The Evolution of Global Trade Over the Last Thirty Years

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UNIVERSIDAD NACIONAL AUTÓNOMA DE MÉXICO

THE EVOLUTION OF THE GLOBAL TRADE OVER THE LAST THIRTY YEARS

INSTITUTO DE INVESTIGACIONES JURÍDICAS
Serie, DOCTRINA JURÍDICA, Núm. 680.

Coordinadora editorial: Elvia Lucía Flores Ávalos
Asistente editorial: Karla Beatriz Templos Núñez
Edición y formación en computadora: Gilda Bautista Ravelo

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INTERNATIONAL ACADEMY OF COMMERCIAL AND CONSUMER LAW

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MÉXICO, 2014

Primera edición: 8 de noviembre de 2013
Primera reimpresión: 10 de abril de 2014

Ciudad Universitaria, 04510 México, D. F.

Instituto de Investigaciones Jurídicas

Circuito Maestro Mario de la Cueva s/n
Ciudad de la Investigación en Humanidades
Ciudad Universitaria, 04510 México, D. F.

Impreso y hecho en México – Printed in Mexico

ISBN 978-607-02-4898-6

CONTENT

CHAPTER I
THE EVOLUTION OF THE GLOBAL ECONOMIC SYSTEM OVER THE LAST THIRTY YEARS

CHAPTER II
THE EVOLUTION OF THE GLOBAL FINANCIAL SYSTEM OVER THE LAST THIRTY YEARS

CHAPTER III
THE EVOLUTION OF THE LEGAL FRAME WORK AROUND THE WORLD OVER THE LAST THIRTY YEARS: FINANCIAL SERVICES, THE HARMONIZATION OF LAWS AND REGULATIONS IN TIMES OF GLOBAL ECONOMIC CRISIS.

ORAL LECTURES

INTERNATIONAL ACADEMY OF COMMERCIAL AND CONSUMER LAW

16TH BIENNIAL CONFERENCE
UNIVERSIDAD NACIONAL AUTÓNOMA DE MÉXICO
JULIO, 2012

Estudio Preliminar

Esta Obra en su conjunto, aporta el análisis sobre Tres Grandes Líneas de investigación planteadas y autorizadas por la Junta Directiva durante los trabajos de la 14th Conferencia Bienal celebrada en la Universidad de Bamberg, Alemania en 2008. El objeto del tema central, "The Evolution of Global Trade Over the Last Thirty Years", fué analizar e intercambiar experiencias en esta 16th Conferencia de la International Academy of Commercial and Consumer Law, siendo anfitriona la Universidad Nacional Autónoma de México, en Julio de 2012.

A través de los diferentes estudios presentados, en lo particular, aportan experiencias y conclusiones jurídicas acerca de los acontecimientos que durante estas tres últimas décadas han incidido en la evolución del comercio internacional, en los diversos países donde se asientan las destacadas universidades en donde cada uno de los académicos, Miembros integrantes de la IACCL, desempeñan su actividad científica y profesional.

En cuanto hace a lo general, la suma de los fenómenos y experiencias jurídico-financiero-económicos, plasmados en esos estudios, desembocan en la actualización no sólo de usos y costumbres; sino además, con el ánimo de impulsar la actualización de las normas jurídicas hacia una total armonización del Derecho Comercial en todos sus campos, logrando de esta manera enfrentar los grandes retos mundiales que en materia mercantil se están presentando en este siglo XXI que es el parteaguas de una Nueva Era en la Evolución de nuestra civilización con la incorporación de las grandes tecnologías como herramienta de una Nueva Forma de Comerciar.

Sin perder de vista que el progreso tecnológico, significa la habilidad de producir los bienes y servicios con una menor cantidad de esfuerzo; en el

corto plazo destruye trabajos, pero a la larga produce crecimiento. Considerando además, que el progreso tecnológico incrementa la productividad y la riqueza social, pero altera la distribución de las recompensas. Sobre estas líneas de investigación se tiene que mantener el rigor científico de las investigaciones jurídicas para atenuar la transición a esta Nueva Era dentro de la actividad comercial.

Además no hay que olvidar que, la suma de las ganancias de los que salen beneficiados es mayor, que la suma de las pérdidas de los que salen perjudicados. Lo cual se ha venido reflejando en que hay oficios o actividades en extinción que nos hace reflexionar sobre la Teoría de *Charles Robert Darwin* (1809-1882), que está presente cuando pensamos por i.e. archivistas, operadores telefónicos, asistentes administrativos, torneros, empacadores.

La Tecnología está alterando el hogar, la calle y el espacio del trabajo. La inteligencia artificial está avanzando agigantadamente; sin embargo, no hay certidumbre de sus resultados, por lo tanto el intercambio del comercio internacional, es una actividad que debe ir de la mano con la revolución industrial y tecnológica; sin olvidar que, la historia de la humanidad no se puede concebir sin la historia del comercio, ya que ambas, a la vez también van de la mano. Por lo tanto, el hombre es el protagonista de la actividad comercial para satisfacer sus necesidades.

De esta manera a través de los 30 años de existencia de esta Academia, la suma de las instituciones jurídicas que se han ido analizando, han contribuido o propiciado la actualización de la normatividad que ha ido surgiendo para regular, facilitar y apoyar el crecimiento económico, el flujo de los sistemas financieros, y la armonización entre derecho doméstico e internacional; el cual también ha ido evolucionando exitosamente al ritmo del impulso del comercio nacional, regional e internacional.

El análisis y debate de los temas presentados, tienen gran relevancia especialmente en estos tiempos de cambios comerciales, económicos y financieros. Como expertos en esta área del Derecho, se ha logrado integrar una gran red de científicos en la materia mercantil o Comercial a nivel mundial. Sus contribuciones que giran siempre en torno de los problemas que aquejan actualmente el intercambio y la actividad comercial, propician a que nuestros diversos países puedan mejorar o perfeccionar tanto el orden jurídico —económico como el orden financiero— comercial ambos integran los binomios base de los sistemas actuales y además de que son Eje Fundamental que impactan tanto a cada País, como a los Organismos Internacionales en este mundo globalizado; aportando nuevas líneas de investigación dentro de la materia Mercantil.

La IACCL a partir de 1983, fecha en que se constituyó aquí en México en el seno de la Universidad Nacional Autónoma de México, ha venido reuniéndose en Conferencias Bianuales en otras Universidades que también han sido Anfitrionas:

University of Innsbruck (1984); Harvard Law School(1986); University of Melbourne (1988); Oxford University (1990); University of Stockholm (1992); Saint Louis University Missouri (1994); Bar Ilan University (1996); Bond University (1998); Pennsylvania State University, The Dickinson School of Law (2000); Max-Planck Institute for Comparative and International Private Law (2002); Riga Graduate School of Law(RGSL) (2004); University of Texas School of Law (2006); University of Bamberg (2008); University of Toronto Law Schooland Osgoode Law School (2010); National Autonomous University of México (1983 y 2012).

Las Conferencias citadas arriba fueron organizadas por: Arcelia Quintana y Acosta Romero (1983); Heinrick Mayrhofer y Donald King (1984); Hal Scout y Boris Kozolchyk (1986); David Allan , Mary Hiscock y David Harlan (1988);Ross Cranston y Roy Goode (1990);Jan Ramberg y Jan Helner (1992); Ulf Bernitz y Donald King (1994); Shalom Lerner, Jacob Ziegel y Arie Reich (1996); David Alan y Mary Hiscock (1998); Louis Del Duca (2000); Jüergen Basedow y Ulrich Drobnig (2002); Norbert Reich (2004); Jay Westbrook y Ross Cranston (2006); Jürgen Basedow y Hans Micklitz (2008); Anthony Duggan, Stephanie Ben-Ishai, Ben Geud y Jacob Ziegel (2010); Arcelia Quintana y Hans Miklitz (2012).

A las Conferencias anteriores podemos sumar, que ya se encuentra en proceso la 17th Biennial Conference , que se celebrará en el año 2014, en Istanbul, Turkey por la Professor Yesmin Atamer organizadora, Anthony Duggan como Presidente y Professor Arcelia Quintana como President Elect. La Conferencia 18th que se celebrará en la Universidad de Kyushu, Japón, organizada por el Professor Toshiyuki Kono y presidida por la Professor Arcelia Quintana.

Este Binomio de Presidente Electo y Presidente, es la figura académica que le ha dado fortaleza y continuidad a la IACCL. Toda vez, que las experiencias se van acumulando y se enriquecen sin interrupción alguna estimulando y fomentando los temas y nuevos fenómenos jurídicos que se han venido presentando en esta nueva era de la llamada inteligencia artificial y cibernética, estrechamente ligada a la teoría de control y teoría de sistemas, que han avasallado la nueva actividad derivada del comercio en todos los enfoques de la Ciencia del Derecho Mercantil Comercial, ahora globalizado.

A C T A

EN UNA REUNION CELEBRADA EL 15 DE JUNIO DE 1983 BAJO LOS AUSPICIOS DEL DIRECTOR DE LA FACULTAD DE DERECHO MIGUEL ACOSTA ROMERO DE LA UNIVERSIDAD NACIONAL AUTONOMA DE - - MEXICO Y EN LA CUAL INTERVINIERON LOS PROFESORES MIGUEL ACOSTA ROMERO, ARCELIA QUINTANA ADRIANO, DONAL B. KING, BORIS KOZOLCHYK Y HAL SCOTT, CONSTITUIDOS EN COMITE EJECUTIVO AD-HOC DE LA ACADEMIA INTERNACIONAL DE DERECHO COMERCIAL Y DEL CONSUMIDOR, ACORDARON SOMETER A LA APROBACION DE LOS MIEMBROS PARTICIPANTES EN LA PRIMERA REUNION DE LA ACADEMIA LOS SIGUIENTES PUNTOS:

1) LA ELECCION DE UNA JUNTA DIRECTIVA COMPUESTA POR LOS SIGUIENTES DIRECTIVOS:

PRESIDENTE	DONALD B. KING.
SECRETARIO EJECUTIVO	MIGUEL ACOSTA ROMERO.
COORDINADORA EJECUTIVA	ARCELIA QUINTANA ADRIANO.
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	ROY GOODE.
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	DAVID HARLAN.
	RAUL A. ETCHEVERRY.
	ARCELIA QUINTANA ADRIANO
	MIGUEL ACOSTA ROMERO

2) LA DESIGNACION DEL PROF. HAL SCOTT COMO PROXIMO PRESIDENTE COMISIONADO PARA LA ELECCION DE DIRECTIVOS EN EL - AÑO DE 1985.

3) LA ADOPCION DEL PRINCIPIO DE NO RE-ELECCION PARA EL - MISMO CARGO DE DIRECTIVO EN MAS DE DOS ELECCIONES CONSECUTIVAS.

