place. We assume that “confirmation” in this context simply means a written offer to use the CESL, along with an information notice.

- 5.19 Where the consumer orders ink, the trader has two choices:
- (1) It can refuse to take payment or dispatch the goods until it has sent the consumer a copy of the information sheet, asking the consumer to phone back once the information sheet has been received. As this is likely to lose the sale, the trader would be under commercial pressures not to do this. It would also be incompatible with next day delivery.
 - (2) It could dispatch the cartridge along with the information sheet, asking the consumer to phone back to confirm acceptance of the CESL. In practice, consumers are unlikely to phone back. Life is too short. They will only be interested in the choice of law if the product proves faulty, and then they may prefer to use their domestic law.
- 5.20 We assume that the policy decision has been taken that the CESL should not be available for this type of sale.
- 5.21 We think this point merits further discussion. The question is whether the information sheet is sufficiently important to restrict those who sell by small advertisement and telephone from using the CESL. Research in 2007 by the Better Regulation Executive and National Consumer Council warned that not all information notices are necessarily helpful to consumers.¹ It recommended that information should be tested on consumers before being applied to goods and services. Restricting the use of the CESL to those sent the information notice may be justified, but only if it is shown to be valuable to consumers.
- 5.22 If it were thought that the CESL should be extended to this form of sale, then Article 19.4 would also need to be reconsidered and redrafted.

Unsolicited phone calls

- 5.23 The third type of telephone selling is where the trader telephones the customer. We can see that, where the trader uses high pressure sales techniques in unsolicited telephone calls, there are good reasons to say that the trader may not enforce the contract until the consumer has consented in writing.
- 5.24 If this is the real danger, there may be a case for restricting Article 19.4 to contracts made where the trader has initiated contact. Article 19.4 could also be redrafted to state that the trader is unable to enforce the contract, rather than the contract is invalid.

Other forms of telephone sales

- 5.25 There are many other forms of telephone sales. For example, a consumer may order goods by text. This remains unusual for initial sales, but may be a useful way of placing continued orders. We think that a text would be sufficient to indicate written consent, but would welcome clarification of this point.

¹ Warning: too much information can harm. A final report by the Better Regulation Executive and National Consumer Council on maximising the positive impact of regulated information for consumers and markets. <http://www.bis.gov.uk/files/file44588.pdf>

- 5.26 We are conscious, too, that as mobile phones develop, the line between internet technology and telephone technology is becoming blurred. New forms of shopping may develop through applications, which may rely on the telephonic communication rather than the internet. It may be helpful to consider how the CESL would work in a variety of new selling techniques.

Conclusion on telephone sales

- 5.27 The issue of how the CESL would apply to telephone sales needs further clarification. Traders who just use telephone sales could continue to use national laws. However, traders who mainly sell by online, but who also use telephone sales alongside the online element may be reluctant to trade under different forms of law for different types of sale. This may undermine the usefulness of the CESL for website sales generally.

DOORSTEP SELLING

- 5.28 For doorstep selling it will be fairly easy for the trader to obtain agreement to use the CESL, as both parties will be negotiating face to face. The question is whether the CESL offers sufficient protection to consumers faced with this form of selling. This is not a major problem if the CESL is confined to cross-border sales, but it becomes a problem if it extended to domestic use.

The problem of aggressive practices

- 5.29 In our recent consultation on misleading and aggressive practices,² we were provided with considerable evidence that consumers are particularly vulnerable when unscrupulous traders visit them in their homes.
- 5.30 We were told that aggressive practices are a particular problem for housebound consumers, especially the elderly. There were many complaints about the techniques used to sell mobility aids, such as mobility scooters and adjustable beds. For example, in 2010 Derbyshire County Council received 603 complaints about doorstep selling of mobility aids and described the problems as follows:

A significant minority of unscrupulous traders will take advantage of vulnerable residents by implying that they are from or working on behalf of Social Services or the Health Service and will use high-pressure sales techniques to sell products at inflated prices which are of little benefit to the user.

² Law Commission and Scottish Law Commission, Consumer Redress for Misleading and Aggressive Practices, Joint Consultation Paper Law Commission Consultation Paper 199/Scottish Law Commission Discussion Paper 149 (April 2011).

- 5.31 A particular problem is that salespersons wear down the consumers' resistance by staying for two or three hours, giving the impression that they would only leave if the consumer agreed to buy. For example, in an investigation by BBC's *Rogue Traders*, an undercover reporter accompanied a salesman to the home of a man in his mid-80s who expressed an interest in a chair to help him stand. The salesman stayed for two hours, wearing down the consumer's resistance, and selling an overpriced product for £2,300. Afterwards, the salesman described it as "like nicking a Mars bar off a baby", boasting of having made about £500 in commission.³
- 5.32 These forms of high pressure techniques are criminal offences under the Consumer Protection for Unfair Trading Regulations 2008, which implement the Unfair Commercial Practices Directive 2005. The problem, however, is that that civil law does not necessarily give a remedy for breaches of the Directive. As we explain in the summary of the report, the current civil law on aggressive practices in the UK is not as clear as it should be:

The most important doctrines are "duress" in England and Wales, and "force and fear" in Scotland. These doctrines developed through cases which were not brought by consumers, and the law is inaccessible to non-lawyers. The doctrines are particularly difficult to apply where the trader does not make explicit threats to the consumer's person or goods.

Doctrines such as undue influence, facility and circumvention, unconscionable bargains and intimidation may also apply. However, the scope of these doctrines is extremely uncertain, and they do not provide a firm foundation for consumers to claim redress.⁴

- 5.33 The uncertainty and complexity of the law deters vulnerable people from exercising their rights. We argued that where there had been an aggressive practice within the meaning of the Regulations, there needed to be a clear, simple right to unwind the contract within three months. The consumer should have the right to the full return of the purchase price and to cancel any linked credit agreement.

The CESL provisions

- 5.34 Some of the complexities in UK law are also found in the CESL. Article 50 on threats is similar to the current law of "duress" (in England) and "force and fear" (in Scotland). It states:

A party may avoid a contract if the other party has induced the conclusion of the contract by the threat of wrongful, imminent and serious harm, or of a wrongful act.

³ See http://www.bbc.co.uk/blogs/watchdog/2010/06/rogue_virgo_healthcare.html.

⁴ Law Commission and Scottish Law Commission, *Reforming Consumer Redress for Misleading and Aggressive Practices: What do you think? Summary* (April 2011). http://www.justice.gov.uk/lawcommission/docs/lc317_Consumer_Remedies_Faulty_Goods_Outline.pdf.

- 5.35 We were given many examples where the salesperson had used techniques which were aggressive within the meaning of the Consumer Protection for Unfair Trading Regulations 2008 because (for example) the trader had ignored the consumer's requests that they should leave. However, the techniques usually stopped short of explicit threats of violence.
- 5.36 The question is whether Article 50 covers contracts induced by any wrongful act, or whether the scope of the article is constrained by the words "imminent and serious harm". Does it apply if the trader makes a threat of future or minor harm, and to all other wrongful acts? We think it would be helpful to re-draft Article 50 to specify that the consumer has a right to avoid a contract induced by aggressive practices within the meaning of the Unfair Commercial Practices Directive.
- 5.37 There is also a possible right under Article 51 (unfair exploitation). This applies where:
- The consumer 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.
- 5.38 We have considered whether this would apply to the man in his mid-80's who expressed an interest in a chair to help him stand, given above. We do not think that he had a relationship of trust with the salesman. Nor was he necessarily in economic distress, improvident, ignorant or inexperienced. Many consumers would be reluctant to bring a case which required them to denigrate their own capabilities in this way, when the true mischief lay in the aggressive tactics of the seller.
- 5.39 The next issue is the remedy. Under both Articles 50 and 51 of the CESL, the consumer may avoid the contract. Elderly consumers with few social contacts may take several months to find out their rights and make a complaint. If so, must the consumer pay the trader for their use of the goods? Under Article 174 it would be open to the trader to argue that the consumer was aware of the ground for avoidance from the start, or that it would be inequitable to allow them free use of the goods. These arguments may add considerable stress to the consumer's battle to obtain their rights.

Negotiated terms

- 5.40 One technique used by unscrupulous doorstep sellers is the manipulative "negotiation". The salesperson starts with an astronomical price, but rapidly reduces the price to something which is merely excessive, because the consumer is "special" or "qualifies" for a particular deal. There may also be negotiations over the size of the deposit or the possibility of making a reduction in price dependant on a particular term in the contract.
- 5.41 In our 2005 report on Unfair Terms we argued that consumers would be better protected if the provisions on unfair terms included negotiated terms. As we noted in Part 4, under Article 83 of the CESL, unfair terms protection is restricted to terms which have not been individually negotiated

The need for certainty

- 5.42 Consumers are particularly vulnerable to doorstep selling. We think member states need to be able to retain the power to reform their laws to provide consumers with clear, simple remedies, which are easy to use.
- 5.43 There is a danger that unscrupulous traders could use the CESL to avoid new laws in this area. They may even use an unfamiliar system to add confusion and complexity to the process of obtaining redress. Indeed, the most unscrupulous could base themselves abroad simply to exploit consumer's lack of knowledge of the CESL.
- 5.44 We think that initially the use of the CESL should be confined to distance selling. It should be permitted for off-premises sales only once it has become established and familiar to consumer advisers.

CONCLUSION

- 5.45 We welcome clarification on how the CESL would apply to telephone sales. Traders who receive orders online and by telephone will naturally wish to use the same legal system for both. If they are unable to use the CESL for telephone sales, this may undermine the usefulness of the CESL for website sales generally.
- 5.46 We would be concerned if the CESL were made available for doorstep selling. This form of selling is particularly problematic, and member states may need to retain their ability to enact new contract law measures to protect consumers against the worse abuses.
- 5.47 If the CESL is introduced for doorstep selling, further changes would be needed. In particular, we would welcome clarification that Article 50 includes aggressive practices within the meaning of the Unfair Commercial Practices Directive; a clear remedy where Article 50 is breached; and the inclusion of negotiated terms within unfair terms protection.

PART 6

COMMERCIAL CONTRACTS: HOW WOULD THE CESL APPLY?

- 6.1 The proposal to introduce a Common European Sales Law (CESL) would not only affect business-to-consumer contracts. It is also intended as a system of contract law which businesses may choose to use when contracting with other businesses. Here we consider how it would operate in the context of business-to-business transactions.
- 6.2 We start with a brief overview of the current regime of applicable law under the Rome I Regulation. For business contracts, Rome I permits a free choice of law. For most European Union countries, the default regime for cross-border sales contracts is the United Nations Convention on Contracts for the International Sale of Goods (CISG).
- 6.3 We consider the problems caused by the current law. We summarise the Eurobarometer survey of businesses involved in cross-border business-to-business sales. The main demand for a new system appears to be from SMEs rather than large businesses.
- 6.4 We then look at how the proposed Regulation would work. The parties would not be required to use any particular procedure for choosing the CESL. In business-to-business contracts, there is no equivalent of the consumer “blue button”. In most cases, the choice will take effect as a term of the contract, though in some cases the parties may agree to negotiate on the basis of the CESL.
- 6.5 On the other hand, the proposed Regulation sets two restrictions on the use of the CESL. First, large businesses are not permitted to use the CESL when contracting with another large business. Secondly, the CESL may not be used for mixed-use contracts. We discuss this restriction and ask, for example, whether the CESL could be used for a distribution contract.

THE CESL AND THE ROME I REGULATION

The effect of Rome I on business to business contracts

- 6.6 In business-to-business contracts, the Rome I Regulation allows a free choice of law. Article 3 states:

A contract shall be governed by the law chosen by the parties. The choice shall be made expressly or clearly demonstrated by the terms of the contract or the circumstances of the case.
- 6.7 The only provisions of national law which cannot be excluded in commercial contracts are “overriding mandatory provisions”. This is a narrow category. Under Article 9, it is defined as provisions which a country regards as crucial “for safeguarding its public interests, such as its political, social or economic organisation”. For example, parties cannot use a choice of law clause to avoid a country’s tax or criminal law.

- 6.8 On the other hand, commercial parties are not caught by the “ordinary” mandatory provisions of another legal system, even where the legal system itself would not permit the parties to derogate from its rules by agreement. This differs from the position in consumer sales. There is no equivalent of Article 6, and no special protection for those habitually resident in another state.