4.- LA DESIGNACION DE LA FACULTAD DE DERECHO DE LA UNIVERSIDAD NACIONAL AUTONOMA DE MEXICO COMO ENTIDAD RESPONSABLE PARA LA PUBLICACION DE LOS ARTICULOS SOMETIDOS A LA - 1a. SESION EN UN NUMERO ESPECIAL DE LA REVISTA DE LA - - UNIVERSIDAD NACIONAL AUTONOMA DE MEXICO, Y TAMBIEN LA IMPRESION DE UN LOGO IDENTIFICATIVO DE LA ACADEMIA Y DE PAPEL PARA COMUNICACIONES OFICIALES DE LA ACADEMIA.

5) LA DESIGNACION DE LA FACULTAD DE DERECHO DE LA UNIVERSIDAD DE ARIZONA COMO UN CENTRO PARA EL DEPOSITO DE MATERIALES PARA LA ACTUALIZACION DE LOS TEMAS DE INTERES A LA ACADEMIA CON RESPONSABILIDAD RESPECTO AL HESMIFERIO OCCIDENTAL CENTRO AL CUAL LE DEBERAN SER ENVIADOS POR TODOS - LOS MIEMBROS DE LA ACADEMIA TODOS LOS MATERIALES QUE CADA MIEMBRO CONSIDERE UTILES E INFORMATIVOS Y CENTRO AL QUE - TENDRAN ACCESO LOS MIEMBROS DE LA ACADEMIA EN SUS PROYECTOS DE INVESTIGACION.

DONALD B. KING.
PRESIDENTE

MIGUEL ACOSTA ROMERO.
SECRETARIO EJECUTIVO

ARCELIA QUINTANA ADRIANO
COORDINADORA EJECUTIVA

A manera de precedente y como homenaje a los trabajos de la International Academy of Commercial and Consumer Law, a continuación transcribo el documento histórico de 1983:

Concluyo este Estudio Preliminar con un amplio reconocimiento a la Universidad Nacional Autónoma de México que a lo largo de más de 100 años, ha fungido como baluarte de enseñanza e investigación Académica con gran liderazgo en Iberoamérica. Siguiendo esta tradición la UNAM, a través de su Rector José Narro Robles, no dudó en apoyar a la Academia en su labor Científica, en ocasión de la 16th Conferencia Bienal celebrada en Julio de 2012, considerando que estas Conferencias Bianuales han permitido integrar a través de los cinco Continentes una gran red de cooperación académica entre los expertos de Derecho Mercantil, recogiendo la UNAM las ideas y los resultados logrados en esta obra.

Elvia Arcelia Quintana-Adriano
President Elect of the International Academy of Commercial and Consumer Law

INTERNATIONAL ACADEMY OF COMMERCIAL AND CONSUMER LAW

16TH BIENNIAL CONFERENCE

NATIONAL AUTONOMOUS UNIVERSITY OF MEXICO

JULY, 2012

Preliminary Study

This work, as a whole, provides the analysis of three major lines of research raised and authorized by the Executive Board of the 14th Biennial Conference held at the University of Bamberg, Germany in 2008. The purpose of the central theme, "The Evolution of Global Trade Over the Last Thirty Years," was to analyze and exchange experiences during the 16th Conference of the International Academy of Commercial and Consumer Law (IACCL), hosted by the National Autonomous University of Mexico (UNAM) in July 2012.

The different studies presented at the conference provided experiences and legal conclusions regarding the events that, during the last three decades, have influenced the evolution of international trade in the various countries where the academics who are members of the IACCL conduct their professional and scientific activities. The sum of the legal, financial, and economic phenomena and experiences embodied in these studies, result not only in updating customs or practices, but in facing the global challenges that in commercial matters are presently occurring in this twenty-first century, which marks the watershed of a new era of our civilization, when great technologies are being incorporated as tools in the new form of Trading.

Without losing sight of the fact that technological progress means the ability to produce goods and services with less effort, in the short-term it may destroy jobs but creates growth in the long-term. Moreover, technological progress increases productivity and social wealth, although alters the distribution of income. On these lines of research, one must maintain the scientific rigor of legal research to mitigate the consequences of the transition to this new age of commercial activity.

One must not forget that the sum of the benefits outweigh the sum of the losses of those who are harmed. Indeed, there are occupations or activities that are slowly becoming extinct, which brings to mind the theory of

Charles Robert Darwin (1809-1882), especially when we think of archivists, telephone operators, administrative assistants, lathe operators, and packers. Technology is altering the home, the streets, and the workspace, and artificial intelligence is advancing tremendously. However, there is no certainly as to its results. As such, international trade is an activity that must go hand in hand with the industrial and technological revolution, without forgetting that the history of humanity cannot be conceived without the history of trade, since also go hand in hand. Therefore, man, as a human being, is the protagonist of commercial activities to meet his needs.

As such, throughout the 30 years of this Academy's existence, legal institutions have contributed or led to the updating of the legal framework that has emerged to regulate, facilitate, and support economic growth, the flow of financial systems, and the harmonization of domestic and international law. These legal institutions have successfully evolved to the rhythm of national, regional, and international commerce.

The analysis and discussion of the issues presented during this conference are of great relevance, especially in these times of commercial, economic, and financial changes. The academics who presented their research findings at the most recent IACCL conference specialize in commercial, or mercantile, law. Through the Academy, they have established a worldwide network of experts in this field of law and their contributions to the field relate to the problems currently affecting trade and commercial activities. Their research is conducive and allows our countries to improve the economic, legal, financial and commercial framework, which are the basis of the current system and a fundamental axis that impacts countries and international organizations in this globalized world, contributing new lines of research within the field of commercial law.

Since 1983, when the IACCL was established in Mexico at the National Autonomous University of Mexico, the Academy has regularly held biennial conferences that other universities have hosted. These include the University of Innsbruck (1984), Harvard Law School (1986), the University of Melbourne (1988), Oxford University (1990), the University of Stockholm (1992), Saint Louis University (1994), Bar-Ilan University (1996), Bond University (1998), the Dickinson School of Law at Pennsylvania State University (2000), the Max-Planck Institute for Comparative and International Private Law (2002), the Riga Graduate School of Law (RGSL) (2004), the University of Texas at Austin (2006), the University of Bamberg (2008), the University of Toronto Faculty of Law (2010), and the National Autonomous University of Mexico (1983 and 2012).

The above mentioned conferences were, respectively, organized by the following members of the Academy: Arcelia Quintana and Miguel Acosta

Romero (1983); Henrick Mayrhofer and Donald King (1984); Boris Kozolchyk Scout Hal (1986); David Allan, Mary Hiscock, and David Harlan (1988); Ross Cranston Roy Goode (1990); Jan Helner and Jan Ramberg (1992); Ulf Bernitz and Donald King (1994); Shalom Lerner, Jacob Ziegel, and Arie Reich (1996); David Alan and Mary Hiscock (1998); Louis Del Duca (2000); Ulrich Drobnig and Jürgen Basedow (2002); Norbert Reich (2004); Jay Westbrook and Ross Cranston (2006); Hans Micklitz and Jürgen Basedow (2008), Anthony Duggan, Stephanie Ben-Ishai, Ben Geud, and Jacob Ziegel (2010); and Hans Miklitz and Arcelia Quintana (2012).

We can now add to this list of prior conferences, now that preparations for the 17th Biennial Conference are already underway. It is to be held in 2014 in Istanbul, Turkey and will be organized by Professor Atamer Yesmin, Professor Anthony Duggan in his capacity as President, and Professor Arcelia Quintana as President-Elect. The 18th Conference is to be held at the University of Kyushu in Japan and will be organized by Professor Toshiyuki Kono and chaired by Professor Arcelia Quintana.

Pairing the President-Elect and President together during the same term has given strength and continuity to the IACCL. Their experiences accumulate and become enriched without interruption, sometimes stimulating and promoting the new issues and legal phenomena that have been presenting themselves in this new era of so-called artificial intelligence and cybernetics, which is closely related to control theory and systems theory, and that has overwhelmed the new trading activity resulting from all approaches to the now-globalized science of commercial law.

By way of precedent and as a tribute to the work of the International Academy of Commercial and Consumer Law, I include the following 1983 document:

I conclude this preliminary study by recognizing that the National Autonomous University of Mexico, over the course of over a hundred years, has served as a bastion of learning and academic research and shown great leadership in Latin America. In keeping with this tradition of excellence, the UNAM, through Rector José Narro Robles, did not hesitate to support the Academy in its efforts during the 16th Biennial Conference held in July 2012. The UNAM was honored to do so in light of how these biennial conferences have enabled the creation of a network of academic cooperation among experts in commercial law throughout five continents.

Elvia Arcelia Quintana-Adriano
President-Elect
International Academy of Commercial
and Consumer Law

CHAPTER I

THE EVOLUTION OF THE GLOBAL ECONOMIC SYSTEM

OVER THE LAST THIRTY YEARS

EVOLUCIÓN DEL DERECHO COMERCIAL, DEL SISTEMA FINANCIERO Y DEL SISTEMA ECONÓMICO GLOBAL. ANÁLISIS DE TRES DÉCADAS

SUMARIO: *I. Introducción. II. Instituciones económico-jurídico–comerciales*. III. *Integración del comercio*. IV. *Estructuras político-comerciales a nivel mundial*. V. *Evolución del sistema financiero*.VI. *Armonización del derecho*. VII. *Era digital*. *Comercial*. VIII. *A manera de conclusión*.

Elvia Arcelia QUINTANA ADRIANO

I. INTRODUCCIÓN

1. *Propósito de este artículo*

Se han intensificado tres grandes tendencias relacionadas con el sujeto del derecho comercial a través de las pasadas tres décadas. La primera se enfoca en el comercio, específicamente el comercio entre naciones, y no solo las vecinas. La segunda tiene que ver con las finanzas, domésticas, regionales e internacionales que ha apoyado al cumplimiento de las metas no solamente de empresas de carácter mercantil, sino también a Naciones. La tercera tendencia que se ha llevado acabo es, quizá, la más importante o por lo menos la más transcendente: la armonización del derecho en materia comercial. Al armonizar leyes, reglamentos, y políticas domésticas con las internacionales se permite el desarrollo económico de países y el bienestar social de los pueblos.

Por eso son de importancia relevante los estudios jurídicos en torno al sujeto de comercio, al objeto del mismo y a las relaciones que derivan de la actividad comercial no sólo nacional, sino también internacional. Al identificar como se pueden mejorar y armonizar las normas jurídicas en torno a cada uno de estos temas ha permitido y facilitado el intercambio comercial al hablar en un mismo lenguaje jurídico mercantil plasmado en las leyes que los regula, lo cual no suele ser un proceso fácil, ni lo ha sido con la veloci-

dad que se ha requerido; sin embargo, se han podido crear una variedad de leyes y organismos que han facilitado el desarrollo económico en particular y mundial.

Es importante destacar y aceptar que: El derecho Mercantil o Comercial se encuentra en una variedad muy amplia de fuentes, incluyendo los Acuerdos y Tratados internacionales, Leyes nacionales, y reglamentos. Este aspecto es el que nos da un punto de referencia para apreciar y valorar el esfuerzo de los países, de los organismos nacionales, regionales, mundiales, comisiones y grupos de trabajo que se han ocupado para lograr armonizar las normas jurídicas mercantiles o comerciales, entre los diferentes Estados, tomando en cuenta el nivel mundial regional y nacional.