Rome I and “soft law”

- 6.9 The main limit is that under Rome I the law must be a system of national law or, like CISG, recognised as a system of national law. The Regulation does not permit a choice of “soft law”.¹ As Nils Willem Vernooij explains:

Rome I does not allow the contracting parties to choose anything but national law. Therefore, non-State rules of law - such as *lex mercatoria*, the Principles of European Contract Law, or the UNIDROIT Principles of International Commercial Contracts - cannot be chosen as the law applicable to the contract. This intentional omission has been criticized as being out-of-touch with international commercial reality, contradictory to the principle of party autonomy and inconsistent with the arbitration laws of many countries.²

- 6.10 Recital 13 stipulates:

This Regulation does not preclude parties from incorporating by reference into their contract a non-State body of law or an international convention.

- 6.11 This, however, is a limited provision. The soft law provisions must exist alongside a choice of national law, and must not conflict with that choice.³ Thus contracting parties may not choose the Draft Common Frame of Reference (DCFR) as their current main choice of law, though they could state that certain terms should be interpreted in line with the DCFR.

- 6.12 The effect of the proposed Regulation would be to give the CESL the status of a national legal system, allowing contracting parties to use if they wished.

¹ Thus in *Shamil Bank of Bahrain EC v Beximco Pharmaceuticals Ltd*, [2004] EWCA Civ 19 a case concerned with the Rome Convention, the Court of Appeal held that “the Convention as a whole only contemplates and sanctions the choice of the law of a country”: see para 48.

² “Rome I: an update on the law applicable to contractual obligations in Europe”, 15 *Columbia Journal of European Law Online* 71 (2009). This update is available at http://www.cjel.net/online/15_2-vernooij/

³ For further discussion of this issue, see Helmut Heiss, “Party Autonomy: The Fundamental Principle in European PIL of Contracts” in Franco Ferrari, Stefan Leible (eds) *Rome I Regulation: the Law Applicable to Contractual Obligations in Europe* (2009) p 2.

The CESL would be another choice of laws

- 6.13 The CESL would be one possible choice, among the many legal systems the parties are free to choose. At present, parties to a commercial contract may choose any of the legal systems in the 27 member states. They may also choose a system from outside the EU, such as the law of Switzerland or New York (both widely used for international commerce).⁴
- 6.14 For most businesses within the European Union, the default regime is the United Nations Convention on Contracts for the International Sale of Goods (CISG), sometimes referred to as the “Vienna Convention”. This has now been ratified by 76 countries, including most EU member states.⁵ The important point about the CISG is that in most cases, it does not need to be chosen explicitly. Where parties have places of business in two different states, and both states have ratified the CISG, the CISG becomes the default regime for international sales of goods contracts. This means that the CISG applies unless the parties make an express choice of some other regime.
- 6.15 For most European states, the CESL would provide a direct competitor to the CISG. Those who are unhappy with the CISG could choose to contract out of the CISG and into the CESL, rather than use another national legal system. In Part 7 we provide a short comparison of the advantages and disadvantages of each.

Jurisdiction

- 6.16 The CESL would not affect issues of jurisdiction, which would continue to be regulated by the Brussels I Regulation.⁶ The general rule is that a person domiciled in a member state must be sued in the courts of that member state.⁷ However, there are exceptions. In contract disputes, a defendant may be sued in the place of performance of the obligation in question.⁸ In particular, in a contract for the sale of goods, a defendant may be sued in the member state where, under the contract, the goods were delivered or should have been delivered.⁹ The parties may also enter into jurisdiction agreements, to choose the jurisdiction which suits them best.¹⁰
- 6.17 These rules are not affected by the European Commission’s proposal.

PROBLEMS WITH THE CURRENT SYSTEM

- 6.18 The problems are different from the problems in consumer sales. The parties are not required to comply with the mandatory provisions of different states. Instead, they have a free choice of laws.

⁴ See Stephan Vogenauer, *Civil Justice Systems in Europe: A Business Survey* conducted by the Oxford Institute of European and Comparative Law and the Oxford Centre of Socio-Legal Studies, 2008.

⁵ The exceptions are the UK, Malta, Portugal and the Republic of Ireland.

⁶ Regulation No 44/2001 of 22 December 2000.

⁷ Above, art 2.

⁸ Above, art 5(1)(1).

⁹ Above, art 5(1)(b).

¹⁰ Above, art 23.

- 6.19 The main problem with the current system is that there is *too much* choice. It is difficult for businesses to find out about different legal systems. This usually requires expensive legal advice. In the absence of full information, businesses will naturally favour their own legal system, which may make it difficult to agree to the choice of law when a business from another state favours their own legal system.
- 6.20 Businesses may also associate the issue of cross-border sales with the difficulties of litigating in other countries, though issues of jurisdiction would not be affected by the CESL. The difficulty of resolving cross-border disputes will remain.
- 6.21 Businesses would favour a world without legal complexity. They would welcome a world with one simple, neutral legal system, which everyone agreed fully met their needs. If the CESL provided such obvious benefits that everyone would agree to use it without difficult negotiations, this would remove a source of business stress. On the other hand, if the CESL is just one more choice, this would add to the current complexity. In Part 7 we consider whether CESL fulfils the promise of one simple, neutral legal system, with such obvious benefits that businesses would no longer need to negotiate over choice of law.

The Eurobarometer survey

- 6.22 In Part 2, we described the results of the Eurobarometer survey of over 6,000 businesses who indicated that they were either sell to consumers across borders or were planning to do so. Flash Eurobarometer carried out a similar survey of over 6,000 businesses who were either involved in cross-border business-to-business sales or where planning to do so in the future.
- 6.23 Again, interviewers presented businesses with a list of 11 potential obstacles and asked if each one had a large impact; some impact; minimal impact; or no impact. Four of these questions were said to relate to contract law, and the results are set out below.

Table 3: The impact of contract-related obstacles on businesses' decisions to sell/purchase across borders from/to businesses from other EU countries

	Large impact	Some impact	Minimal impact	No impact
Difficulty in finding out about the provisions of a foreign contract law	8%	12%	15%	57%
Problems in resolving cross-border conflicts, including costs of litigation abroad	9%	10%	13%	60%
Obtaining legal advice on foreign contract laws	6%	10%	15%	62%
Difficulty in agreeing on the foreign contract law	5%	10%	15%	63%

Source: Flash Eurobarometer, European contract law in business-to-business transactions, page 15.

- 6.24 As one might expect, the impact of these obstacles was slightly less than for business-to-consumer sales. There were all ranked below the effect of tax and formal requirements, such as licensing and registration procedures.
- 6.25 In all, 49% of the survey reported that at least one of the factors has at least some minimal impact, and these businesses were then asked: “How often did these obstacles deter you from conducting cross-border transactions?” Four answers were provided: always; often; not very often; never. The results are shown below – first as a proportion of those who answered the question (the 49%) and then as a proportion of all the businesses in the sample.

Table 4: How often do contract law obstacles deter businesses from conducting B2C cross-border transactions?

	% of those reporting some impact	% of all businesses conducting cross-border sales or with an interest in them
Always	3	1
Often	12	6
Not very often	49	24
Never/no impact/don't know	36	69

Source: Flash Eurobarometer, European contract law in business-to-business transactions, page 25.

- 6.26 In other words, out of all the businesses in the study, 7% reported a major impact: that they were always or often deterred; 24% reported that although these factors had some impact on them, they were “not very often” deterred; and 69% said they were never deterred.
- 6.27 Again this shows that contract law differences cause some concern, but it is important not to overemphasise the problem. Some readers may misunderstand the comment in the European Commission’s impact assessment that:

61% of companies involved in B2B transactions and affected by contract law differences were often or at least occasionally deterred by contract law related barriers.¹¹

- 6.28 This figure looks only at those businesses who said that contract law differences had some impact on them. If one looks across the sample of all businesses conducting or planning to conduct cross-border business-to-business transactions, it appears that 31% of businesses were “always”, “often” or “not very often” deterred by contract law related barriers. This is around half the European Commission’s figure, but, nonetheless, not negligible.

¹¹ Commission Staff Working Paper Impact Assessment, p 11.

Who would use the CESL?

Small and medium enterprises

- 6.29 Commissioner Reding has identified small and medium enterprises (SMEs) as the main beneficiaries of an optional system of European contract law. She explained:

We need to consider how to make the optional instrument particularly attractive for small and medium-sized companies. After all, SMEs make up 99% of the businesses in the European Union. They are the lifeblood [of] our single market, and this is why I want to make transactions in the single market easier and legally more certain for them. I want also to ensure that the optional instrument takes the specificities of SMEs into account, notably the fact that they can often be the weaker party in a business-to-business context.¹²

- 6.30 Where SMEs from different member states negotiate over a contract, their negotiations may occasionally reach deadlock over which national law should govern their contract. An impasse of this sort could slow down negotiations and increase costs. In some cases, it could prevent a contract from being formed at all.

- 6.31 In its response to the European Commission's Green Paper, the Scottish Law Commission provided a fact-based example to illustrate this. Two SMEs, one Scottish, one Polish, agreed the terms and scope of an international trade agreement within a matter of days but then became embroiled in negotiations lasting several weeks over which national law should govern their contract:

As neither party had any knowledge of the other's legal system, and indeed had no accessible means of finding out the relevant law in that jurisdiction in their own language, the parties could not agree on either Polish or Scottish law. This divergence held up and complicated what should [have been] a straightforward exercise of businesses' rights to trade freely across the internal market.¹³

- 6.32 The Federation of Small Businesses had a similar story to tell. They explained that while small UK-based businesses rarely engage in cross-border trade at present, some of those which do had cited legal issues as a problem. The Federation took the view that an optional instrument on European contract law had the potential to remove the need for specialist legal advice for such trade.¹⁴

¹² Speech to Conference "Towards a European Contract Law", Leuven. 3 June 2011, p 19.

¹³ Scottish Law Commission response to the European Commission Green Paper on policy options for progress towards a European Contract Law for consumers and businesses (27 January 2011), para 2.2.

¹⁴ The Federation added that small businesses would not wish to operate with reference to different legal regimes depending on whether the contract was cross-border or domestic.

Large businesses

- 6.33 Large businesses who engage in international trade already have favourite legal systems, and they are likely to stay with the systems they know. Large businesses tend to look for systems that provide certainty.¹⁵ In its initial stages, where the CESL comes with no guiding jurisprudence, it may not provide large businesses with the certainty they require.
- 6.34 Another factor is that large businesses tend to favour legal systems which are familiar to the judges of their chosen forum.¹⁶ Thus if the parties have decided to submit their dispute to the English courts, they often use English law because the judges will be more familiar with it. It is, of course, possible to ask English judges to apply, say, German law,¹⁷ but the litigation would be more expensive and uncertain.
- 6.35 Furthermore, large businesses are unlikely to use the CESL in their dealings with small businesses. As discussed in Part 7, the draft CESL contains several protections for the weaker party, to prevent a stronger party from taking advantage of their lack of bargaining skills. For this reason, any business with the upper hand in negotiations is unlikely to choose the CESL. One advantage of stronger bargaining power is that you can impose the law of your choice, to produce the outcomes you desire.
- 6.36 That said, it is one thing to recognise that large businesses are less likely to use the CESL and another to prohibit them from using it. As we discuss below, we do not think a prohibition is justified.

LIMITS ON THE USE OF THE CESL

- 6.37 The European Commission's proposal places two limits on the use of the CESL in business-to-business contracts:
- (1) Under Article 7 of the Regulation, one of the parties must be a small or medium enterprise (SME), defined as employing fewer than 250 persons, and having a turnover not exceeding €50 million.
 - (2) Under Article 6 of the Regulation, the CESL may not be used for mixed purpose contracts which include "any elements other than the sale of goods, the supply of digital content or the provision of related services".
- 6.38 Below we consider each in turn.

¹⁵ See Stephan Vogenauer, *Civil Justice Systems in Europe: A Business Survey* conducted by the Oxford Institute of European and Comparative Law and the Oxford Centre of Socio-Legal Studies, 2008.

¹⁶ In recent research on arbitration, 68% of respondents said that choices about governing law and the seat of the arbitration influence each other. Thus a choice of English law may be coupled with a seat in London. This was considered more rational and efficient and less risky in the event of an appeal to the courts: see Queen Mary College, 2010 International Arbitration Survey.

¹⁷ For an example of a recent case in which English courts applied German law see *BMT Marine v Lloyd Werft Bremerhaven GmbH* [2011] EWHC 32 (Comm).

THE PROHIBITION ON LARGE BUSINESSES USING THE CESL

- 6.39 Recital 21 explains that in order to tackle the problems of the internal market in a “targeted and proportionate fashion” the proposal should focus on those parties who have most need of it, namely SMEs. Thus initially, in a business to business context, the CESL would be confined to contracts where at least one of the businesses is an SME. However, member states should be entitled to remove this prohibition if they wish.
- 6.40 Thus Article 7 prevents two large businesses from using the CESL between themselves. Under Article 13(b), member states may remove this prohibition.

Comment

- 6.41 Although we understand the need to start cautiously, we are not sure that this restriction to SMEs is justified. We have three concerns with it.
- (1) It conflicts with the principle that businesses should be given a free choice of law.
 - (2) We are not sure it is feasible to restrict choice of law in this way without amending the Rome I Regulation.
 - (3) The definition of an SME adds unnecessary complexity to the process.
- 6.42 We discuss each in turn.

The principle of free choice

- 6.43 The policy behind the Rome I Regulation is that businesses should have a free choice of law. We cannot see any reason to interfere with this freedom as far as large businesses are concerned. If the CESL is an acceptable choice between a large and a medium business, we cannot see why it should not be acceptable between a large business and another large business. Even if the CESL is not a good choice, we cannot see any reason to attempt to protect businesses from themselves.

Would the prohibition be effective?

- 6.44 We are not sure that the prohibition would be effective without changes to Rome I. This is because the CESL would technically be “a second contract law regime within the national law of each Member State”.¹⁸ This means that if one Member State exercises its option under Article 13(b) to extend the CESL to larger businesses, then that becomes a national law which is available for choice under Rome I.
- 6.45 For example, if one state in the EU (say Hungary) exercises this option, every large business in Europe (wherever situated) could write its contract under the CESL, as incorporated into Hungarian law.

¹⁸ This is explained in the Explanatory Memorandum, p 6.

6.46 There are already precedents for this. For example, if a UK business wishes to write an international sales contract under the CISG, it may not choose the CISG directly, but can achieve the same effect by writing the contract under Swiss law, as Switzerland has fully incorporated the CISG. The same would apply here, unless Rome I is re-written to prohibit certain choices. This, we think, would be incompatible with the principle underling the Regulation.

The definition of an SME

6.47 Under Article 7, an SME is defined as a trader which employs fewer than 250 persons, and either has a turnover not exceeding €50 million or an annual balance sheet not exceeding €43 million (or the equivalent amount in the national currency). Recital 21 explains that the definition must be interpreted according with Recommendation 2003/361. This is a long and complex document, which raises the following issues.

- (1) **Counting employees:** The Recommendation states that one should count “annual work units”, in which part-time staff count as part employees and seasonal staff count only for the proportion of the year. For example, a fruit farm which has 50 staff in the winter and 500 part-time pickers in June, should look not at the number of employees but at the number of “annual work units” it has employed. This can be a complex sum to do.
- (2) **Converting turnover figures:** If a firm has a financial year of January to December 2010, and files its accounts in April 2011, we think that these would be the relevant figures in March 2012 when the contract is signed. If so, is the relevant conversion rate the one which applies in December 2010, April 2011, or March 2012? In a world of financial instability, this could become an important issue.
- (3) **Linked enterprises:** Recommendation 2003/361 includes complex rules to distinguish between autonomous and linked enterprises. Although these rules are not referred to specifically in the draft Regulation, we think they would apply.
- (4) **Renewals:** Under Article 35.2, a contract may be concluded by usage. Take a case in which a contract arrangement proves to be very successful; the seller grows rapidly; and both sides roll over the contract, without thinking about its terms. There is a danger that the original choice of the CESL would become invalid because (unnoticed by the parties) the seller is now too large.

6.48 These issues add unnecessary complexity. The parties may be well advised to use a version of the CESL which does not include Article 7 (in the example above, Hungarian law), even if at first sight one of the parties is an SME.

Conclusion

6.49 The justification for restricting the use of the CESL appears to be a political one: commercial lawyers may be less concerned about the proposal if it does not affect their clients. On the other hand, we do not think that it can be justified as matter of principle, and it may prove impossible to enforce.

- 6.50 If the CESL is brought in, the UK Government should consider exercising its option under Article 13 to extend the availability of the CESL to large businesses contracting between themselves.

THE EXCLUSION OF MIXED-USE CONTRACTS

- 6.51 Article 1 of the Regulation outlines the subject matter of the CESL. It states that the rules can be used for “cross-border transactions for the sale of goods, for the supply of digital content and for related services”. Article 6.1 emphasises that the CESL may not be used for “mixed use contracts”:

The Common European Sales Law may not be used for mixed-purpose contracts including any elements other than the sale of goods, the supply of digital content and the provision of related services within the meaning of Article 5.

This is a significant restriction which may not be removed by member states. The main terms (“sales contract”, “digital content” and “related service”) are defined in Article 2 of the Regulation.

- 6.52 This restriction is surprising. One of the main criticisms made of the CISG is that it is a limited document, which is useful in simple sales contracts, but may be insufficiently protective in more complex deals. We had originally thought that the main use of the CESL would be in relatively complex arrangements to manufacture and export goods, involving some element of joint venture. As the British Exporters Association put it in their response to the Feasibility Study:

Whereas many exports are simple supply of goods, contracts that relate to a capital investment by the customer can be quite complex. These capital and semi-capital goods and services exports may include developmental engineering, specialised manufacture, deliveries taking place over a period of time, installation, commissioning and training services.

When does a contract become mixed use? A tentative example

- 6.53 It is not clear when an export contract strays outside the terms of Article 6 to become a mixed use contract, which is not permitted under the CESL. Below we provide an example of a relatively complex sales contract, asking which terms would stray out of the area of sales, digital content and related services into a mixed use contract. We give a provisional view, but would stress that this is highly tentative. We welcome further clarification.

- 6.54 In our example, a major British clothing retailer (B) contracts with a small Polish manufacturer (P) to supply clothing, according to B’s designs. The deal covers the following areas:

- (1) *P agrees to supply 10,000 dresses; B agrees to pay the price.*

This is the core sales contract and is covered. Under Article 2(k) a sales contract specifically includes contracts for goods to be manufactured or produced.

- (2) *The dresses are to be shipped on a CIF basis*, whereby P pays freight to and insures the goods, handing over the documents as the dresses are loaded onto the ship.

This is standard in an international commercial sales contract, and we think that it must be covered. We did consider whether the exclusion of transport and financial services in Article 2(m) might apply, but if so, almost all sales contracts would be excluded.

- (3) *B agrees to deliver the designs*. They license P to use them for some purposes, but not others

If the designs were emailed to P, they might come under the definition of a contract to supply digital content. Under the CESL, this includes content in picture form, so it could include designs and patterns. The license agreement is an integral part of any contract to supply digital content, so would appear to be covered.

- (4) *B agrees to supply and install specialist machines* (for example, to allow particularly complex stitching).

If B were to sell the machines, this would also be a sales contract, and would be covered by the CESL. The problems arise if B were to lease the machines to P. This would fail to meet the definition of a sale: under Article 2(k) ownership must be transferred from seller to buyer. Thus if the agreement included a hire clause, it would be an element other than the sale of goods. This, we think, would make it a mixed-purpose contract, and the CESL could not apply.

If the machines are lent, the installation obligation would also take the contract outside the definition. Under Article 2(m) installation may be a related service, but only if provided by *the seller*. Here installation is provided by the buyer so it would not be within the definition.

- (5) *B provides a loan* to enable P to lease an additional building.

If this was only an advance of the purchase price it would probably be covered. If however, it was more than this (for example giving B a security interest) the whole agreement would probably become mixed use, and fall outside the CESL.

- (6) *B has the right to inspect the factory*.

This is not a service, but only a way of ensuring compliance. We think this could be included.

- (7) *B provides training* in the specialist techniques required to cut their patterns and produce the stitching.

Art 2(m) suggests that this would almost certainly take the agreement outside the CESL. Training by the buyer cannot be said to be a related service for two reasons. First it is provided by the buyer rather than the seller; and secondly training services are specifically exempt.

- 6.55 This suggests that many provisions might take the deal outside the scope of Article 6.1, including hire, loans or training.
- 6.56 The training exclusion may be especially limiting. Take a case in which the parties agree a deal on the basis of the CESL, but after the initial sample products are delivered, it becomes clear there is a problem with the stitching. As a result, before the full contract is signed, the buyer agrees to provide training in their specialist techniques. This may be a useful and helpful way of addressing the problem, but it would suddenly invalidate the use of the CESL, throwing the contract negotiations into confusion.
- 6.57 We think it may be inappropriate to limit the use of the CESL in this way. The CISG already provides a common regime for simple sale of goods contracts. We had originally understood that the more protective provisions of the CESL were designed for more complex deals.

Are distribution contracts included?

- 6.58 The Draft Common Frame of Reference (DCFR) describes a distribution contract in the following terms:

Distribution contracts are contracts concluded between a supplier (who may also be the manufacturer of the products) and a distributor (who may either be a wholesaler or retailer). The supplier agrees to supply the distributor with products. The distributor commits itself to purchasing, distributing and promoting such products in its own name and on its behalf.¹⁹

- 6.59 Book IV of the DCFR deals with “specific contracts and the rights and obligations arising from them”. Part E covers commercial agency, franchise and distributorship, and includes special provisions for distribution contracts. For example, there are obligations that the parties should exchange information both before and during the course of the contract,²⁰ maintain confidentiality²¹ and make reasonable efforts not to damage the reputation of the products.²² The supplier must provide the distributor with advertising materials²³ while the distributor must make reasonable effort to promote the products²⁴ and follow the supplier’s reasonable instructions to maintain the reputation or the distinctiveness of the products.²⁵
- 6.60 These distinctive provisions are not part of the CESL. The question is whether the CESL is intended to cover distribution contracts, despite the fact that it does not include specific provisions to deal with them.

¹⁹ See Comments to IV.1- 5:101.

²⁰ See IV.E – 2.101 and 2.202.

²¹ IV.E – 2.203.

²² IV.E – 5.205 and IV.E – 5.306.

²³ IV.E – 5:204.

²⁴ IV.E – 5:301.

²⁵ IV.E – 5.304.

6.61 To answer this question we must return to Article 1 of the Regulation which outlines the subject matter of the CESL. It states that the rules can be used for “cross-border transactions for the sale of goods, for the supply of digital content and for related services”. A “sales contract” is then defined in Article 2(K) as:

any contract under which the trader (‘the seller’) transfers or undertakes to transfer the ownership of the goods to another person (‘the buyer’) and the buyer pays or undertakes to pay the price thereof....

6.62 There are many distribution contracts which do not meet this definition. The agreement may not transfer title in the goods to the distributor. It may be for services rather than for goods. The DCFR further explains that distribution agreements are framework agreements (“*contrat cadre*”) which provide the context for subsequent contracts (“*contrat d’applications*”). It may be that the framework agreement does not include undertakings either to transfer ownership or to pay the price, in which case the CESL would not apply; but any subsequent contracts may very plausibly involve such elements and would therefore be likely to fall within the CESL.

6.63 On the other hand, if title in the goods is transferred from seller to buyer and the buyer agrees to pay the price under the distribution contract itself, the definition of a sales contract would be met. It would therefore fall within the scope of the CESL, unless it included a related service which fell outside the terms of Article 2(m) of the Regulation, such as transport, training or financial services. There is nothing otherwise to suggest that distribution contracts are specifically excluded.²⁶ We have therefore tentatively concluded that distribution contracts involving the sale of goods are intended to be included in so far as their terms cover sale of goods, through we would welcome further clarification on this point.

Should the CESL be interpreted in the light of the DCFR?

6.64 This raises a further point. What is the status of the various provisions of the DCFR which have not been included in the CESL? Many of the provisions in Book IV are specific examples of the more general principle of good faith and fair dealing, and it would be possible to interpret the general provisions of the CESL in light of these principles. On further reflection, however, this approach may not be consistent with Article 4, which states that the CESL must be interpreted autonomously. Article 4.2 states that:

Issues within the scope of the Common European Sales Law but not expressly settled by it are to be settled in accordance with the objectives and principles underlying it and all its provisions, without recourse to the national law that would be applicable in the absence of an agreement to use the Common European Sales Law or to any other law.

²⁶ The agreement may include an obligation for the seller to provide advertising material – but if this were conveyed electronically it would be digital content, and if on paper, it would be goods.