Claro el hecho de que el comercio internacional se ha expandido impresionantemente y que las instituciones internacionales política-económicas; comerciales-financieras y jurídicas se hayan incrementado en su importancia geopolítica, son éxitos notables también. Esa es la razón por la cual este artículo busca analizar el desarrollo de estas tres tendencias a través de los años y como se han concretado gracias a la efectividad de las normas jurídicas que las mantienen como ejes fijas de nuestro mundo.

La actividad comercial de los pueblos desde la antigüedad, se ha caracterizado por intercambiar bienes y servicios lo que ha implicado, además, movilizarlos. A su vez, estos tres grandes aspectos: bienes; servicios y movilización o intercambio, originaron los usos y costumbres que desembocaron en normas que fueron recogidas en los diversos Estatutos y Ordenanzas *i.e.* el Código de Hamurabi, las Reglas de Wisby, las Ordenanzas de Burgos, Sevilla y Bilbao, los *Rooles* de Olerón, los *Ordinamenta et Consuetudo Maris,* los *Capitula et Ordenamenta et Curiae maritimae nobilis civitatis Amalfae* o Tablas Amalfitanas; entre otras, que originariamente rigieron la actividad de los comerciantes. Posteriormente se transformó en la normatividad comercial que envolvió y rigió a las personas físicas o morales comerciantes, a los objetos materia y sustancia del comercio; a las relaciones que derivan de esa movilización de riqueza que; a su vez, se ha venido reflejando en infinidad de contratos atípicos, en las actividades realizadas en operaciones financieras, bancarias, bursátiles, de seguros y fianzas y en títulos-valor en un mundo globalizado.

Toda aquella normatividad primaria que surge de la fuerza de los usos y costumbres de los comerciantes, pasa a ser el contenido de los Estatutos y Ordenanzas plasmándose posteriormente en diversas leyes que tratan de regular la actividad comercial al ritmo del impulso del comercio que se ve reflejada en infinidad de contratos atípicos. Actualmente la evolución de las nuevas tecnologías, sobre todo en el campo de la informática, se han aprovechado,

en apoyo a esta gran evolución de las operaciones de los inmensos mercados que abastecen y proporcionan la satisfacción global de las necesidades de los consumidores.

A medida que la tecnología perfeccionó los medios de comunicación, el comercio se fue ampliando, evolucionando desde el primitivo comercio de los pueblos de la antigüedad al desarrollado comercio contemporáneo. Esta evolución significó una ampliación de la actividad en dos aspectos: en cuanto al volumen de los intercambios y a la extensión de la zona geográfica de influencia de dichos intercambios.

Es el momento en que podemos hablar de que el comercio sobrepasó las fronteras nacionales apareciendo como una necesidad natural, el comercio internacional. Actualmente se puede afirmar que "en materia de comercio no hay fronteras".

A su vez, jurídicamente hablando ha surgido la necesidad metodológica de agrupar el inmenso cúmulo de normas y leyes domésticas, regionales y mundiales para lo cual se llega a establecer la metodología de integrar, tres grandes universos de estudio que a su vez propiciaron la existencia de un cuarto universo. Estos *universos* son: 1. *El que incluye el estudio relativo a las personas comerciantes*, sean *físicas* o sean *empresas*; 2. El que se refiere *a la determinación de los objetos del comercio* sean *bienes* o *servicios*; 3. El que *estudia* a los *hechos y negocios jurídicos derivados de las relaciones comerciales* que surgen de la *interacción de los dos primeros universos* de estudio y finalmente en el intercambio jurídico de los tres primeros universos para desembocar en el *cuarto universo*, relativo a los *procedimientos* que pueden ser *jurisdiccionales* o *administrativos* como son: la amigable composición, la mediación y el arbitraje comercial que puede presentarse en los tres niveles: doméstico, el regional y el mundial.

El conjunto de estos universos es la materia de estudio de la Ciencia del Derecho Mercantil o Comercial, base de una buena armonización de normas jurídico- económico- social y político que envueltas éstas, en la creatividad de los juristas, debe propiciar jurídicamente hablando el desarrollo jurídico, social y político del comercio, para alcanzar el objeto último del derecho que es el bienestar de los miembros de la sociedad.

Lo planteado hasta aquí permite establecer que el Derecho mercantil o Comercial al ser profundamente social y dinámico, se aplica a las relaciones comerciales, sean éstas empresas o personas físicas, a las cuales el mismo derecho siempre tomará en cuenta debido a que son indudablemente necesarias para el mantenimiento del orden Jurídico Comercial que necesariamente debe ser armonizado. Así el Derecho Comercial, sin dejar de observar las relaciones humanas de carácter jurídico-económico que se dan entre

los comerciantes y siendo éstas producto de la práctica consuetudinaria de la actividad comercial, las toma en cuenta para reglamentarlas de manera armoniosa, lo cual ha dado origen al movimiento unificador del Derecho Comercial a través de Leyes Modelo o Acuerdos o Tratados internacionales que ha venido desarrollando la Organización de las Naciones Unidas a través de la UNCITRAL o CNUDMI en un esfuerzo por facilitar los intercambios comerciales a nivel global.

La reflexión anterior encauzó la idea de investigar cuál ha sido la evolución que han tenido las Instituciones comerciales, en el ámbito de los tres primeros Universos referidos arriba; además, del cuarto universo que implica la solución de problemas o conflictos económico-comerciales-financieros sean nacionales, regionales o internacionales durante las tres últimas décadas, coincidentes con el origen y evolución de la International Academy of Commercial and Consumer Law, que fue constituida en julio 15 de 1983 siendo sede la Universidad Nacional Autónoma de México.

Así, este artículo busca analizar tres grandes tendencias que a lo largo de los treinta últimos años se han constituido como ejes del desarrollo económico, comercial, y armonización del derecho.

II. Instituciones económico - jurídico - comerciales

En torno a la materia económica, han girado fundamentalmente diversas teorías como: la Teoría de la Ley de la Oferta y la Demanda; la Teoría del valor; la conceptualización acerca de la Espontaneidad de las Instituciones Económicas y el Comercio Internacional de Adam Smith; la Teoría General de la ocupación, el interés y el dinero de Keynes, así como las Teorías de Shumpeter acerca del Desenvolvimiento Económico en lo relativo a la economía dinámica, siendo todas en cierta medida, aún vigentes.

Económicamente hablando, las Teorías en esta materia se han visto enmarcadas en estudios científicos que han tenido el terreno propicio, tanto en el mundo en donde se producen los bienes y servicios, como en el mundo donde se consumen; o sea los grandes mercados de consumidores. Que son la Institución Social-comercial o arreglo institucional de la sociedad, mediante la cual se establecen mecanismos para que los compradores y los vendedores de un bien o servicio entren en contacto para intercambiarlos.

En el desarrollo del análisis de este punto, se debe tener presente que el acto de comercio tiene un carácter económico por lo que resulta insuficiente iniciar un estudio jurídico de la actividad comercial, sin considerar que el comercio es simultáneamente un fenómeno, tanto jurídico como económico.

La actividad comercial a través del tiempo y fundamentalmente en las últimas décadas ha ido gestando no sólo los instrumentos jurídicos-económicos-comerciales y políticos que han sido necesarios para el desarrollo de la actividad, sino además, las instituciones regionales y mundiales indispensables para coordinar y regular la producción y distribución de los bienes y servicios indispensables para los consumidores, base de la tranquilidad y protección de las respectivas sociedades de cada país.

El siglo XX se caracterizó por los pasos acelerados y trascendentes con que han evolucionado distintos renglones del conocimiento humano, lo cual dio apertura al derecho comercial que es una ciencia autónoma que consta de los elementos necesarios para considerarla principal en el conocimiento jurídico mercantil; por eso, como en toda rama del saber humano, está supeditada a los grandes inventos y descubrimientos del hombre en el transcurso de la historia y a servirse de ellos. Así, podemos destacar y observar, que hacia finales de aquel mismo siglo, las nuevas modalidades de contratación mercantil responden a la evolución tecnológica, al servicio de una economía de mercado, en donde uno de sus términos es la empresa jurídica, y a la creciente demanda de bienes y servicios, debido a las profundas transformaciones económicas, sociales y políticas que se han venido dando en el mundo.

En la actualidad, factores como la globalización, una mayor interdependencia entre los países, los avances de la tecnología y de las comunicaciones, han logrado que el mercado comercial mantenga un constante desarrollo en su campo de acción, traspasando fronteras nacionales; por tanto se reitera que el concepto clásico de derecho comercial se encuentra en plena evolución, esta es la razón por la cual se reitera que "*en materia comercial no hay fronteras*".

El proceso de globalización comenzó en la década de los sesenta, continuó progresando en la década de los setenta y llegó a su madurez en los ochenta. Esta actividad se inició con la función de los bancos comerciales mediante una globalización de las transacciones efectivas en los mercados de cambio y de depósito; posteriormente, se agregaron de una manera importante los mercados de activos y préstamos de los bancos internacionales. Los Estados al encontrarse inmersos en una manera de comerciar en donde el derecho de la materia se encuentra en constante evolución; propiciando la progresiva caída de las barreras y fronteras comerciales, limitando cada vez más la posibilidad de aislarse de un mercado global donde los factores primarios e intercambio: dinero, bienes y servicios, tecnología e incluso personas; transitan con mayor facilidad entre las distintas naciones, se enfrentan a las nuevas reglas comerciales que no pueden, ni deben, ser exclusivas para cada nación.

III. Integración del comercio

El proceso de integración comercial implica además, el de la integración económica-política-social y jurídica que ha evolucionado determinantemente durante éstas tres últimas décadas, entrelazando todos los aspectos de cada campo, generando una interdependencia entre países o sectores económicos mundiales, regionales o subregionales, producto de la fusión de mercados, de la armonización del derecho nacional formalizado en instituciones creadas para coordinar políticas e instrumentos de desarrollo que brindan la posibilidad de mejorar el nivel de vida de sus miembros (párrafo 2427, libro *El comercio Exterior de México. Marco Jurídico Estructura y Política*).

En dicho proceso se desarrollan varias fases de la integración que se han exteriorizado en tres grandes aspectos como lo son: *Zona de Libre Comercio*: ALADI, TLCAN, AFTA, ASEAN, APEC; Unión Aduanera: UE (Unión Europea), MERCOSUR (Mercado Común del Sur), CARICOM (Comunidad del Caribe), CAN (Comunidad Andina), GCC (Consejo de Cooperación para los Estados Árabes del Golfo), EAC (Comunidad Africana Oriental), CMAC Comunidad Económica y Monetaria de África Central, WAEMU Comunidad Económica de los Estados de África Central. *Mercado Común* esta etapa de la integración no tan solo implica una Unión Aduanera, sino que representa una mayor voluntad política por parte de los países integrantes de la región en la liberalización de todos los factores productivos, es decir, es un nuevo universo de mercancías originarias que circulan libremente dentro de un espacio aduanero. *Unión Económica*, con su máximo exponente que es la Unión Europea supone un grado más en la armonización de las políticas fiscales y monetarias. En esta etapa se produce una mayor cesión de soberanía, pues se dota de un sistema monetario único; cada país se somete a una disciplina monetaria para mantener los tipos de cambio dentro de los márgenes autorizados.