- 6.65 It is not clear whether the DCFR is to be considered “any other law” for these purposes. The recitals to the CESL make no mention of the DCFR, suggesting that the DCFR has no special status in interpreting the CESL. Courts may find the commentary to the DCFR helpful, but we think that its status as an interpretive guide is intended to be weak. Again, we would welcome clarification on this point.

CONCLUSION

- 6.66 The current law of cross-border transactions allows businesses contracting with other businesses a free choice of national legal systems.
- 6.67 The main problem appears to be that businesses have too much choice. It is difficult for small and medium enterprises to find out about different legal systems, as this usually involves expensive legal advice. Businesses tend to favour their own legal system, making it difficult to negotiate on choice of law with businesses from other states.
- 6.68 The CESL would provide another possible choice. If the CESL provides such obvious benefits that everyone would agree to use it without difficult negotiations, it would remove a source of business stress. On the other hand, if the CESL is just one more choice, this would add to the current complexity. In Part 7 we consider whether CESL fulfils the promise of one simple, neutral legal system, with such obvious benefits that businesses would no longer need to negotiate over choice of law.
- 6.69 Under the proposed Regulation, two restrictions are placed on the use of the CESL. The first is that the CESL could not be chosen by a large business contracting with another large business. This restriction does not appear either principled or practical. Member states are given the option to remove this restriction, and we think that the UK Government should exercise this option.
- 6.70 Secondly, the CESL may not be used for “mixed-use” contracts, which include any elements other than the sale of goods, the supply of digital content or the provision of related services. We have attempted to interpret this article. We provisionally think the CESL is intended to cover distribution contracts in which the seller undertakes to transfers title in the goods to the distributor and the distributor undertakes to pays the price. On the other hand, the CESL is not intended to be used in joint ventures where, for example, one party provides training, or loans, or supplies equipment on hire. There may be many other common cases. We are not sure that this an appropriate distinction and think that the issue merits further debate.

PART 7

COMMERCIAL CONTRACTS: DOES THE CESL MEET THE NEEDS OF BUSINESSES?

INTRODUCTION

- 7.1 In this Part we provide a brief overview of the main provisions of the draft Common European Sales Law (CESL) as it applies in businesses-to-business contracts.
- 7.2 As noted in Part 6, for most businesses selling goods to other businesses across EU borders, the default regime is currently the United Nations Convention on Contracts for the International Sale of Goods (CISG), also referred to as the “Vienna Convention”. We start by comparing the two regimes, to see why businesses may prefer to use the CESL rather than the CISG.
- 7.3 We then look at how the CESL might be used in standard-term contracts. We consider the possibility that a small or medium enterprise (SME) might include a clause choosing the CESL within its standard terms. Although there is nothing in the Regulation to prevent this, such a clause would need to be brought to the attention of the other party.
- 7.4 We then consider the content of the CESL. We give a brief overview of the CESL’s most distinctive provisions. We ask how well these provisions would meet the needs of the SMEs for which it is intended. The CESL puts considerable emphasis on fairness, allowing judges discretion to alter contract terms in some cases, and giving possible compensation for actions not carried out in good faith. Our concern is that, at least in the early days of the CESL, this might create uncertainty. There is a danger that this uncertainty may give an undue bargaining advantage to the party most able to litigate, disadvantaging the party who is less able to bear the costs of court action.

WHY CHOOSE THE CESL RATHER THAN THE CISG?

- 7.5 In most EU states, the CISG is the default regime for businesses contracting with other businesses for the international sale of goods. Where both parties are habitually resident in states which have ratified the CISG, the CISG applies unless the parties make an express choice of some other regime. It does not apply to consumer sales.
- 7.6 The UK has not ratified the CISG, along with three other EU states: Malta, Portugal and the Republic of Ireland. For UK businesses (and businesses from the other three states), the parties may choose to use the CISG if the other party is from a CISG country. They may also incorporate the CISG indirectly, by choosing the law of a country which fully incorporates the CISG (such as Swiss law).

7.7 In business-to-business cross-border contracts for the sale of goods, the CESL is now promoted as a direct competitor to the CISG. The implicit conclusion is that the CISG has failed, and should be replaced by an alternative system. Given the significance of this conclusion, there is remarkably little discussion of the CISG in the European Commission's Communication. The Communication includes one paragraph on the subject:

At the international level, a set of rules of a broader scope for B2B transactions was introduced by the 1980 UN Convention on the International Sales of Goods (the Vienna Convention). However, the Vienna Convention was not ratified by all Member States and is not applicable in the UK, Ireland, Portugal and Malta. It does not cover the whole life-cycle of a contract comprehensively and (in the absence of a compulsory jurisdiction within the UN system comparable to the one offered by the European Court of Justice for the EU's single market) contains no mechanism ensuring its uniform application as different national courts may interpret it differently. Only a relatively small number of traders use the Vienna Convention.¹

7.8 Similarly, a report from the European Parliament in April 2011 concluded that an option system of European Contract Law would have a clear advantage compared with the CISG as it would "provide legal certainty under the jurisdiction of the Court of Justice and language plurality".²

7.9 The CISG has several advantages. It is used widely throughout the world, not just the EU. It has been used since 1988. A generation of lawyers has been educated about it, and there is a growing body of case law about how to interpret it. On the other hand, five criticisms are made of the CISG. These are:

- (1) The CISG has not been ratified by four member states, including the UK.
- (2) The CISG is unduly limited, and fails to cover the whole life-cycle of the contract.
- (3) Different countries interpret it differently, and there is no mechanism for resolving these differences. By contrast, disputes under the CESL would be resolved by the European Court of Justice.
- (4) The CESL provides greater language plurality: authoritative versions would be available in languages of all member states.
- (5) Only a minority of traders currently use the CISG.

7.10 We look at each point in turn.

¹ Communication from the European Commission, A Common European Sales Law to facilitate cross-border transactions in the single market, Com (2011) 636 final, p 5.

² See Communication for the Commission of 22 October 2009 on Cross-Border Business to Consumer e-Commerce in the EU (COM(2009)0557), quoted in European Parliament, "Report on Policy Option for Progress towards a European Contract Law", Rapporteur Diana Wallis, 18 April 2011, p 15.

The CISG has not been ratified by four states, including the UK

7.11 The fact that the UK, Ireland, Portugal and Malta have not ratified the CISG is an obvious weakness. Over the years, there have been many calls for the UK to ratify the CISG. As the Scottish Law Commission commented in its 1993 Report on Formation of Contracts:

The Scottish Law Commission, when consulted as part of the consultation exercises carried out by the Department of Trade in 1980 and by the Department of Trade and Industry in 1989, recommended that the United Kingdom should become a party to the Convention. The English Law Commission has also given a favourable response.³

7.12 The Report commented that that:

The Convention contains a modern, internationally agreed set of rules on the formation of certain contracts. These rules now apply very widely in international trade.⁴

7.13 The Scottish Law Commission saw “obvious advantages for Scottish traders, lawyers and arbiters in having our internal law the same as the law which is now widely applied throughout the world in relation to contracts for the international sale of goods”.⁵ In the absence of ratification, the Scottish Law Commission considered whether the more general rules on contract formation in the Vienna Convention could be adopted as part of the general law of Scotland on the formation of contracts.

7.14 The calls for the UK to ratify will continue, though it may be more difficult to achieve ratification if the CESL were to be introduced.

³ Scottish Law Commission, Report on Formation of Contracts: Scottish Law and the United Nations Convention on Contracts for the International Sale of Goods (1993) Scot Law Com No 144, para 1.7.

⁴ Above.

⁵ Above.

“The CISG is unduly limited”

- 7.15 The CISG is a much shorter document than the CESL. Its substantive provisions run to less than 9,000 words,⁶ compared to over 26,000 words in the CESL.⁷ In some ways, this makes it a more concise, user-friendly document. On the other hand, it also leaves a wide range of issues to national law, including duties of disclosure and rules on mistake and fraud. The UNIDROIT Principles of International Commercial Contracts have been drafted in an attempt to fill in these gaps, but these principles are soft law, and may not be chosen directly under Rome I.⁸
- 7.16 The CISG is also less protective towards vulnerable parties. Under the CISG, good faith is merely an interpretive principle,⁹ and the CISG does not include any provisions against unfair terms. Under the CESL, a breach of good faith may lead to specific consequences (a remedy or the unavailability of a remedy).
- 7.17 We can see that the wider provisions of the CESL may be useful in more complex deals, though we are not sure they are crucial in simple sales contracts. Meanwhile, the protective provisions may be helpful to some small businesses. There is a danger, however, that those most liable to be exploited by a party with greater bargaining power would be required to contract under that party’s choice of a law other than the CESL.

“The CISG lacks authoritative rulings”

- 7.18 A criticism made of the CISG is that it has been interpreted inconsistently by national courts.¹⁰ For example, the German Supreme Court found that it is not the duty of the seller to ensure that goods meet the public health regulations of the buyer’s home state,¹¹ while the French courts have found that it is.¹²
- 7.19 One advantage of the CESL is that these types of disagreement can be resolved by the European Court of Justice (CJEU). This, however, is not necessarily an attractive prospect for the businesses concerned. Taking disputes to the Court of Justice can be slow and expensive. As the Swedish Government commented in its response to the European Commission’s 2010 Green Paper:

⁶ This does not include the provisions on how the Convention may be ratified.

⁷ Again, this relates only to the substantive provisions in Annex 1 and does not include the proposed Regulation itself.

⁸ The third edition of the Principles was published in 2010. It has 211 articles in 11 chapters, including (for example) chapters in illegality, set-off and assignment of contracts. The UNIDROIT’s website is <http://www.unidroit.org/>. The 2010 edition is available at <http://www.unidroit.org/english/principles/contracts/main.htm>. The UNILEX website is an important tool to understand the Principles as it provides official comments, cases and a bibliography relating to all the articles and book about the Principles: see <http://www.unilex.info/dynasite.cfm?dssid=2377&dsmid=14311>

⁹ CISG, art 7(1).

¹⁰ See M J Bonell and F Liguori, ‘The UN Convention on the International Sale of Goods: A Critical Analysis of Current International Case Law’ (1997) 2 *Revue de Droit Uniforme* 385.

¹¹ Bundesgerichtshof VIII ZR 159/94.

¹² *Caiato Roger v La Société française de factoring* (1995) 93/4126.

Parties must be assured that legal disputes would be resolved uniformly throughout the EU immediately, not in a few decades' time... The European Court of Justice already has long processing times, to which are often added long processing times in the national courts as well. The business sector cannot wait for years for disputes in such a key area as contract law to be resolved.¹³

7.20 According to the European Court of Justice annual report, it has faced a consistent backlog of 700 to 800 cases for each of the past five years.¹⁴ In 2010, the average time from reference by the national court to judgment by the CJEU was 16.1 months. The delays before the EU's General Court are longer. In 2010, there was a backlog of 1,300 cases, with an average delay of 28 months.¹⁵ If the CESL led to an influx of business contract disputes, provision would need to be made for additional resources.

7.21 The problem with these delays is that they are additional to the delays caused by national courts. For this advice, we analysed ten recent cases and found that the litigation had continued for an average of 59 months by the time the CJEU gave judgment. Nor does the CJEU judgment conclude the issue. Following the reference, the case will then return to the national court. One recent case concerning whether chocolate-covered teacakes attracted VAT took 13 years to conclude and two references to the European court.¹⁶ SMEs may be wary of becoming involved in this sort of litigation.

“The CISG fails to provide language plurality”

7.22 Authoritative versions of the CISG exist in six languages, including three EU languages: English, French and Spanish. The other languages are Russian, Arabic and Chinese.

7.23 By contrast, the EU has 23 official languages. All legislation must be published in each language, and all 23 languages are equally authoritative. The leading case emphasises that as each language is equally authentic, it is necessary to compare different versions.¹⁷

7.24 This would have the advantage of the making the CESL accessible. There is, however, a risk that the different versions may convey different meanings, which would increase uncertainty. It may also make litigation more prolonged, as the differences in meaning between versions are resolved.

¹³ The Swedish Government's views on the Green Paper on European contract law, p 6.

¹⁴ http://www.theioi.org/downloads/7muqr/ECJ%202010_version_integrale_en.pdf, p 83 and p 97 (Accessed 7 September 2011).

¹⁵ Above, p 175. Chart 9 shows that in the General Court in 2010 the median delay was 24 months, and the mean delay 28 months.

¹⁶ *Marks & Spencer Plc v Customs and Excise Commissioners (No.5)* [2009] UKHL 8, [2009] 1 All ER 939.

¹⁷ *Case 283/81 Srl CILFIT and Lnificio di Gavardo SpA v Ministry of Health*.

7.25 The recent case of *Weber v Wittmer*¹⁸ illustrates how the court considers a selection of languages. The case considered the extent of the seller's liability to "replace" faulty goods, as required by the Consumer Sales Directive. Was the seller of faulty tiles merely obliged to provide new tiles, or did it also have to bear the cost removing the old tiles and installing the new ones? To resolve this issue, the court considered at least eight languages.¹⁹ As the Court commented:

With regard to the term 'replacement', it should be noted that its precise scope varies in the different language versions. While in some of those language versions, such as the Spanish ('sustitución'), English ('replacement'), French ('remplacement'), Italian ('sostituzione'), Dutch ('vervanging') and Portuguese ('substituição'), that term refers to the operation as a whole, on completion of which the goods not in conformity must actually be "replaced", thus obliging the seller to undertake all that is necessary to achieve that result, other language versions, such as in particular the German language version ('Ersatzlieferung'), might suggest a slightly narrower reading.²⁰

7.26 The CJEU uses four competing tests to resolve conflicts between languages:

- (1) Identify the clearest version and disregard ambiguous versions;²¹
- (2) Identify and accept the wording contained in the majority of the different versions;²²
- (3) Identify and accept the version which is deemed to best reflect the legislature's intent (even if it is statistically in the minority);²³
- (4) Contrast the version in question against the version in which the legislation was drafted.²⁴

¹⁸ Case C65/09 *Gebr. Weber GmbH v Jürgen Wittmer* (2011) (unreported).

¹⁹ The other language, Slovak, was referred to by the Advocate General.

²⁰ Case C65/09 *Gebr. Weber GmbH v Jürgen Wittmer* (2011), at para 54.

²¹ Case 45/83 *Ludwig-Maximilians-Universität München v Hauptzollamt München West* [1984] ECR I-00267.

²² Case C-64/95 *Konservenfabrik Lubella Friedrich Büker GmbH & Co. KG v Hauptzollamt Cottbus* [1996] ECR I-05105.

²³ Case 76/77 *Auditeur du travail v Bernard Dufour, SA Creyf's Interim and SA Creyf's Industrial* [1977] ECR I-2485.

²⁴ Case C-265/03 *Igor Simutenkov v Ministerio de Educacion y Cultura, Real Federacion Espanola de Futbol* [2005] ECR I-2579, opinion of Advocate General Stix-Hackl.

7.27 It is difficult to say which test is adopted most frequently, but the final test is the least common. Advocate General Jacobs described Option 4 as merely a “supplementary means of interpretation”²⁵ whilst Professor Solan of Brooklyn Law School suggests that this was just an approach adopted in early cases. He criticises it as being the “functional equivalent of selecting an official language” which “offends against basic notions of sovereignty and equality among the members”.²⁶

7.28 The cost of considering different language versions becomes a particular problem in private litigation. If the parties wish to predict how the CJEU would interpret a word or phrase in the CESL, they would be well-advised to take advice on its meaning in a selection of different languages. This may be particularly difficult for SMEs.

“The CISG is not used”

7.29 The European Commission cites the Eurobarometer survey to show that “only a relatively small number of traders use the Vienna Convention”. The survey asked firms “which contract law most often governs your business to business cross-border transactions”. They were provided with five possible answers, which drew the following results:

- (1) The national contract law of [their own country]: 60%;
- (2) The national contract law of the country where the other party is based: 15%;
- (3) The national contract law of a third country: less than 1%;
- (4) “Contract laws not related to any particular country, eg international conventions or UNIDROIT principles”: 9%;
- (5) Don’t know/not applicable: 17%. It appears that 8% did not trade across borders, while 9% did trade, but did not know what law they used.

7.30 Most of the businesses in the study were small: 79% had 9 or fewer employees. Such businesses tend to have a low awareness of contract law issues. As the analytical report makes clear, these answers therefore reflect businesses’ impression, rather than the actual choice of law.²⁷ That may be why over half (60%) claimed that the national contract law of their own country most often governed their business to business cross-border transactions. Logically, that is unlikely to be the case.

²⁵ Case C-6/98, *Arbeitsgemeinschaft Deutscher Rundfunkanstalten (ARD) v PRO Sieben Media AG* [1999] ECR I-7599.

²⁶ L Solan, “The interpretation of multilingual statutes by the European Court of Justice” [2009] *Brook J Int’l L* 277 at 287.

²⁷ See European Contract Law in Business-to-Business Transactions: Analytical Report, p 7: “The majority (60%) of the surveyed enterprises had the impression that their own national law applied to the transaction”.

- 7.31 The survey did not specifically mention the “Convention on International Sale of Goods” or the “Vienna Convention”. For many member states, the CISG has been incorporated into national law: thus many businesses may think of these provisions as their own law, rather than law unrelated to a country. Furthermore, the CISG operates as a default regime; those who have given no thought to choice of law may be genuinely unaware that it applies to their contracts. We do not think these results indicate the use made of the CISG.
- 7.32 If it is true that many businesses are contracting out of the CISG, the reasons for this would need to be explored in more detail. Unless we know why businesses distrust the CISG, we cannot say whether or not the CESL would be more suited to their needs.

Conclusion

- 7.33 Several criticisms may be levelled at the CISG, but we are not sure that these criticisms necessarily require the EU to start again with a different system.
- 7.34 In the short term, the proposal is that the systems should co-exist. The CISG will be the default regime, and the CESL could be explicitly chosen by the parties. The market will decide which it prefers. On the other hand, the main problem with the current system is too much choice. The existence of two separate supra-national systems of law to govern cross-border sales contracts may confuse businesses, and lead to more difficult negotiations.

STANDARD-TERM CONTRACTS

- 7.35 Standard terms are used in two ways: firms may draft their own set of terms, or they may use industry standard terms, drafted by trade associations. Legally, it is difficult to distinguish between these two uses.²⁸ In commercial terms, however, the two approaches may differ. Whereas internal terms are often drafted by one side and imposed on the other, industry terms usually represent careful negotiations between representatives of the parties.
- 7.36 Here we start by looking at terms drafted by one party. We then consider whether the CESL would be used for industry terms.

Standard terms written by one party to the contract

- 7.37 In practice, those who routinely sell goods to other businesses often write a set of standard terms and use them for all sales, unless the buyer objects. The Regulation does not require commercial parties to use any formalities in how they choose to use the CESL. For business-to-business contracts, Article 8.1 only requires “an agreement of the parties to that effect”.

²⁸ In the Law Commissions’ joint report on unfair terms we argued that although industry terms often represented a fair balance, some may be drafted by a trade association representing the interests of only one party and imposed on the other side. Although the provenance of the terms may be highly relevant to their reasonableness, one could not make a clear cut division between the two: see *Unfair Terms in Contracts* (2005) Law Com No 292, Scot Law Com No 199, para 4.61.

- 7.38 This would allow businesses to specify the CESL as a choice of law within their standard terms. To do this, however, the business would need to make sure that it was not engaged in a “battle of the forms”. It would also need to take reasonable steps to bring the choice of law to the attention of the other party.

The “battle of the forms”

- 7.39 The “battle of the forms” is a common commercial problem. Typically, it occurs where a commercial buyer orders goods on a purchase order form. The front of the form sets out the buyer’s requirements (including a description of the goods, quantity ordered, price, place and time of delivery). The back has a set of standard terms. The seller accepts the order on an “acknowledgment of order” form. The main requirements are agreed, but the seller’s form includes a rival set of standard terms. Neither side puts their mind to the difference between the standard forms until something goes wrong, when the court is asked to decide which terms are to be included in the contract.
- 7.40 Resolving the battle of the forms can be complex, especially if the parties send a long series of emails and forms to each other. It also causes difficulties where the standard forms include different choice of law clauses, because then the dispute is not only about who wins the battle, but also about which rules should govern the battle.
- 7.41 Different legal systems vary in their approach to the battle of forms. The UK courts tend to apply a “last shot wins” rule. The exchange of forms is interpreted as a series of offers and counter-offers, with the last form to be sent constituting the final offer which is accepted.²⁹ Under the CESL, the issue is governed by Article 39, which states that where the offer and acceptance refer to conflicting standard terms, the standard terms form part of the contract only “to the extent that they are common in substance”.
- 7.42 Where one set of terms is governed by English or Scots law, and one set by the CESL, this could lead to surprising results. Take a case in which an English buyer ordered goods on standard terms written under English law. A Portuguese supplier acknowledged the order, with terms written under the CESL. Under English law, the buyer’s form is ineffective. Instead, the contract is written on the supplier’s terms, which was the “last shot fired”. The English courts would consider the choice of the CESL to be valid. Yet under the CESL, the term incorporating the CESL would be ineffective. Only terms which were common between the parties form part of the contract, and the adoption of the CESL was not one of them.
- 7.43 According to Article 10(1) of Rome I, a choice of law clause must be valid under the law which it purports to choose. In this scenario, neither choice of law clause is valid. The buyer’s choice of English law is not valid under English law, and the seller’s choice of the CESL is not valid under the CESL. This means that the default law would apply, which in this case would be Portuguese law.

²⁹ See *Tekdata Intercommunications v Amphenol Ltd* [2009] EWCA Civ 1209; 1 Lloyds Rep 357, which rejected previous cases suggesting neither set of terms were applicable.

The need to bring the CESL clause to the other party's' attention

7.44 Under Article 70, non-negotiated terms supplied by one party:

may be invoked against the other party only if the other party was aware of them or the party supplying them took reasonable steps to draw the other party's attention to them before the contract was concluded.

7.45 This has the same effect. If a party writes standard terms under the CESL, but then fails to bring the choice of the CESL to the buyer's attention, the term choosing the CESL would be invalid. The applicable law would be the default law set out in Rome I.

7.46 Firms who are aware of contract law issues would find this relatively easy: asking the other party to sign and return the document would probably suffice. It would be more difficult for the small firms in the European Commission's survey who gave no thought to choice of law issues. We think it would be helpful if the European Commission explained in practical terms how the CESL could be incorporated into a standard contract.

Industry standard terms

7.47 Industry standard terms drafted by trade associations are a common and extremely important way of contracting. They are particularly useful for small businesses, which do not have the resources to draft their own terms. Many of the problems encountered by small businesses noted earlier would be resolved if they could reach for a trustworthy set of terms drafted to meet their particular needs.

7.48 In April 2011, the European Parliament's report noted that:

Whilst an optional instrument will have the effect of providing a single body of law there will still be need to seek provision of standard terms and conditions of trade which can be produced in a simple and comprehensible form, available off-the-shelf for businesses, and in particular SMEs and with some form of endorsement to ensure consumer confidence.³⁰

7.49 It is not the responsibility of the European Commission to draft standard terms on behalf of businesses. If, however, problems over contracting are proving to be a barrier to the internal market, it would be legitimate for the Commission to encourage trade associations to draft suitable contracts, perhaps by making funding available. We would welcome initiatives of this type. We think that it would address many of the issues raised by businesses in the study.

7.50 The European Parliament thought that an optional instrument would offer a better choice of law for such standard terms. It noted that:

³⁰ European Parliament – Committee on Legal Affairs, Report on policy options for progress towards a European Contract Law for consumers and businesses, 18 April 2011, para 30.

Standard contract terms and conditions based upon a [Common European Sales Law] would offer greater legal certainty than EU-wide standard terms based upon national laws which would increase the possibility for differing national interpretations.

7.51 Below, we discuss the tension between certainty and fairness, and describe how the CESL leans towards the fairness end of the spectrum. We are not sure that the CESL, as currently drafted, would necessarily be more certain than national law. One advantage of the CESL is that it would, ultimately, be interpreted by the European Court of Justice but, as we have seen, it will take time to build up a body of case law.

7.52 It will be important for the European Commission to consult trade bodies to see if they feel that the CESL offers advantages over current national laws.

THE CONTENT OF THE CESL

7.53 The CESL includes freedom of contract as a general principle. Article 1 states that:

Parties are free to conclude a contract and to determine its contents, subject to any applicable mandatory rules.