Finalmente es necesario precisar que la integración comercial impone la necesidad de desarrollar los mecanismos internacionales necesarios para regular las relaciones comerciales y resolver los problemas que puedan surgir dentro de éste nuevo orden de tráfico mundial, tomando en cuenta no sólo las fronteras , al menos en lo relativo al comercio, están desapareciendo formando un solo mundo comercial, sino también que disciplinas como el derecho, la economía y la política deben tener una visión global, capaz de regular las relaciones entre Estados-nacionales que surgen en el marco de la globalización.

Actualmente se puede hablar de un sistema tripartito de organizaciones financiera-económico-comerciales internacionales: el Fondo Monetario

Internacional que pretende asegurar el orden y la estabilidad de las transacciones financieras internacionales; el Banco Mundial que pretende en términos generales promover la inversión y la Organización Mundial del Comercio que pretende:

— Elevar los niveles de vida, a lograr el pleno empleo y un volumen considerable, en constante aumento de los ingresos reales y demanda efectiva.
— Acrecentar la producción y el comercio de bienes y servicios, permitiendo al mismo tiempo la utilización óptima de los recursos mundiales de conformidad con el objetivo de un desarrollo sostenible, procurando proteger y preservar el medio ambiente, incrementando los medios para hacerlo, de manera compatible con sus respectivas necesidades e intereses, según los diferentes niveles de desarrollo económico.
— Que los países en desarrollo, y especialmente los menos adelantados, obtengan una parte del incremento del comercio internacional que corresponda a las necesidades de su desarrollo económico.
— Preservar los principios fundamentales y favorecer la consecución de los objetivos que forman el sistema Multilateral del Comercio.

En mi opinión la integración comercial - económica debe entenderse como un proceso constante que entrelaza los aspectos de carácter jurídico, económico, social y político generando una interdependencia entre países o sectores económicos regionales producto de la fusión de mercados, de la armonización del derecho nacional formalizado en las instituciones creadas y los instrumentos jurídicos.

IV. Estructuras política-comerciales a nivel mundial: Organización Mundial del Comercio (OMC-Fondo Monetario Internacional-Banco Mundial)

En este ámbito se debe considerar a la Organización Mundial del Comercio que con sus 159 miembros al 2 de marzo de 2013, impulsan al comercio dentro de un marco jurídico que pretende ser armonioso y equitativo, "*con el objetivo primordial de impedir que los países adopten medidas unilaterales, en contra de otro miembro, buscando elevar los niveles de vida, acrecentar la producción y el comercio de bienes y servicios que los países menos adelantados obtengan una parte del incremento del comercio internacional y preservar los principios*

fundamentales y favorecer la consecución de los objetivos anteriores que integran el sistema multilateral del comercio".

Hay que resaltar que la Organización Mundial del Comercio nace para garantizar el derecho de las relaciones comerciales entre sus miembros, y para gestionar, así como vigilar el cumplimiento de las nuevas obligaciones asumidas por todos ellos. Los Acuerdos más importantes administrados por la OMC se dividen de acuerdo con el Consejo que los administra, y se enlistan de la siguiente manera:

a) *Consejo de Mercancías* (*GATT*). A través de este Acuerdo se consideran como objeto basado en principios fundamentales: las relaciones económicas multilaterales tendentes a lograr altos niveles de vida, pleno empleo, crecimiento de la producción y de intercambio de productos. Plena y racional utilización de los recursos mundiales. Celebración de acuerdos encaminados a obtener a base de reciprocidad y ventajas mutuas, la reducción de aranceles y demás barreras comerciales.

b) *Consejo de Servicios (AGCS)*. Este Acuerdo abarca todos los servicios que son objeto del comercio internacional con dos excepciones: los servicios suministrados al público en el ejercicio de las facultades gubernamentales y, en el sector del transporte aéreo, los derechos del tráfico y todos los servicios relacionados con el ejercicio de los derechos del tráfico; Este Acuerdo surgió en respuesta al enorme crecimiento de la economía de servicios durante los últimos treinta años y al incremento del comercio de servicios propiciado por la revolución de las comunicaciones.

c) *Consejo de los Aspectos de Derechos de la Propiedad Intelectual* (*CADPIC*). El Acuerdo sobre Derechos de Propiedad Intelectual (*TRIPS*), contempla la protección de los derechos de autor, marcas de fábrica o comerciales, los dibujos, modelos y partes industriales, los esquemas de trazados de circuiros integrados, las denominaciones de origen y los secretos comerciales.

Naciones Unidas
(CNUDMI, ECOSOC,UNCTAD)

Naciones Unidas

Principales Objetivos: Mantener la Paz; Fomentar las relaciones de amistad entre las naciones; Ayudar a trabajar para mejorar la vida de los pobres, vencer el hambre, las enfermedades y el analfabetismo, fomentar el respeto

de los derechos y libertades de los demás; *Servir de Centro que armonice los esfuerzos de las naciones para alcanzar estos objetivos comunes*.

UNCITRAL

A través de esta Comisión Naciones Unidas en el ámbito del derecho mercantil internacional y de este movimiento armonizador de la regulación comercial busca acelerar el crecimiento, mejora el nivel de vida, crea nuevas oportunidades en los países tomando como base los principios generales y especiales de esta comisión.[1]

Consejo Económico y Social (ECOSOC)

Otro de los organismos que colabora en materia económica en las Naciones Unidas en el Consejo Económico y Social (*ECOSOC*), el cual tiene una amplia responsabilidad respecto del 70% aproximadamente de los recursos humanos y especializados, 9 comisiones orgánicas y cinco comisiones regionales y que dentro de sus últimos foros han considerado varios temas dentro de los cuales el más relevante es que para 2015, es necesario que todos los agentes de la cooperación internacional para el desarrollo unan sus fuerzas para mejorar la calidad y los resultados de la cooperación para el desarrollo con miras al logro de los Objetivos de Desarrollo del Milenio.[2]

Conferencia de las Naciones Unidas sobre Comercio y Desarrollo (UNCTAD)

Siendo órgano principal de la Asamblea General en la esfera del comercio y el desarrollo. La UNCTAD coordina el tratamiento integrado del desarrollo y otras cuestiones afines en los sectores de comercio, finanzas tecnología, inversión y desarrollo sostenible.

La creación de la UNCTAD pretende lograr cambio en las relaciones entre el mundo desarrollado y los países de la periferia; a pesar de que no se ha traducido todavía resultados importantes dentro de los países pobres.

Asimismo no han faltado pugnas y fricciones entre los distintos grupos de países miembros. Sin embargo , el buen sentido y las fórmulas de conciliación han permitido no solamente que la organización sobreviva a las críticas que se le dirigieron, sino que , hoy en día, la UNCTAD es uno de

[1] Fuente: *http://www.uncitral.org/uncitral/es/about_us.html*.

[2] Fuente: *http://www.un.org/es/ecosoc/newfunct/2012dcf.shtml*.

los órganos más vigorosos y con mayor futuro de todos los que integran las Naciones Unidas. Las actitudes de la mayoría de los países desarrollados son más positivas.

Los organismos comerciales financieros, BIRF, FMI y GATT, establecidos en el periodo posbélico, están haciendo serios intentos tendientes a adecuar mejor sus políticas y prácticas a las necesidades de los países menos desarrollados.

V. Evolución del sistema financiero

Ante la internacionalización de los servicios financieros se ha pretendido favorecer la implantación de sistemas en la materia financiera más estables y eficaces por cuanto alude a la introducción de normas y prácticas internacionales, donde destaca la calidad, eficiencia y alcance de estos servicios, facilitando fuentes más sostenibles de fondos a partir de la eliminación del trato discriminatorio que existe entre los proveedores extranjeros y los nacionales; así como, en la supresión de obstáculos al suministro transfronterizo que revisten esta clase de servicios, permitiendo con tales acciones abrir las puertas para la entrada de proveedores extranjeros en el mercado doméstico.

Bajo el anterior orden de ideas, es posible sostener que el aumento de la competitividad promovida por la apertura de sector financiero estimula el crecimiento económico de cualquier país, pues la cantidad de proveedores extranjeros en el mercado, es la que tiene un efecto positivo en el funcionamiento de los mercados bancarios nacionales.

El Acuerdo General sobre Comercio de Servicios (AGCS), se considera uno de los acuerdos más importantes que entró en vigor en enero de 1995. Es el único instrumento de normas multilaterales que regula el comercio internacional de servicios. Representa el primero y único conjunto de normas multilaterales por el que se rige el comercio internacional de servicios dentro de la OMC.

Dentro del AGCS que es una parte importante del movimiento internacional de capital, se adopta la figura de la inversión extranjera que implica el flujo internacional de capital en los que una empresa de un país crea o amplia una filial en otro país, en la que su nota distintiva es, no solamente la transmisión de recursos, sino también la adquisición del control en la toma de decisiones.

El acceso a los servicios mundiales, contribuye, a que tanto a los exportadores como productores de los países en desarrollo aprovechen su capacidad productiva, independientemente de los bienes y servicios que estén

ofreciendo en el mercado. Por ello, la liberalización de los servicios se ha convertido en un elemento clave de un sinnúmero de estrategias de desarrollo.

En el marco de referencia, los países en los que sus mercados de servicios se encuentran liberalizados han presentado mayor dinamismo en la circulación de los productos y sus respectivos procesos, contribuyendo a estimular la inversión directa extranjera.

Con la regulación del sector de los servicios a nivel mundial, expresamente en el AGCS, se ha pretendido obtener un rápido crecimiento de la economía internacional, aportando el mayor porcentaje del producto mundial. Genera en muchos países un alto número de empleos, toda vez que las ventajas potenciales que provoca la liberalización de los servicios son tan amplias como en el sector de las mercancías.

La importancia de contar con un acuerdo en materia de servicios, como el AGCS, radica en que éstos desempeñan un papel preponderante en la economía internacional, ya que contribuyen a fomentar la productividad basada en la informática y en los múltiples conocimientos que con ellos se generan.

Es inminente que en los albores del siglo XXI, junto con el desarrollo del fenómeno de la globalización y ayudados por los novedosos medios electrónicos, los mercados internacionales están realizando innumerables transacciones comerciales y financieras, lo cual vuelve necesaria su vigilancia y regulación. Las normas encaminadas a satisfacer esta función deben ser claras, sencillas y no deben haber lagunas, que puedan crear confusiones en su aplicación.

Además dichos autores deben tener motivos sólo así ofrecerá confianza en la integridad del mercado, en las transacciones que allí se realizan y en la solución de controversias lográndose un comercio mundial con mecanismos jurídicos que proporcionen seguridad y confianza para realizar cualquier tipo de actividad mercantil, a través de cualquier medio electrónico y sin importar qué tan cerca o lejos se encuentren de su interlocutor comercial.