7.54 Article 2 sets out another general principle: good faith and fair dealing. It must be interpreted in the light of Recital 31, which states:

The principle of good faith and fair dealing should provide guidance on the way the parties have to cooperate. As some rules constitute specific manifestations of the general principle of good faith and fair dealing, they should take precedence over the general principle. The general principle should therefore not be used as a tool to amend the specific rights and obligations of parties as set out in the specific rules. The concrete requirements resulting from the principle of good faith and fair dealing should depend amongst others, on the relative level of expertise of the parties and should therefore be different in business-to consumer transactions and in business to business transactions. In transactions between traders, good commercial practice in the specific situation concerned should be a relevant factor in this context.

7.55 The important issue, therefore, is whether traders observed good commercial practice in the specific situation. The CESL allows judges discretion to intervene to ensure that good commercial practice is observed.

7.56 There is a tension between these two principles, which we discuss below.

The tension between certainty and fairness

- 7.57 All systems of commercial contract law must grapple with the tension between certainty and fairness. How far should the parties be held to the words of the agreement they have reached? And how far should a judge re-interpret that agreement, to do justice between the parties? It is an old problem. In 1598, it formed the central tenet of Shakespeare's play, *The Merchant of Venice*. Should Antonio be held to his voluntary agreement that if he is unable to repay the loan, the penalty should be "a pound of flesh"? Or was that an unfair contract term, to be tempered by "the quality of mercy"?
- 7.58 There is no easy answer to this tension. Each contract system needs to find an appropriate balance. Nowadays, no system would actually permit bodily injury as a penalty for late-payment of a debt. Nor would any system regulate relations simply through a judge's retrospective view of what is fair. But different systems find the balance in different places. English law has a reputation for leaning towards the certainty end of the scale.³¹ By contrast, the CESL is firmly towards the fairness end.

The emphasis on good faith and fair dealing

- 7.59 The CESL sets high standards of good faith, fair dealing and openness. Furthermore, it provides many discretionary remedies to a party who has suffered from a lack of good faith. These provisions can be seen throughout the document. Here we highlight six such articles:
- (1) Article 2 states that each party has a duty to act in accordance with good faith and fair dealing, defined as "a standard of conduct characterised by honesty, loyalty and consideration for the interests of the other party". Under the CISG, this acts only as an interpretive principle. By contrast, under the CESL, breach of the duty gives rise to direct liability. Under Article 2(2), it may preclude the party in breach from relying on a right, remedy or defence they would otherwise have, and may also make that party liable for loss. Article 2 must be read subject to Recital 31, set out above.³²
 - (2) Under Article 23, a seller has a duty to disclose any information concerning the main characteristics of any goods or services which "it would be contrary to good faith and fair dealing not to disclose". This duty is to be interpreted with regard to a range of circumstances, including "good commercial practice".³³ This goes further than the equivalent duty in English and Scots law, which is normally confined to not making misrepresentations.³⁴

³¹ For example, English law does not recognise a general obligation to act in good faith: see *Walford v Miles* [1992] 2 AC 128.

³² See para 7.54.

³³ See Art 23.2(f).

³⁴ A wider duty of disclosure exists for a limited class of contracts, including insurance, partnership, agency and guarantees.

- (3) Under Article 55, a party who has made a mistake may in some circumstances claim against a non-mistaken party who has not acted in good faith. When read in conjunction with Article 48, Article 55 allows a party who made a mistake of fact or law to claim damages against another party who “knew or could be expected to have known of the mistake” but caused the contract to be concluded by failing to point out the mistake, contrary to the requirement of good faith and fair dealing. In English or Scots law, a party would not be liable for damages for failing to point out the other party’s mistake, but only for making a negligent or fraudulent misrepresentation that caused the party to enter into the contract.
- (4) Under Article 51, a party may avoid a contract if they were “in economic distress or had urgent needs” or were “improvident, ignorant or inexperienced” and the other party knew this and took unfair advantage of it. In English law, the equivalent doctrine, “undue influence” is confined to cases where there is a special relationship of trust and confidence between the parties.³⁵ The Scots law doctrines of undue influence and lesion may be wider, but are unlikely to be applied to a commercial contract.³⁶ The CESL approach allows a court more extensive powers to intervene to protect the ignorant and inexperienced.
- (5) Under Article 86, the court may strike out a term in a set of standard terms if it “grossly deviates from good commercial practice, contrary to good faith and fair dealing”. In UK domestic law, unfair terms intervention is confined to exclusion terms, and terms which permit a party to render a performance substantially different from what was reasonably expected.³⁷ By contrast, Article 86 covers a wide range of terms. The only terms to be exempt are those which relate to the main subject matter of the contract and the price.³⁸ That said, the term must not simply be unfair: it must “grossly deviate” from good commercial practice.
- (6) Article 89 applies where “performance becomes excessively onerous because of an exceptional change of circumstances”. In these circumstances, the parties have a duty to negotiate in good faith “with a view to adapting or terminating the contract”. If one side fails to negotiate in good faith, it is possible that the injured party may be entitled to claim damages for breach of good faith and fair dealing under Article 2.2, though this is far from certain. The main remedy is set out in 89.2: either party may ask a court to adapt the contract in line with what the parties would reasonably have agreed had they known about the exceptional change of circumstance.

³⁵ See Chitty on Contracts (30th Edn), para 7-0560.

³⁶ For further discussion of the difference between the English and Scottish approaches in this area, see Law Commission and Scottish Law Commission, Consumer Redress for Misrepresentation and Aggressive Practices (2011) paras 7.56 to 7.58.

³⁷ Unfair Contract Terms Act 1977, ss 2 and 3.

³⁸ See art 80.3. Terms are also exempt from review if they reflect the existing law: art 78.1.

- 7.60 There are other differences between the CESL and contract law in England and Scotland. For example, under Article 59, when a court interprets a contract, it can look at a wide range of issues, including preliminary negotiations, the subsequent conduct of the parties and good faith. By contrast, in 2009, in *Chartbrook Ltd v Persimmon Homes Ltd*, the House of Lords held that pre-contractual negotiations may be relevant to establish the surrounding context of a contract, but could not be used to establish the parties' intentions.³⁹ The same rule applies in Scots law.⁴⁰
- 7.61 In February 2011, the Scottish Law Commission consulted on possible changes to the current rule in Scots law. It described the distinction between context and intentions as difficult to draw.⁴¹ Furthermore, it might deprive the court of potentially relevant evidence. However, there was a possible danger that allowing a generous approach to evidence of pre-contract negotiations may increase the costs of trials and lead to uncertainty and inconsistency. The Scottish Law Commission thought that abuse could be controlled by judges' case management powers, by the Scottish system of pleading and by judicial discretion to make cost orders against "any party who chooses to deluge the court with material without having ensured its relevance to the issue in dispute".

DOES THE CESL ACHIEVE THE RIGHT BALANCE FOR ITS MARKET?

- 7.62 In the Feasibility Study, the European Commission provided a hypothetical example to illustrate the type of case where a new optional system of contract law would be particularly useful. We summarise the example as follows:

Mr K, the owner of a small Polish company, develops an organic wooden bed for children. He takes part in a trade fair for which he pays a €2,500 participation fee. His beds attract the attention of German and Italian retailers. Mr K's company has the capacity to sell to both retailers so he starts negotiations. Mr K then approaches Ms J, a local lawyer, for legal advice on the draft sales contracts. Ms J discovers that they are to be governed by German and Italian law and recommends that Mr K use his own standard contract governed by Polish law. The German and Italian retailers do not want this as they are not familiar with Polish law. Ms J advises Mr K to use an international law firm in Warsaw to advise him, which would cost €10,000. Mr K considers this to be unaffordable.

- 7.63 If Mr K simply wished to export a give number of beds to Italy and Germany in one-off transactions, the CISG would appear to provide a neutral and tested solution to the problem. It is possible, however, that the CISG may be too limited in its scope to cover more complex, on-going deals, such as those involving some form of exclusivity. We have considered how well the CESL provisions would meet Mr K's needs if he were entering into an exclusive sales agreement with a medium or large business. Would the parties be more likely to value certainty or fairness? That depends on the way they conduct their negotiations.

³⁹ [2009] UKHL 38. [2009] 1 AC 1101.

⁴⁰ *Luminar Lava Ignite Ltd v Mama Group plc* 2010 SC 310 (Inner House).

⁴¹ Scottish Law Commission, Review of Contract Law: Discussion Paper on Interpretation of Contract DP No 147(2011), para 7.13.

Negotiating strategies

- 7.64 There are two basic strategies to negotiating a contract: “front-loading” and “back-loading”. In the first strategy, “front-loading”, the parties put considerable resources into negotiating every aspect of the deal, anticipating possible problems and agreeing solutions. Businesses usually use lawyers to do this, often because lawyers emphasise problems, at a time when entrepreneurs focus on opportunities. This careful negotiation will have a cost – in terms of time, emotion and legal fees. If the parties incur this cost, they would not welcome the possibility that a judge will unpick the agreement they have crafted so carefully. If parties use the “front-loading” strategy, they will want certainty – to know that the agreement will be upheld.
- 7.65 Under the alternative strategy, “back-loading”, the parties will look only at the main elements of the deal – the subject matter and the price. They will ignore possible problems, and assume lawyers and judges would sort things out if it all goes wrong. Lawyers tend to disapprove, but many deals are done on this basis. That is why the “battle of the forms”, discussed earlier, remains such a common problem. The parties simply do not have the time or resources to put effort into negotiating solutions to problems which may never happen. When the risk of problems is low, this is an economically rational approach.
- 7.66 Parties who use a “back-loaded” approach will want a legal system that has clear, sensible default rules, tempered with a substantial element of fairness. They will not wish to be caught by some harsh standard term which no-one paid any attention to at the time. That is why, even in the UK, the Unfair Contract Terms Act 1977 allows a court to consider the fairness of exclusion clauses in standard terms. The parties may welcome an extension of unfair terms provision, such as that set out in the CESL.
- 7.67 So which strategy should Mr K take to negotiating an exclusive agreement with his Italian buyers? This depends on the balance of risks. He should use a back-loaded strategy if there is a low risk of problems occurring, or if, when problems do occur, they can be resolved easily, for example through small compensation payments. It may also make sense to back-load the cost of sorting out problems if he has access to a trustworthy, low-cost system of dispute resolution, such as an arbitrator. In this context, it would make sense to choose the CESL, on the grounds that it gives the arbitrator considerable discretion to do justice between the parties.
- 7.68 On the other hand, Mr K should negotiate carefully if the deal has a high risk of causing problems, and those problems would be serious or catastrophic for his business, and the costs of litigation would be high. If he enters into a high risk deal without access to a low-cost dispute resolution system, he should be wary of an undue emphasis on fairness (and the open-ended judicial discretion and uncertainty that goes with it). Prolonged litigation can be a test of endurance and resources. There is a danger that if a legal system gives too much scope for litigation, any final resolution will reflect the parties’ ability to litigate, rather than the merits of the case.
- 7.69 In complex high-risk deals, we think that the CESL may lean too far towards fairness at the expense of certainty. Below we illustrate this point with an example.

An example: a dispute over a break clause

- 7.70 In this example, Mr K, the owner of a Polish firm making children's beds, enters into an agreement with an Italian retailer, ICO, which owns a chain of furniture stores across Italy. Mr K grants ICO exclusive rights in the Italian market. The agreement is to last for five years. However, Mr K insists on the right to terminate the agreement after one year if the Italian firm does not achieve a minimum level of sales. The parties agree that Mr K can terminate the agreement unless 100 beds are sold in the first year.
- 7.71 As the year progresses, Mr K becomes increasingly dissatisfied with ICO. Mr K is unhappy that they do not stock the bed in their more prestigious Milan store, and that their enthusiasm for the bed is fading. He discusses the matter with a rival firm, who think they can do better. At the end of the year, only 90 beds have been sold. Mr K exercises his right under the break clause to terminate the agreement.
- 7.72 Under the laws in the UK, this would be a fairly straightforward case. The break clause clearly permits Mr K to end the agreement. He has acted within his rights. If, however, the contract is written under the CESL, ICO may have other lines of defence.
- 7.73 Under Article 5(1)(b) of the Brussels I Regulation, Mr K may be sued in the jurisdiction where the goods are to be delivered. Mr K receives papers from an Italian court in which ICO claim damages, citing five articles of the CESL.

Article 89: change in circumstances

- 7.74 The main claim is under Article 89. ICO allege that they only failed to achieve the sales target because of an exceptional change of circumstances: an earthquake in Naples, which reduced Italian consumer sales. ICO allege that Mr K failed to enter into negotiations in good faith to adapt the break clause in these exceptional circumstances. They are also asking the court to adapt the break clause under 89.2, to substitute a figure of 90 beds, which the parties would reasonably have agreed had they taken account of the earthquake.