Para los estudiosos del Derecho Comercial ó Mercantil, se presenta en este siglo un paradigma que le obligará a replantear analizar y evaluar las instituciones mercantiles que hasta ahora se dan por válidas, para determinar si seguirán siendo prácticas y útiles en el futuro inmediato; es decir si son capaces de regular, tanto a los actos de comercio; a las personas que lo realizan, a las cosas o bienes materia de dichos actos de comercio; y a los procedimientos judiciales o administrativos.

El Derecho Comercial es precursor de estos nuevos retos jurídicos permitirá que sus instituciones conserven el carácter evolutivo de transformación y superación de conceptos, acorde con las nuevas ideas, con los avances

tecnológicos, con los nuevos medios de comunicación, con los nuevos estilos de contratación masiva para esos mercados de consumo.

En la alborada de un nuevo milenio, donde la soberanía nacional se ha visto disminuida por la globalización de las empresas, de las instituciones internacionales financieras y políticas; así como por las normas multilaterales en materia económica-comercial, la teoría del Estado vive un proceso de renovación y transformación que lleva a reflexionar y abrir paso a la transición del Estado moderno hacia el Estado contemporáneo.

El proceso de globalización, no sólo jurídica-económica-financiera, sino también tecnológica ha planteado, además, cambios radicales en cuanto a la producción y la organización empresarial, así como la definición de nuevas estrategias para fortalecer la incorporación y el desarrollo de empresas multinacionales en los mercados nacionales.

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VI. Armonización del derecho

El comercio y las relaciones mercantiles, desde sus orígenes hasta el actual siglo XXI, han evolucionado de la simple reunión de comerciantes y el tránsito de mercancías en un espacio geográfico delimitado, a la creación de empresas regionales, multinacionales y mundiales dando origen a principios rectores de libre comercio, procesos de integración regionales y mundiales, acuerdos de libre comercio y la globalización del mercado en un intercambio global.

Lo anterior ha provocado la necesidad de establecer un derecho comercial con aplicación internacional que armonice las diferentes normas mercantiles de los distintos sistemas jurídicos nacionales.

En la actualidad, las fuertes tendencias de *integración de mercados* como resultado de la mecánica globalizadora, los acuerdos comerciales y las prácticas comerciales internacionales, demandan una solución a los conflictos desde una perspectiva supranacional que *se ve materializada en tratados o convenios internacionales* para dar una solución a la problemática. Organizaciones como la *Comisión de las Naciones Unidas para el Derecho Mercantil Internacional* (CNUDMI- UNCITRAL), *promueve* la confección de un derecho *armonizado*, que diluye los conceptos de jerarquía normativa establecidos por la doctrina

tradicional en aras de evitar que las controversias que se susciten en el tráfico comercial queden sin solución; procurando la implementación de reglas específicas de aplicación.

En la armonización del derecho comercial como ha quedado planteado han sido muy importantes los organismos políticos como Naciones Unidas, con su movimiento unificador a través de Leyes Modelo o de Acuerdos y Tratados Internacionales en materia de Derecho Comercial, han sido muy provechosos para quienes los han adoptado o propiciado un lenguaje jurídico armonizado. Sobre todo en materia de Servicios Financieros; contratos mercantiles; comercio electrónico; compra venta internacional de mercaderías; transporte marítimo; seguros; propiedad intelectual; derechos de autor; garantías mobiliarias, arbitraje comercial, insolvencia transfronteriza, entre otros.

La armonización del Derecho Comercial a nivel internacional debe darse no sólo en los aspectos relativos a la contratación, sino también en el ámbito de la *solución de controversias comerciales*.

Lo importante de este movimiento es que ha permitido a los diversos países analizar el contenido de las propuestas, incorporando a su derecho nacional, conjugando las diferentes idiosincrasias y fenómenos internos de cada país, permitiéndoles adoptar o adecuar a su Legislación interna sin violentar su derecho.

Como ejemplo de lo anterior se menciona a continuación la Leyes Modelo de la CNUDMI: Ley Modelo de Arbitraje Comercial 1985; Ley Modelo sobre el Intercambio Electrónico de Datos elaborada por la Comisión de las Naciones Unidas para el Derecho Comercial Internacional y la implementación de las Tecnologías de la Información y de la Comunicación Comercio Electrónico 1996; Ley Modelo sobre la Insolvencia Transfronteriza 1997; Ley Modelo sobre las Firmas Electrónicas 2001 y la Ley Modelo sobre Conciliación Comercial Internacional 2002.

VII. Era digital comercial

A través del rápido desarrollo de los sistemas informáticos y de comunicación, se han agilizado las actividades comerciales, logrando acortar las distancias y los plazos de orden y entrega entre los participantes de la actividad comercial, lo que ha permitido una mayor eficacia para competir a nivel mundial, generando beneficios a la economía mundial.

El desarrollo de la tecnología y la innegable mundialización del comercio y los servicios financieros ha generado que las opciones de inversión se

hayan incrementado de forma significativa en los últimos años del siglo XX, debido también al cada vez más frecuente uso a nivel internacional del mercado de valores como mecanismo de financiamiento en comparación con el sistema bancario.

Uno de los grandes acontecimientos para el Derecho Comercial, en las postrimerías del siglo XX, fue el Comercio Electrónico, el cual vino a revolucionar el concepto formal con que se venían haciendo los negocios y a formar una nueva percepción de los actos jurídicos sin dejar por ello de considerar los conceptos antiguos de oferta y policitación previstos en el Código de Comercio.

Por otra parte tratándose de los *servicios financieros* partiendo de la idea que ayudan de manera muy importante al desarrollo de los negocios, y de esa manera al crecimiento económico de un país; por ello, es necesario que se encuentren al alcance de la población interesada en su uso, como son las pequeñas empresas. En la actualidad, se han creado instrumentos financieros que facilitan a los individuos celebrar contratos y llevar a cabo transacciones comerciales relacionadas con los servicios financieros, bancos, mercado de valores. Se trata de negociaciones que por el uso de la tecnología pueden hacerse en fracciones de minutos, particularmente cuando se hacen a través de Internet, ya que conectan al prestador del servicio directamente con el usuario final, quien solamente requiere de una *computadora ó dispositivos móviles* para que en minutos lleve a cabo dichas transacciones.

En este sentido, ha sido un verdadero desafío mundial, la integración de estándares nacionales e internacionales en las áreas económicas y jurídicas que permitan la plena identificación del individuo contratante, pero que además protejan, no sólo la veracidad de los contratos, inversiones o pagos que se realizan vía internet, sino también los datos personales que en muchas ocasiones son requeridos para realizar ciertas actividades comerciales a través de dichos medios electrónicos; incluso los derechos de propiedad intelectual se han visto vulnerados ante los avances tecnológicos.

Por otra parte en materia de comercio internacional cabe destacar, otros esfuerzos ya de orden mundial que coadyuvan a la aproximación cultural constituyendo las bases de datos que contienen pronunciamientos judiciales y arbitrales de distintos puntos recónditos del orbe. Para coadyuvar en la interpretación uniforme de sus textos, UNCITRAL ha establecido un sistema de reporte de fallos basados en aquello, bajo la denominación abreviada con las siglas CLOUT (Sistema para recopilar y difundir información sobre decisiones judiciales y laudos arbitrales relativos a las convenciones y leyes modelo elaboradas por la CNUDMI), la cual puede ser accedida en versión impresa o a través de Internet. Algo parecido ocurre con UNIDROIT y la

base de datos conocida como UNILEX. Merecen también mención aquí otras bases de datos con valiosa información, como la de la Universidad de Pace en los Estados Unidos, relativa a la Convención de Viena, conteniendo un sinnúmero de fallos judiciales, laudos arbitrales, doctrina y otros documentos relativos a las misma y la de la Universidad de Colonia, en Alemania, a través de su Center for Transnational Law (CENTRAL) y su método de "*creeping codification*" del nuevo derecho mercantil transnacional. A dicho efecto, se elaboró una lista abierta de principios sobre la *lex mercatoria,* que se mantiene fácilmente accesible a través de Internet, con lo que se logra una constante actualización, confiriendo flexibilidad a esta forma de codificación y evitando estancamientos en el desarrollo de la misma. Cada principio y cada regla traen consigo las referencias de sus fuentes, cuyo texto completo se vuelve así asequible.

Finalmente es importante considerar que los avances tecnológicos como elementos en una cultura globalizada, han impactado de manera trascendente en el campo del derecho los cuales hacen necesaria una constante adecuación de las instituciones jurídicas a la nueva era digital.

VIII. A manera de Conclusión

En resumen, la globalización y los avances tecnológicos obligan a regular nuevos aspectos en las relaciones comerciales, la insolvencia transfronteriza, la contratación internacional, el comercio electrónico, las empresas transnacionales, las transferencias electrónicas la solución de controversias internacionales son sólo algunas de las nuevas materias; sumándose a las ya reguladas.

Debemos decir que: es importante continuar revisando, ajustando y actualizando la base jurídica, institucional, multilateral e internacional del comercio, con el objeto de fortalecer la estructura de la Organización Mundial del Comercio en beneficio del intercambio comercial de mercancías, de servicios y de la propiedad intelectual, no sólo para facilitar dichos intercambios, sino además, para la armonización de la legislación interna de los Estados nacionales en estos aspectos.

THE EVOLUTION OF THE GLOBAL TRADE OVER THE LAST THIRTY YEARS

SUMMARY: I. *Introduction*. II. *Economic-Legal-Commercial Institutions*. III. *Trade Integration*. IV. *Political-Commercial Structures at the Global Level*. V. *Evolution of the Financial System*. VI. *Harmonization of Law*. VII. *Commerce in the Digital Age*. VIII. *Conclusion*.

Elvia Arcelia QUINTANA -ADRIANO

I. INTRODUCTION

There are three major trends related to commercial law that have intensified over the course of the last three decades. The first pertains to trade, specifically trade among nations, and not only those bordering each other. The second trend has to do with domestic, regional, and international finance, which has supported the goals of commercial enterprises, as well as countries. The third trend that has taken place during this time is, perhaps, the most important or at least is the most transcendental: the harmonization of commercial law. By harmonizing domestic laws, regulations, and policies with international ones, one can promote the economic development and social wellbeing of countries. For these reasons, legal research regarding commercial activities is of such importance, as are relationships derived from domestic and international commercial activities.

Identifying how to improve and harmonize the legal norms regarding each one of these three trends has facilitated commercial exchanges by allowing people to speak the same 'language' that is contained in the laws that regulate us. This has not tended to be an easy process, nor has it taken place with the required speed. Despite this, a variety of laws and organizations have been created, which has facilitated economic development on a global and individual level.

It is worth noting and acknowledging that commercial, or mercantile, law is found in a wide variety of sources. These include international agreements and treaties, national statutes, and regulations. This aspect gives us a point of reference for appreciating and valuing the efforts made by working groups, commissions, countries, and national, regional, and international organizations that worked to harmonize commercial legal norms among different states while taking into account the international, regional, and national levels.

Of course, the fact that international commerce has grown impressively and that international institutions have increased their geopolitical importance are also notable successes. That is the reason why this article seeks to analyze the development of these three trends throughout the years and how they have solidified themselves thanks to the effectiveness of the legal rules that maintain them as fixed axes in our world.

Since ancient times, the commercial activity of peoples has been characterized by the interchange of goods and services, which has also involved transporting them. At the same time, these three main aspects (goods, services, and transportation or exchanges) gave rise to the practices that led to rules that were integrated into various statutes and regulations. These included the Code of Hammurabi, the Laws of Wisby; the Laws of Burgos, Seville, and Bilbao; the 'Rooles' of Olerón; the Ordinamenta et Consuetudo Maris or Ordinances and Custom of the Sea; the Capitula et Ordenamenta et Curiae maritimae nobilis civitatis Amalfae or Amalfian Laws; among others, which originally regulated the activities of merchants. Subsequently, they became the commercial norms that applied to and regulated businesses and businesspersons, the objects of trade, and the relationships that stemmed from the mobilization of wealth that, in turn, has become reflected in an infinite variety of atypical contracts used in the multiple financial, security, insurance, bond, and certificate of title transactions in a globalized world.

All those regulations that stem from the force of the customs and activities of merchants, then became the contents of statutes and ordinances, and subsequently formed the basis of various laws that seek to regulate commercial activities to the rhythm of commerce reflected in an infinite variety of contracts. Nowadays, the evolution of new technologies, especially in the field of computer science, has been taken advantage of in order to support this great evolution in the operations of the immense markets that satisfy the global needs of consumers.

As technology perfected means of communication, commerce continued expanding, evolving from the primitive trade between ancient communities into the commerce of today. This evolution has meant an expansion

of activity in two ways: the volume of trade and the extent of the geographic area of influence of this trade. This is the moment in which we can say that trade has surpassed national borders such that international commerce has become an inherent necessity. Today we can affirm that "in matters of commerce, there are no borders".

At the same time, legally speaking, there has arisen a methodological need to categorize the immense collection of domestic, regional, and global laws and regulations so that one can establish the methodology to integrate three major fields of study that, in turn, indicate the existence of a fourth field. These fields are 1) the one that includes the comparative study of persons or organizations involved in commerce, 2) the one that refers to the determination of objects of commerce, either goods or services, 3) the one that studies the legal activities and exchanges derived from the commercial relations that arise from the interaction of the first two fields of study, and finally 4) the legal exchange of the first three fields, which gives rise to the fourth field. This last field pertains to the procedures that can be jurisdictional or administrative, such as cordial agreements, mediation, and commercial arbitration, and that can present themselves at three levels: domestic, regional, and global.

The combination of these four fields is the science of commercial law, which forms the foundation of a positive harmonization of legal, economic, social, and political norms that, thanks to the creativity of jurists who become involved in the process of harmonization, promote the legal, social, and political development of commerce in order to reach the ultimate objective of law: the wellbeing of the members of society.

The principles that have been put forward allow one to establish that commercial law, which is deeply dynamic and social, applies to commercial relations, be they among natural persons or companies, which will always be taken into account by the law since they are undoubtedly necessary to maintain that legal-commercial order that must be harmonized. In this way, commercial law, while continuing to observe human relationships of a legal-economic character that exist among merchants and which are a result of the routine practices of commercial activities, takes these relationships into account in order to regulate them in a harmonious manner. This gives rise to the unifying trend in commercial law via model laws and international agreements or treaties that the UN (United Nations) has developed through UNCITRAL (United Nations Commission on International Trade Law) in an effort to facilitate commercial transactions at a global level.

The preceding considerations put forward the idea of researching the evolution of commercial institutions in the area of the first three fields men-

tioned above, in addition to the fourth field that involves solving economic, commercial, and financial problems or conflicts, be they national, regional, or international, during the last three decades. This era has coincided with the birth and evolution of the International Academy of Commercial and Consumer Law, which was founded on July 15, 1983 in the National Autonomous University of Mexico.

As such, this article seeks to analyze the three major trends that, over the course of the last 30 years, have become axes of economic and commercial development, and harmonization of law.

II. Economic-Legal-Commercial Institutions

Regarding commercial matters, there have been fundamentally different theories such as the theory of the law of supply and demand, the theory of value, the conceptualization of the spontaneity of the economic institutions and international commerce of Adam Smith, the general theory of employment, interest, and money of John Maynard Keynes, as well as Schumpeter's theories regarding economic development relative to a dynamic economy. All of these theories, to an extent, remain valid.

Economically speaking, the theories in this field have seen themselves framed in scientific studies that have favorable ground, both in the world of producing goods and services as well as in the world of their consumption. That is, in the large consumer markets that are the socio-commercial institution, or institutional arrangement of society, through which mechanisms for buyers and sellers of a good or service are established and allow themselves to come into contact to interchange them. In developing this analysis, it must be kept in mind that the act of commerce has an economic character, which is why it is insufficient to begin a legal analysis of commercial activity without considering how commerce is both a legal and economic phenomenon.

Commercial activity throughout time, and especially in the last few decades, has created not only legal, economic, commercial, and political instruments that have been necessary for the development of this activity, but also regional and global institutions that are indispensable for coordinating and regulating the production and distribution of goods and services that, in turn, are indispensable for consumers and are the foundation for the peace and protection of societies in each country.

The twentieth century was characterized by accelerated and transcendental steps that evolved distinct paths of human knowledge, which gave rise to commercial law, which consists of the elements necessary to consider it

foremost in legal commercial knowledge. For this reason, like in all branches of human knowledge, commercial law is subject to the great inventions and discoveries of man in the course of history. In this way, we can highlight and observe how, toward the end of that century, new forms of commercial contracts respond to the technological evolution at the service of a market economy. One of its goals is the incorporated business and the growing demand for goods and services due to the profound social, political, and economic transformations around the world.

Nowadays, factors such as globalization, greater interdependence among nations, and advances in technology and communications have been able to keep commercial markets in a constant stage of development in its field of action, going beyond the limits of national borders. As such, the classic conceptualization of commercial law is in a constant state of evolution. This is why "in matters of commerce, there are no borders".

The process of globalization began in the sixties, it continued during the seventies, and came of age in the eighties. This activity began with the role of commercial banks via a globalization of the actual transactions in foreign exchange and deposit markets. Subsequently, asset markets and international bank lending were added in a major way. Various countries find themselves immersed in a form of commerce in which the law is in a constant state of evolution, encouraging the progressive decline of trade barriers and borders, and increasingly limiting the possibility of isolating a global market where the primary factors and exchange (money, goods and services, technology, and even people) pass between different nations more easily. Those countries are facing new trade rules that cannot, and should not, be unique to each nation. This activity began with the role of commercial banks by a globalization of transactions in foreign exchange markets and deposit markets, after which asset markets and international bank lending were added in a major way.

III. Trade Integration

The process of trade integration also involves the economic, socio-political, and legal integration that has evolved determinately during these last three decades, linking together all the aspects of each field and creating an interdependence among countries or global economic sectors, regional or subregional, a product of the fusion of markets and the harmonization of national law formalized in institutions created to coordinate development policies and instruments that offer the possibility of improving their members' living conditions.

In that process, various stages of integration are carried out, which have been externalized in three major aspects. First are free trade zones, such as the following: LAIA (Latin American Integration Association), NAFTA (North American Free Trade Agreement), ASEAN (Association of Southeast Asian Nations), APEC (Asia-Pacific Economic Cooperation) Forum, European Union (EU), MERCOSUR (Southern Common Market), CARICOM (Caribbean Community), CAN (Andean Community), GCC (Cooperation Council for the Arab States of the Gulf), EAC (East African Community), CEMAC (Economic and Monetary Community of Central Africa), and WAEMU (West African Economic and Monetary Union).

Second are common markets. This stage of integration involves not just a customs union, but also represents a greater political will on the part of the member states of the region in favor of liberalization of all factors of production. That is, it involves a new universe of goods that circulate freely within a customs union. Third is an economic union, of which its greatest example is the European Union, and which involves a greater degree of harmonization of fiscal and monetary policies. In this stage, there is a greater surrender of sovereignty as there is a single monetary system. Each country submits itself to a monetary discipline in order to maintain exchange rates within the authorized margins.

Finally, it is necessary to state that trade integration imposes the need to develop international mechanisms needed to regulate trade relationships and to resolve the problems that may arise in this new world order of global traffic. This requires taking into account not only borders since, at least as they pertain to trade, they are disappearing and forming a single commercial world, but also disciplines such as law, economics, and politics that must have a global vision capable of regulating the relations between nation-states that arise in the context of globalization.

Currently, one can speak of a tripartite system of financial, economic, and commercial organizations. The International Monetary Fund (IMF) seeks to ensure the order and stability of international financial transactions, the World Bank seeks to promote investment, and the World Trade Organization (WTO) aims to accomplish the following objectives:

— Raise standards of living by ensuring full employment and constantly raise real income and effective demand.
— Increase the production and trade of goods and services, while also allowing for the optimal use of global resources in accordance with the objective of sustainable development, seeking to both protect and preserve the environment, increasing the means of doing so,

consistent with their respective needs and interests, and based on different levels of economic development.
— Ensure that developing countries, especially the least developed ones, obtain a share of the increase in international trade commensurate with the needs of their economic development.
— Preserve the fundamental principles and support the achievement of the objectives that form the multilateral trading system.

In this author's opinion, commercial and economic integration should be understood as a constant process that intertwines legal, economic, social, and political aspects, generating an interdependence among countries or regional economic sectors. This integration is a product of the merger of markets and the harmonization of national law, formalized in institutions and legal instruments.

IV. Political-commercial structures at the global level: world trade organization (WTO), international monetary fund (IMF), world bank

One must consider how the World Trade Organization, with its 159 members as of March 2, 2013, boosts trade within a legal framework that purports to be both harmonious and equitable "with the primary objective of preventing countries from adopting unilateral actions against another member, seeking to raise living standards, expanding the production and trade of goods and services so that the least developed countries obtain a share of the increased international trade, and preserve the basic principles and promote the achievement of the previous objectives that make up the multilateral trading system".

It should be noted that the World Trade Organization was created to guarantee the right of trade relations among its members and to manage, as well as monitor compliance with, the new obligations assumed by member states. The most important agreements administered by the WTO are divided according to the council that administers them, and are listed as follows:

a) Council for Trade in Goods (GATT). The object of GATT includes fundamental principles such as establishing multilateral economic relations aimed at achieving high living standards, full employment, growth in the production and exchange of products, full and rational use of global re-

sources, and the creation of agreements meant to obtain, based on reciprocity and mutual benefit, the reduction of tariffs and other trade barriers.

b) Council of Services (GATS). The GATS (General Agreement on Trade in Services) covers all services that are traded internationally with two exceptions, services provided to the public through the exercise of governmental functions and, in the area of aerial transportation, traffic rights and all services related to the exercise of those traffic rights. This agreement arose in response to the enormous growth of the services sector over the last thirty years and the increase in exchange of services promoted by the communications revolution.

c) Council for Trade-Related Aspects of Intellectual Property Rights. The Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS) envisions the protection of copyrights, trademarks, designs, models and industrial parts, layout designs of closed circuits, designations of origin, and trade secrets.