Article 2: breach of good faith

- 7.75 ICO also claim that Mr K has not acted in accordance with good faith and fair dealing under Article 2 on the grounds that he has had secret discussions with a rival firm. This, they say, shows a lack of honesty, openness and consideration for their interests. They also allege that at one of the meetings he gave the rival firm confidential information about ICO's profit margins.
- 7.76 ICO say that under Article 2.2, Mr K should not be entitled to rely on his right to exercise the break clause. Furthermore, they claim damages for the loss this has caused them. Under Article 160, ICO claim for all the profits they allege they would have earned if the agreement had continued for five years.

Article 59: interpreting the term

- 7.77 ICO allege that the term specifying 100 sales is ambiguous. On a correct interpretation, it does not require that 100 sales must be achieved by an arbitrary deadline. Instead it should be interpreted as meaning that ICO would use its best endeavours to achieve around 100 sales.

7.78 ICO allege that during pre-contract negotiations, Mr K often said that he was not looking for quick sales but to develop a long term business. Furthermore, ICO quote members of Mr K's staff saying that after six months, they were satisfied with the level of sales. There is a page of statements which ICO allege were made by members of Mr K's firm over the course of the contracting relationship. They say that under Article 59 these statements are relevant to the interpretation of the term.

Article 23: failure to disclose

7.79 For good measure, ICO allege that Mr K failed to disclose information about the goods, as required under Article 23. They say that he entered into a similar agreement with a Spanish retailer, which was also terminated early when sales were less than expected. ICO allege that Mr K did not tell them about the poor Spanish sales, even though this information would have been very important to them. They say that the information concerned the saleability of the beds, which they claim is "a main characteristic" of the goods. They say that keeping quiet about his Spanish experience was not good commercial practice.

7.80 ICO claim damages under Article 29. Their claim is for the profits they would have made if the beds had been as popular as they reasonably understood them to be.

Article 55: failure to point out ICO's mistake

7.81 In the alternative, ICO claim that even if the problems in Spain were not a main characteristic of the product, Mr K still owes them damages under Article 55, when read in conjunction with Article 48. ICO allege that they made a mistake of fact in thinking that the beds had sold well in Spain. Mr K knew that they had made this mistake, but caused the contract to be concluded without pointing out that the Spanish sales were poor, even though good faith and fair dealing would have required this. This, they say, was contrary to the requirement in Article 48.1(b)(iii).

7.82 ICO claim that they have incurred losses in advertising and promoting the beds, which they demand from Mr K.

Mr K's reaction

7.83 Mr K takes legal advice. Ms J tells him that there are strong arguments to be put against the application of the CESL proposed by ICO. She writes back disputing the claim, making the following points:

- (1) Article 89.2 only applies where performance has become *excessively* onerous because of an *exceptional* change of circumstances (emphasis added). It is likely that the courts would interpret it restrictively. She points out that there have been at least five earthquakes in southern Italy over the last 100 years, and the events have not affected consumer confidence in Milan.
- (2) Article 2 must also be used cautiously. It would not be a breach of good faith to hold exploratory talks with another firm. The information about profit margins was not confidential, and even if it was, adapting the break clause is not the appropriate remedy.

- (3) Article 59 only applies to ambiguous terms, and here the break clause is quite clear.
 - (4) Article 23 is limited to the main characteristics of the goods, and does not include the events in Spain.
 - (5) Article 55 only applies if “good faith and fair dealing” would have required Mr K to point out the mistake. This is strongly denied.
- 7.84 Ms J thinks that Mr K has a strong case. On the other hand, she advises him that many of the words used in the CESL are general (a breach of duty “may” preclude a party from relying on a right; what the parties would “reasonably” have agreed). The provisions are untested as there is no case law.
- 7.85 She also says that the proceedings may be protracted and expensive. Mr K will need to pay for a lawyer experienced in Italian court procedure who also has a good understanding of the CESL. These are few and far between. The Italian court may refer the interpretation of some articles to the CJEU, involving further delay and expense. She suggests that Mr K might wish to pay for advice on the meaning of some articles not just in Polish and Italian but in a selection of other EU languages.
- 7.86 By now, Mr K wants nothing more to do with ICO, or the litigation. He takes out a bank loan to pay compensation to ICO, which proves to be a considerable burden to his business.

COMMENT

- 7.87 This example is hypothetical, and is not an argument against the provisions cited.
- 7.88 We think that Article 89.2 may go too far in allowing the court to re-write the contract. On the other hand, it only applies in exceptional circumstances⁴² and it may be excluded by the parties. The parties would need to put their mind to the issue, however. If one party simply lists it as a standard exclusion, without taking reasonable steps to bring it to the other party’s attention, the exclusion will be invalid under Article 70.
- 7.89 Article 2 on good faith cannot be excluded. On the other hand, it must be interpreted in the light of Recital 31, which limits its application. Most European systems have a duty of good faith, which is interpreted cautiously, suggesting that Article 2 will also be used cautiously. That said, the provision of damages under Article 2.2 goes beyond most European contract law systems. It will take time for judges, lawyers and litigants to understand the limits of the provision.

⁴² It may be designed to deal with cases similar to the inter-war hyper-inflation in Germany, the fall in the value of money noted in the *Staffordshire Area Health Authority v South Staffordshire Waterworks Co* [1978] 3 All ER 769 or the vast increase in energy prices in the US case of *Aluminium Co. of America (ALCOA) v Essex Group Inc.* 499 E Supp.53 (W.D. Pa. 1980).

- 7.90 Article 59 allows for a wider approach to interpreting the contract than would be allowed under UK law. As we saw, under the laws of the UK, pre-contractual negotiations may be relevant to establish the surrounding context of a contract, but may not be used to establish the parties' intentions.⁴³ On the other hand, there are strong arguments that the exclusion in UK law is artificial and may deprive the court of potentially relevant evidence.
- 7.91 Finally, we are concerned that a party may claim damages under Article 55 against a party for failing to point out a mistake. That goes further than English and Scottish law, and we do not know how far it would extend. Article 55 may be excluded by contract, but only well-informed parties would do so.
- 7.92 So should Mr K use the CESL? If we were asked to advise Mr K whether to use the CESL to govern the law of his contract, we would counsel caution. He should look carefully at the jurisdiction arrangements. If a dispute would end up in the Italian courts, would he find it difficult to sustain prolonged litigation in Italy? If so, the open-textured rules of the CESL might allow the other party to exploit their greater ability to litigate. If Mr K does find himself before the Italian courts, he may be better off using Italian law: the judges and lawyers will be more familiar with it; and as a more developed system it may provide greater certainty.
- 7.93 The CESL may develop into a helpful legal system in time, but we would not advise Mr K to be an early adopter of the new product.

CONCLUSION

- 7.94 For a legal system to succeed it needs to develop a critical mass. It needs to be sufficiently popular and important for lawyers and judges to study it. It needs to develop case law to guide its interpretation, and put flesh on the bare bones of the text.
- 7.95 There may be a market for the CESL, but we are unsure whether the market would be sufficiently large or significant for the CESL to develop the critical mass it needs. Those who would most benefit from it are the least likely to use it. Where a weaker party contracts with a stronger party, the choice of law is likely to be dictated by the stronger party.
- 7.96 There may be some interest from SMEs dealing with other SMEs, especially those who are reluctant to seek (and pay for) legal advice. But those who contract without legal advice are unlikely to give much thought to choice of law. And where they do, they will be naturally risk averse. They will be wary about using an untried legal system, unfamiliar to lawyers and judges alike.
- 7.97 We think this caution is a rational response in the circumstances. The CESL strives to protect the weaker party from being exploited during contractual negotiations. In doing so, however, it could enable a different form of exploitation, in the uncertainties and vagaries of the litigation process.

⁴³ *Chartbrook Ltd v Persimmon Homes Ltd*, [2009] UKHL 38; [2009] 1 AC 1101. The equivalent authority in Scots law is *Luminar Lava Ignite Ltd v Mama Group plc* 2010 SC 310 (Inner House).

- 7.98 We are aware that that there is support for the principle of the CESL from some small business associations. It is possible that trade associations drafting standard term contracts may use the CESL as the governing law for the contracts. It would offer a neutral choice, without being tied to any one member state, and disputes would eventually be resolved by the European Court of Justice. The draft CESL does not necessarily offer certainty, however. The European Commission will need to consult further about how far the draft CESL would be a helpful basis for trade association standard term contracts.
- 7.99 The CESL offers the parties a free choice – which we welcome. Even if we are right to be pessimistic, and the CESL is hardly ever used, no harm would be done. On the other hand, we are not convinced that developing a CESL for commercial parties should be seen as a priority for the European Commission's scarce resources. We think efforts would be better spent on developing a European code for consumer sales over the internet, where there is stronger evidence that the current variety of contract laws inhibits the single market.

PART 8

THE FORM OF THE INSTRUMENT AND ITS TREATY BASE

- 8.1 In this Part we give a brief description of the legislative form that the European Commission has proposed that the Common European Sales Law (CESL) should take (a regulation rather than a directive), and discuss the proposed treaty base. We identify the reasons in favour of a regulation, and one potential concern about the applicability of the proposed treaty base for business-to-business transactions.

THE FORM OF THE INSTRUMENT

- 8.2 Even after the publication of the Feasibility Study in May 2011 it was not clear what legal form the European Commission's proposed instrument would take, although this was a topic on which views were sought in the Commission's Green Paper.¹ Generally speaking, EU legislation in the field of consumer affairs (which is not exclusively the territory occupied by the CESL but which forms a significant part of its scope) has proceeded by way of directives. It is the responsibility of individual member states to implement these, within a specified time period.
- 8.3 Originally directives in this area took a "minimum harmonisation" approach. That is they specified minimum standards which member states were required to incorporate into their domestic laws. Member states were free to adopt higher standards unless otherwise prohibited by the directive. A recent academic study, published in February 2008, analysed the incorporation of eight consumer directives into national law and found "substantial differences between the various national implementing measures as a result of utilising minimum harmonisation clauses and regulatory options".²
- 8.4 In recent times the approach has changed to favour "full harmonisation" or standardisation. The Consumer Rights Directive (CRD), for instance, adopts this approach. It is based on a review of two earlier directives: those on doorstep selling (85/577/EEC) and distance selling (97/7/EC). Recital (2) to the CRD says:

"[...] That review has shown that it is appropriate to replace those two Directives by a single Directive. This Directive should therefore lay down standard rules for the common aspects of distance and off-premises contracts, moving away from the minimum harmonisation approach in the former Directives whilst allowing Member States to maintain or adopt national rules in relation to certain aspects."

¹ COM (2010) 348, 1.07.2010.

² Hans Schulte-Nölke, Christian Twigg-Flesner, Martin Ebers, Consumer Law Compendium: Comparative Analysis (February 2008), p 30. http://www.eu-consumer-law.org/consumerstudy_full_en.pdf.

8.5 For the CESL, by contrast, the European Commission has taken a different approach and proposes a regulation. The Explanatory Memorandum which was published along with the proposal contains a brief discussion of this decision.³ The main effects of choosing a regulation rather than a directive are that:

- (1) no national legislation is needed on the part of member states;
- (2) as a result, the law will be identical across the EU;⁴
- (3) the regulation will take simultaneous effect across the EU rather than – as is often the case with a directive – whenever member states pass implementing legislation;
- (4) it is immediately clear where the law is to be found (which is not necessarily the case where each member state implements a directive into domestic legislation); and
- (5) it is immediately available in all official EU languages.⁵

8.6 Each of these effects appears to be advantageous. In particular, given that the scope of the CESL is limited to cross-border transactions, the *simultaneous* entry into force of the sales law across the EU is highly desirable. Although simultaneous changes to the law across the Union can be achieved by means of a directive,⁶ there will nonetheless need to be a lengthy period during which national administrations and legislatures decide what changes to make and pass them.⁷

TREATY BASE

8.7 The legal basis for the proposed regulation is stated to be Article 114 of the Treaty on the Functioning of the European Union (TFEU). Several other treaty bases were speculated upon prior to its publication (notably Articles 81, 169 and 352 TFEU). Article 114 forms part of a Chapter dealing with the approximation of laws. Two aspects of the Article merit particular consideration.

³ 2011/0284 (COM), 11.10.2011 at p 10.