UNITED NATIONS (UNCITRAL, ECOSOC, UNCTAD)

United Nations

The main objective of this international organization is to preserve peace, promote friendly relations among nations, help improve the lives of the poor, conquer hunger, disease, and illiteracy, promote respect for the rights and freedoms of others, and serve as a center for harmonizing the nations' efforts to achieve these common goals.

UNCITRAL *(United Nations Commission on International Trade Law)*

Through this United Nations commission in the subject of international trade law, the trend toward harmonizing trade regulations seeks to accelerate growth, improve living standards, and create new opportunities in countries based on the general and special principles of this committee.[1]

ECOSOC *(Economic and Social Council)*

Another agency that works on economic matters in the United Nations is the Economic and Social Council (ECOSOC), which has broad

[1] Source: *http://www.uncitral.org/uncitral/es/about_us.html.*

responsibilities regarding approximately 70% of human resources and specialized resources, and has nine functional commissions and five regional commissions. These commissions' latest forums have considered several issues, among which the most important is that by 2015 it is necessary for all agents of international cooperation for development to join forces in order to improve the quality and results of development cooperation with a view toward achieving the Millennium Development Goals.[2]

UNCTAD (United Nations Conference on Trade and Development)

As the principal organ of the General Assembly in the field of trade and development, UNCTAD coordinates the integrated treatment of development and related issues in the areas of trade, finance, technology, investment, and sustainable development.

The creation of UNCTAD aims to achieve a change in relations between developed countries and periphery countries, even though this has not yet translated into important results within poor countries.

At the same time, there has not been a lack of conflict and friction among different groups of member states. However, common sense and dispute resolution formulas have allowed the organization to not only survive the criticism directed toward it, but also become one of the most vigorous and promising organs of all those that make up the United Nations.

The attitudes of most developed countries are more positive. The financial trade institutions, IBRD (International Bank for Reconstruction and Development), IMF, and GATT, which were established in the postwar period, are making serious efforts aimed at tailoring their policies and practices to the needs of the least developed countries.

V. Evolution of the financial system

Given the internationalization of financial services, there have been efforts to promote the implementation of systems in financial matters that are more stable and efficient as they introduce international standards and practices that emphasize the quality, efficiency, and scope of these services, providing more sustainable sources of funding, beginning with the elimination of discriminatory treatment that exists between foreign and domestic suppliers as well as the removal of barriers to cross-border supply of services of this type, permitting such actions to open doors for the entrance of foreign suppliers in a domestic market. Under the preceding order of ideas,

[2] Source: *http://www.un.org/es/ecosoc/newfunct/2012dcf.shtml.*

it can be argued that the increased competition caused by the opening of the financial sector stimulates the economic growth of any country, since the number of foreign suppliers in the market has a positive effect on the functioning of national banking markets.

The General Agreement on Trade in Services (GATS) is considered one of the most important agreements that entered into force in January 1995. It is the only instrument of multilateral rules that govern the international trade of services. It represents the first and only set of multilateral rules governing the international trade in services within the WTO. Within the GATS, which is an important part of the international movement of capital, there is a great importance placed on foreign investment that involves the international flow of capital in which the capital of one a company from one country creates or enlarges a subsidiary in another country, in which its distinctive note is not only the transfer of resources but also the acquisition of control in decision-making.

Access to global services helps, such that both exporters and producers in developing countries can exploit their productive capacities regardless of the goods and services that they are offering in the market. As such, the liberalization of services has become a key element of a number of development strategies. Given this framework, countries that have liberalized their service markets have shown greater dynamism in the movement of products and their respective processes, which stimulates foreign direct investment.

By regulating the services sector at a global level, specifically through the GATS, it has been sought to achieve a rapid growth of the international economy. In many countries, this generates a large number of jobs, given that the potential benefits that result from liberalizing the services sector are as vast as in the goods sector. The importance of having an agreement on services, like the GATS, stems from the fact that services play a leading role in the international economy, as they help promote productivity based on information technology and the vast knowledge that it generates.

It is imminent that at the dawn of the twenty-first century, together with the development of the phenomenon of globalization and aided by innovative electronic media, international markets conduct countless commercial and financial transactions, which necessitates their monitoring and regulation. The rules designed to fulfill this function should be clear, simple, and should not have gaps that may create confusion in their application. Furthermore, the authors of these rules should offer justifications for these rules. Only then will they create confidence in the integrity of the market, in the transactions carried out, and in dispute resolutions, thereby achieving a global trade with legal mechanisms that provide safety and confidence for

conducting any type of commercial activity through any electronic means and regardless of how close or far they are from one's business partners.

For students of commercial, or mercantile, law, this century poses a paradigm that will force one to rethink, analyze, and evaluate market institutions that are currently accepted in order to determine whether they will continue being practical and useful in the immediate future. That is, if they are capable of regulating commercial transactions, as well as the persons who conduct those transactions, the things or goods involved in such acts of commerce, and judicial or administrative proceedings. The study of commercial law allows one to preview these new legal challenges and will thus allow institutions to retain their evolutionary character of transformation and conceptual improvement, in keeping with new ideas, technological advances, new media, and new styles of standard form contracts for these consumer markets.

At the dawn of a new millennium, where national sovereignty has seen itself diminished by the globalization of businesses, international financial institutions and policies, as well as by multilateral economic and commercial rules, the theory of the state is undergoing a process of renewal and transformation that leads one to reflect on and make way for the transition from the modern state to the contemporary state. The process of globalization, not only economic, legal, and financial but also technological, has created radical changes regarding production, business organization, and new strategies to support the incorporation and development of multinational businesses in domestic markets.

VI. Harmonization of law

Trade and commercial relations, from their origins to the present century, have evolved from a simple gathering of merchants and transit of goods in a limited geographic space to the creation of regional, multinational, and global companies, giving rise to guiding principles of free trade, regional and global integration processes, free trade agreements, and globalization of the market in a global exchange. This has led to the need for international commercial law that harmonizes the commercial standards of different national legal systems. Currently, the strong tendencies toward market integration due to the mechanics of globalization, trade agreements, and international trade practices, demand a solution to conflicts from a supranational perspective that is embodied in international treaties or agreements to provide a solution to

those problems. Organizations like the United Nations Commission on International Trade Law (UNCITRAL) promote the creation of harmonized law that dilutes the normative hierarchical concepts established by the traditional doctrine in order to prevent disputes that arise in commercial traffic from remaining unresolved, ensuring the implementation of specific rules of application.

In the course of harmonizing commercial law, as it now exists, a very important role has been played by political entities like the United Nations, with its unifying effects through model laws or international treaties and agreements regarding commercial law. These laws and agreements have been very helpful to those that have adopted them and have fostered a harmonized legal language, especially in the areas of financial services, commercial contracts, e-commerce, the international sale of goods, shipping, insurance, intellectual property, copyrights, secured transactions, commercial arbitration, and cross-border insolvency proceedings, among others.

The harmonization of commercial law at the international level should exist not only in aspects regarding contracts, but also in the area of commercial dispute resolution. The important thing to remember about this trend toward harmonization is that it has enabled several countries to analyze the content of proposals, incorporate them into their national laws, combine the different idiosyncrasies and internal phenomena of each country, and allowed countries to adopt or adapt them to their internal legislation without violating their rights. In order to illustrate the idea set forth above, the UNCITRAL Model Laws are as follows: the Model Law on International Commercial Arbitration of 1985, the Model Law on Electronic Commerce of 1996, the Model Law on Cross-Border Insolvency of 1997, the Model Law on Electronic Signatures of 2001, and the Model Law on International Commercial Conciliation of 2002.

VII. Digital commercial age

Through the rapid development of computer and communication systems, commercial activities have become facilitated, shortening distances and times between orders and deliveries by parties, which has allowed greater efficiency for competing on a global scale and thus generated benefits for the world economy. The development of technology and the undeniable globalization of trade and financial services have generated a significant increase in investment options in the last years of the twentieth century, which is also due to the increasingly frequent use of the international stock

market as a funding mechanism comparable to the banking system. One of the major developments in commercial law in the late twentieth century was electronic commerce, which came to revolutionize the formal concept with which business had been conducted and to form a new perception of legal actions without ceasing consideration of the ancient concepts of supply and offer under the Code of Commerce.

In the case of financial services, let us first set forth from the idea that they help the development of business in a very important manner, and thus encourage a country's economic growth. For this reason, it is necessary for them to be accessible to those interested in using them, such as small businesses. Currently, financial instruments have been developed that enable individuals to enter into contracts and conduct business transactions related to financial services, banking, and securities. Specifically, the use of technology allows transactions to be made in fractions of a minute, particularly when done through the Internet, as they connect the service provider directly with the end user who only requires a computer or mobile device to carry out such transactions in only minutes Alpha.

In this regard, the integration of national and international standards in economic and legal areas in a manner that allows the complete identification of a contracting party has truly been a global challenge. Yet, such integration has ensured not only the authenticity of contracts, investments, or payments made via the Internet, but also protect personal data that is often required to perform certain business activities through the aforementioned electronic media. In fact, intellectual property rights have become vulnerable in the face of technological advances.

Moreover, regarding international trade, it should be noted that there are other efforts afoot at the global level and that contribute to the cultural approximation that constitute the databases that contain rulings by judicial courts and arbitration tribunals from remote points of the world. To assist in the uniform interpretation of its texts, UNCITRAL has established a reporting system of rulings based on those texts, which has been abbreviated with the acronym, CLOUT (Case Law on UNCITRAL Texts), which can be accessed in print or online. Something similar exists with UNIDROIT and the database known as UNILEX. Also worthy of mention are those other databases with valuable information, like the one of Pace University in the United States, which pertains to the Vienna Convention and contains a number of judicial rulings, arbitration awards, legal doctrines, and other documents relating to the Convention. There is also the University of Cologne in Germany, with its Center for Transnational Law (CENTRAL) and its method of "creeping codification" of new transnational commercial law.

To this end, a list of principles regarding the *lex mercatoria* has been developed, which remains easily accessible via the Internet, thus allowing one to continually update this database, giving flexibility to this method of coding and avoiding stagnation in the development of the same. Every principle and every rule also references its sources, thus making the full text affordable.

Finally, it is important to consider how technological advances, as elements in a globalized culture, have impacted the field of law in a transcendental manner, which necessitates a constant adaptation of legal institutions to the new digital age.

VIII. Conclusion

In sum, globalization and technological advances require regulating new aspects of commercial relationships. Cross-border insolvency, international contracts, e-commerce, transnational corporations, wire transfers, and international dispute resolution are just some of the new subjects, which are added to those already regulated. It is important to continue reviewing, adjusting, and updating the legal, institutional, multilateral, and international bases for trade, with the goal of strengthening the structure of the World Trade Organization for the benefit of trade in goods, services, and intellectual property, not only to facilitate such exchanges but also to harmonize the domestic laws of nation states and bring about the benefits resulting from such harmonization.

SECURITY INTERESTS IN BANK DEPOSITS UNDER UCC article 9: A PERSPECTIVE

Benjamin GEVA*

SUMMARY: Part I. *Introduction.* Part II. *The Scheme Under Canadian Personal Property Security Legislation*. Part III. *The Scheme Under Revised UCC article 9*.