⁴ As with any regulation (or indeed other instrument) there is still the possibility of divergent meanings between its different language versions. It must also be remembered that areas not covered by the CESL will remain subject to the various national laws.

⁵ This would have gone some way to solving the problems experienced by the Scottish and Polish traders as discussed in para 6.31 above.

⁶ Eg, Art 28 of the CRD which requires member states implement the directive in such a way that the resulting legislation shall apply from, and regulate contracts concluded after, a date 30 months after the CRD's entry into force.

⁷ Given that Art 15 of the proposed regulation requires the Commission to present a review of its operation within 5 years of its taking effect, any delay would be highly undesirable.

Significance of Article 114 TFEU as a treaty base: qualified majority voting

- 8.8 Under Article 114 TFEU measures are passed by qualified majority voting by the Council. This contrasts with the requirement of unanimity of the member states under, for example, Article 352 TFEU. Therefore, although the UK Government will, of course, have the opportunity to argue for changes to the CESL as it progresses through the European Institutions, the UK's vote will not necessarily be decisive as the current weightings of each member state's votes in the Council mean that a qualified majority could be achieved without the support of the UK.

Significance of Article 114 TFEU as a treaty base: extension to business-to-business transactions?

- 8.9 In the recitals to the proposed regulation⁸ and accompanying explanatory memorandum⁹ the European Commission refers, in particular, to Article 114(3) TFEU. This states that the European Commission will take a high level of consumer protection when drafting legislation under Article 114, and the CESL contains a number of measures to protect consumers.
- 8.10 While Article 114(3) does not limit the application of Article 114 to proposals involving consumer protection, the explanatory memorandum to this instrument consistently focuses on the improvements that the CESL will make to consumer protection rules.
- 8.11 There is therefore a legitimate concern that Article 114 TFEU may not support the application of the CESL to a business-to-business context. However, the European Commission's case for extension to business-to-business transactions is itself partly framed in terms of providing further protection to consumers:

"In cross-border transactions between traders, negotiations about the applicable law could run more smoothly, as the contracting parties would have the opportunity to agree on the use of the Common European Sales Law – equally accessible to both of them – to govern their contractual relationship.

As a direct consequence, traders could save on the additional contract law related transaction costs and could operate in a less complex legal environment for cross-border trade on the basis of a single set of rules across the European Union. Thus, traders would be able to take better advantage of the internal market by expanding their trade across borders and, consequently, competition in the internal market would increase. Consumers would benefit from better access to offers from across the European Union at lower prices and would face fewer refusals of sales."¹⁰

⁸ Recital (11).

⁹ 2011/0284 (COM), 11.10.2011 at pp 8-9.

¹⁰ 2011/0284 (COM), 11.10.2011, Explanatory Memorandum, p 4.

Conclusion

- 8.12 The question of appropriate legal base was widely debated in the period leading up to publication of the European Commission's proposal. The choice of Article 114 TFEU will need to be kept under review as negotiations about the substance of the proposed regulation progress. The fact that the Commission has opted for a regulation rather than a directive is welcome.

APPENDIX

RECENT INITIATIVES TO IMPROVE CROSS-BORDER ENFORCEMENT

- A.1 Consumers have huge hurdles to face when it comes to obtaining redress and enforcing judgments in cross-border disputes. A few years ago Jonathan Hill expressed doubts over the enforcement regime.¹

The enforcement regime places almost insuperable financial obstacles in the way of consumers and it remains to be seen whether the recent developments in European civil procedure (including the European Small Claims Regulation) will do anything to reduce cross-border enforcement problems.

- A.2 Over the years the European Union has adopted a number of measures in order to improve the effectiveness of the enforcement regime. In this Appendix we look at three issues:

- (1) The European Small Claims Procedure.
- (2) Legal aid.
- (3) The recent proposals for amendment of the Brussels I Regulation.

THE EUROPEAN SMALL CLAIMS PROCEDURE

- A.3 The European Small Claims Procedure (ESCP) is designed to “simplify and speed up litigation concerning small claims in cross-border cases”.² The procedure came into operation in 2009 through Regulation No 861/2007 of 11 July 2007.
- A.4 The ESCP can be used if the value of a claim does not exceed €2000.³ However, it does not replace the small claims procedures already in force in the Member States: it is simply an alternative.⁴
- A.5 The procedure is primarily written, and oral hearings will be held only if necessary.⁵ Representation by a lawyer is not mandatory.⁶

¹ Jonathan Hill, *Cross-border consumer contracts*, Oxford University Press 2008 para 3.139. See also Hess Burkhard, Pfeiffer Thomas, Schlosser Peter, *Report on the Application of Regulation Brussels I in the Member States*, (2007) Study JLS/C4/2005/03 Ruprecht-Karls-Universität Heidelberg para 525.

² Regulation No 861/2007 of 11 July 2007, recital 8.

³ Above, art 2(1).

⁴ Above, art 1 and recital 8.

⁵ Above, art 5(1).

⁶ Above, art 10.

- A.6 The procedure takes place within national courts. Litigants must submit the relevant documents to the competent court in the language of the court or tribunal.⁷ As the ESCP Regulation does not contain jurisdictional rules, a claimant has to decide which court is competent on the basis of the Brussels I Regulation.
- A.7 No declaration of enforceability is required in order to have a judgment enforced in a member state different from the one in which it was given.⁸
- A.8 In the UK the ESCP is covered by Part 78 of the Civil Procedure Rules and Practice Direction 78, and the Act of Sederunt (Sheriff Court European Small Claims Procedure Rules) 2008.⁹ In England and Wales, the relevant court is the County Court, and in Scotland it is the Sheriff Court.

Assessment of the ESCP so far

- A.9 The most updated assessment of the ESCP so far is provided by a report by the European Parliament on Cross-Border Alternative Dispute Resolution in the EU.¹⁰ This report contains the following data as to the use of the ESCP:¹¹

The French Ministry of Justice indicated that there were 36 ESCP applications in 2010, whereas the interviewees in the UK pointed to 233 ESCP applications and 139 applications to enforce the ESCP decision in 2009-2010. The Dutch Ministry of Justice reported in an interview that there were only 10 or 20 cases in 2009 and 2010 (and only in six of the 19 district courts). The contact persons within the Commission indicated that ESCP has not been used often.

- A.10 These figures seem low. The 233 UK applications compares with 290,000 defended actions in the English and Welsh county courts in 2010, of which almost 80,000 were allocated to the small claims track. In Scotland, 41,450 cases were initiated in the domestic small claims procedure.
- A.11 The report observes that despite the theoretical advantages of the ESCP:
- one must acknowledge the small use of the ESCP by consumers for enforcing their rights in crossborder cases.¹²
- A.12 The reasons for this are as follows:¹³

⁷ Above, art 6.

⁸ Above, art 20.

⁹ See <http://www.justice.gov.uk/guidance/courts-and-tribunals/courts/procedure-rules/civil/contents/parts/part78.htm> and <http://www.scotcourts.gov.uk/library/civil/docs/European%20Small%20Claims%20Procedure%20Forms.pdf>.

¹⁰ European Parliament's Internal Market and Consumer Protection Committee, *Cross-Border Alternative Dispute Resolution in the EU* (June 2011). The report is available at <http://www.europarl.europa.eu/activities/committees/editoDisplay.do?language=EN&id=1&body=IMCO>.

¹¹ European Parliament's Internal Market and Consumer Protection Committee, *Cross-Border Alternative Dispute Resolution in the EU* (June 2011) p 55.

¹² Above, p 62.

- (1) The threshold of €2000 is too low.
- (2) Consumers may not be fully aware of the availability of the procedure.
- (3) Consumers may find it difficult to fill in the claim form, especially where the questions are open.
- (4) Consumers may have to fill in the claim form in a foreign language.
- (5) The ESCP Regulation does not harmonise national procedural law, so differences continue to exist, and consumers have to deal with them.

A.13 The fact that the ESCP is an alternative to national procedures was also criticised even before the Directive came into force:¹⁴

It is unreal to believe that a small claims litigant (who is often a litigant in person) is equipped to make such a choice. ... If there are two quite different procedures available for small cross-border claims, there will be plenty of scope for confusion and administrative error on the part of hard pressed court staff and judges.

LEGAL AID

A.14 Legal aid is available for the recognition and enforcement of judgments. Under article 50 of Brussels I, a person who seeks recognition and enforcement of a judgment is entitled to receive legal aid under the law of the member state addressed, if that person received complete or partial legal aid, or exemption from costs in the member state of origin.¹⁵

A.15 This article benefits the claimant for two reasons. First, it extends the benefit of legal aid to the country where recognition and enforcement is sought. Secondly, legal aid is automatically granted without further examination of the claimant's entitlement.¹⁶

A.16 In its review of legal aid, published in November 2010, the Government expressed its intention to retain funding for these cases.¹⁷

A.17 Legal aid is also provided for under Council Directive 2002/8/EC of 27 January 2003. This Directive established minimum common rules relating to legal aid for cross-border civil and commercial disputes.¹⁸

¹³ European Parliament's Internal Market and Consumer Protection Committee, *Cross-Border Alternative Dispute Resolution in the EU* (June 2011) pp 62-63.

¹⁴ House of Lords, European Union Committee, *European Small Claims Procedure*, 23rd Report of Session 2005 – 06, Report with Evidence, Dyson LJ para 74.

¹⁵ Regulation No 44/2001 of 22 December 2000 art 50.

¹⁶ Magnus Ulrich and Mankowski Peter (eds), *Brussels I Regulation*. European Commentaries on Private International Law (2007) Art 50, paras 2 and 3, p 684.

¹⁷ Ministry of Justice, *Proposals for the Reform of Legal Aid in England and Wales*, Consultation Paper CP12/10 (November 2010) paras 4.102 and 4.103.

¹⁸ Council Directive 2002/8/EC of 27 January 2003, art 1(2).

- A.18 The decision to grant or refuse legal aid rests with the competent authority of the member state where the court sits, or enforcement is sought.¹⁹ Legal aid granted in the member state in which the court sits covers the following costs.²⁰
- (1) interpretation;
 - (2) travel costs incurred by the legal aid applicant where the court requires the presence of the persons appearing in favour of the applicant.
- A.19 The member state in which the applicant is domiciled or habitually resident must provide legal aid covering.²¹
- (1) costs relating to the assistance of a local lawyer, until the legal aid application is received by the member state where the court sits;
 - (2) the translation of the application and of the necessary supporting documents when the application is submitted to the member state where the court sits.
- A.20 In its consultation paper on the reform of legal aid, the UK Government clarified that it does not intend to withdraw funding for cases falling under the Legal Aid Directive.²²

REFORM OF BRUSSELS I

- A.21 Problems with the enforcement regime have prompted the European Commission to put forward proposals for reviewing the Brussels I Regulation.²³ They include:
- (1) Abolition of the intermediate procedure for the recognition and enforcement of judgments with a few exceptions.²⁴
 - (2) Extension of the jurisdiction rules of the Regulation to disputes involving third country defendants.
 - (3) Enhancement of the effectiveness of choice of court agreements.
 - (4) Improvement of the interface between the Regulation and arbitration.
 - (5) Better coordination of proceedings before the courts of Member States.
 - (6) Improvement of access to justice for certain specific disputes.

¹⁹ Above, arts 9, 12 and 13. See also recitals 23 and 24.

²⁰ Above, art 7.

²¹ Above, art 8.

²² Ministry of Justice, Proposals for the Reform of Legal Aid in England and Wales, Consultation Paper CP12/10 (November 2010) para 4.141.

²³ Proposal for a regulation of the European Parliament and of the Council on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, Brussels, 17 December 2010, 2010/0383.

²⁴ The exceptions are defamation cases and judgments given in collective compensatory proceedings.

- (7) Clarification of the conditions under which provisional and protective measures can circulate in the EU.
- A.22 The proposals leave the jurisdiction provisions under articles 5(1)(b) and 15 to 17 unchanged.²⁵
- A.23 The Ministry of Justice held a consultation on the European Commission's proposals between December 2010 and February 2011.²⁶ However, the UK Government has not yet provided a final response to the consultation.

²⁵ Proposal for a regulation of the European Parliament and of the Council on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, Brussels, 17 December 2010, 2010/0383, pp 23, 27 and 28.

²⁶ Ministry of Justice, Revision of the Brussels I Regulation – How should the UK approach the negotiations, Consultation Paper CP18/10, 22 December 2010. The document is available at <http://www.justice.gov.uk/consultations/392.htm>.