PART I
INTRODUCTION

In the course of the 19th century, the process of the characterization of the bank deposit as a loan, so as to be owed by the banker to the customer as a debt on a loan, reached in the common law its logical conclusion.[1] The landmark case is *Foley vs Hill*.[2] In that case, the House of Lords dealt with the "*common position of a banker … receiving money from his customer on condition of paying it back when asked*…".[3] Holding that "*the banker is not an agent or factor, but [rather] he is a debtor*",[4] Lord Cottenham spoke of the banker's right to mix and use money deposited

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1 For this discussion in a broader historical and comparative context, see Geva, Benjamin, *The Payment Order of Antiquity and the Middle Ages. A Legal History*, Oxford and Portland Oregon, Hart Monographs, 2011, at 596-604.

2 (1848), 2 HLC 28, 9 ER 1002. A slightly earlier authority is Pott *vs* Clegg, 1847, 16 M & W 321, 153 ER 1212.

3 Foley *v* Hill, *ibidem*, at 43 (HLC), 1008 (ER).

4 *Ibidem*, at 37 (HLC), 1006 (ER).

with him, subject to a repayment obligation of an equivalent sum, either with or without interest.

The analysis of the debtor and creditor relationship between the banker and customer was subsequently refined in *Joachimson* v *Swiss Bank Corp*.[5]

The Court acknowledged that a sum of money held by the banker for the customer on a demand deposit forms a debt "owing or accruing", albeit, in the absence of a demand properly made, "not presently payable"[6] by the banker to the customer. As such, the deposit is garnishable by the customer's creditors.[7]

In the hands of a debtor, balance available on a deposit account[8] held by that person is an item of property. Accordingly, the debtor may give it as security for credit extended to him or her by a third party. Funds deposited to secure an obligation are known to constitute "cash collateral". The latter term is a misnomer; the 'deposit' is a debt owed by the depositary, whether or not it is a bank. It neither consists of 'cash', in the sense of coins and banknotes, nor is the 'cash' truly segregated.[9]

As well, a bank[10] extending credit to its customer may rely on a credit balance in the customer's account with it. In each case, upon the account holder's default on the credit contract, the creditor would like to be in a position to apply the credit balance in the deposit account towards the discharge of the account holder's indebtedness on the credit contract.

Various rights and devices exist to obtain priority in the balances of deposit accounts maintained by a defaulting account holder. This paper focuses on the security interest given by the customer either to the bank where the deposit account is maintained or to a third party. The discussion is on the priority among competing security interests and between a security interest and other rights. Such rights may be of a garnishor seizing or assum-

5 1921, 3 KB 110 (CA).

6 Terminology is, however, not always consistently used. Cf. e.g. the ambiguous use of the word 'due' as observed in Ontario Hydro-Electric Power Commission *v* Albright (1922), 64 SCR 306, at 312: The word "due" in relation to moneys in respect of which there is a legal obligation to pay them may mean either that the facts making the obligation operative have come into existence with the exception that the day of payment has not yet arrived, or it may mean that the obligation has not only been completely constituted but is also presently exigible.

7 Supra, n. 5 at 131.

8 In this paper, unless specifically indicated otherwise, terms such as 'deposit account', 'bank deposit', 'balance due on the account' and similar expressions are used loosely and interchangeably.

9 The origin of the term (in a different context and not identical sense) can be probably traced to the United States Bankruptcy Code 11 USC §363(a), 1978.

10 Unless otherwise indicated, 'bank' (or 'banker') loosely denotes any type of deposit-taking institution, usually making loans and extending credit in its own name.

ing control of the account. Alternatively, they may be of the bank holding the account and seeking to combine the account in a credit position with another account in a debit position. In so combining accounts, the bank holding them purports to avoid the release of the funds in the account in credit to a third-party creditor of the customer, and rather, use them to satisfy the customer's debt owed to the bank on the account in debit.

This paper explores from a Canadian perspective the provisions of article 9 of the Uniform Commercial Code as revised in 1999 as a model for reform for Canadian provinces and territories that adopted personal property security legislation. This legislation has not followed the 1999 UCC revisions. The perspective is particularly that of Ontario where a proposal for perfecting security interests in deposit accounts by control inspired by the 1999 US scheme is pending.[11] The article is a sequel to an earlier one exploring at length the deficiencies of the current situation but does not touch upon any specific proposal for reform.[12]

The paper proceeds as follows. Part II analyzes the statutory scheme under personal property legislation in Canada, particularly the one of the Ontario Personal Property Security Act ("OPPSA").[13] This statute, as others under this name in all common law provinces and territories, governs 'secured transactions',[14] or more specifically, "*security agreements*"[15] *giving rise to* "*security interests*"[16] in personal property.[17] Part III sets out the treatment of the subject

[11] For the proposal visit, Ontario Bar Association, "Perfecting Security Interests in Cash Collateral", 2012, online: *http://www.oba.org/en/pdf/perfectingSecurityInterests.pdf*.

[12] Geva, B. "Rights in Bank Deposits and Account Balances in Common Law Canada", 2012, 28, *Banking and Finance Law Review*. The two articles are of different scope and focus; nevertheless, some overlap is inevitable.

[13] RSO 1990, c P.10, Last amendment: 2012, c 8, Sched 45.

[14] Term is not defined in the OPPSA which in principle is stated in section 2 to apply to:

[(a)] every transaction without regard to its form and without regard to the person who has title to the collateral that in substance creates a security interest including, without limiting the foregoing; (i) a chattel mortgage, conditional sale, equipment trust, debenture, floating charge, pledge, trust indenture or trust receipt, and (ii) an assignment, lease or consignment that secures payment or performance of an obligation;

[(b)] a transfer of an account or chattel paper even though the transfer may not secure payment or performance of an obligation; and

[(c)] a lease of goods under a lease for a term of more than one year even though the lease may not secure payment or performance of an obligation.

[15] Defined in OPPSA Section 1(1) to mean "an agreement that creates or provides for a security interest and includes a document evidencing a security interest".

[16] Defined in OPPSA Section 1(1) to mean"an interest in personal property that secures payment or performance of an obligation, and includes, whether or not the interest secures payment or performance of an obligation".

[17] Comprehensively defined in OPPSA Section 1(1) effectively to cover all items of property other than real property.

under the 1999 revisions of article 9 of the Uniform Commercial Code in the United States. Specifically these revisions introduced perfection by control and a new priority scheme.[18] Part IV highlights the inadequacy of the present scheme and hence the need for reform. It briefly assesses the revised scheme under article 9 as a basis for statutory reform in Canada.

PART II
THE SCHEME UNDER CANADIAN PERSONAL PROPERTY SECURITY LEGISLATION

In the United States, former article 9 of the Uniform Commercial Code did not apply to the "transfer of an interest in any deposit account",[19] thereby excluding security interests in deposit accounts serving as original collateral. At the same time, under the OPPSA, from its original adoption,[20] a deposit account has fallen into the definition of 'account';[21] in turn, 'account' is a species of 'intangible'.[22] A security interest in an intangible is perfected by the registration of a financing statement.[23]

In *Caisse populaire Desjardins de l'Est de Drummond v Canada*,[24] the Supreme Court of Canada analyzed a contractual term under which a bank[25] took a security interest in a deposit account maintained with it.[26] Considering the agreement as giving the Caisse a right over the customer's property,[27] the ma-

[18] Another noteworthy innovation, pointed out further below, is that of the coverage given to security interests in bank deposits in the first place. However, as also discussed further below, this has always been the legal position in Canada.

[19] Section 9-104(l), 1972.

[20] The Personal Property Security Act, RSO 1970, c 344.

[21] Defined in OPPSA Section 1(1) to mean "a monetary obligation not evidenced by chattel paper or an instrument, whether or not it has been earned by performance, but does not include investment property".

[22] Defined in OPPSA Section 1(1) to mean "all personal property, including choses in action, that is not goods, chattel paper, documents of title, instruments, money or investment property". "Account" is not excluded; hence it is included.

[23] OPPSA Section 23.

[24] 2009, 2 SCR 94.

[25] Strictly speaking it was a Caisse Populaire, which is the equivalent of a credit union in Quebec.

[26] See Binnie, Ian J., "Comment on Caisse populaire Desjardins de l' Est de Drummond *v* Canada" (2011), 26 *Banking* and *Finance Law Review* 327. From a Quebec perspective see Deschamps, Michel "La compensation comme mécanisme de garantie et les sûretés sur les dépôts bancaires", (2012) published in Lemieux, M., *Le Droit bancaire en 2011: nouveautés et tendances*, Les Éditions Thémis, 2012, at 1.

[27] Drummond, supra, n. 24 at para 16.

jority of the Supreme Court of Canada concluded that the agreement gave the Caisse a security interest in customer's saving deposit. Effectively, this followed the English position under which it is feasible for a debtor, including a bank owing on a deposit account, to take a security interest in the very debt it owes.[28] Thus, the deposit account is collateral available to both the bank owing it and any third party.

Under the OPPSA, the first to register obtains priority against any competing security interest.[29] A notable exception is a holder of a "purchase-money security interest", who must be either a seller of a deposit account (such as a seller of an already issued certificate of deposit) who takes a security interest in it "to secure payment of or part of its price" or who holds a security interest to secure value given "for the purpose of enabling the debtor to acquire rights in or to the *deposit account* to the extent that the value is applied to acquire *such* rights".[30] A holder of a "purchase-money security interest" in an intangible, which became perfected "before or within 15 days after its attachment", has priority over any other security interest in deposit account.[31] "Attachment" in the debtor's hands consists of receiving value, having rights in the deposit account, and signing a security agreement adequately describing the deposit account.[32] Between two unperfected security interests it is the first to attach which prevails.[33]

As well, until perfected, a security interest[34] is defeated by "*a person who causes the collateral to be seized through execution, attachment, garnishment … or other legal process*".[35] An unperfected security interest is also defeated by a creditors' representative such as a trustee in bankruptcy.[36] The general principle is that of 'first in time first in right'. However, a holder of a "purchase money security interest", securing either the purchase price of the collateral or the loan that

[28] Re Bank of Credit and Commerce International, n. 8, 1998, 1 AC 214 (HL), r'vsg, 1996 2 All ER 121 (CA) on this point and disapproving of Re Charge Card Services Ltd., 1986, 3 All ER 289 (Ch D).

[29] OPPSA Section 30 (1) Rule 1.

[30] OPPSA Section 1(1).

[31] OPPSA Section 33(2)(b).

[32] OPPSA Section 11(2).

[33] OPPSA Section 30(1) Rule 4. Under OPPSA Section 11(2), "attachment" consists of receiving value, having rights in the deposit account, and signing a security agreement adequately describing the deposit account.

[34] In the context of an intangible, "perfection" requires both attachment and registration. OPPSA Section 19.

[35] OPPSA Section 20(1)(a)(ii).

[36] OPPSA Section 20(1)(b).

funded the payment for it,[37] prevails over a seizing or garnishing creditor as well as a creditors' representative such as a trustee in bankruptcy even if perfected after seizure or bankruptcy, as long as perfection by registration occurs "before or within 15 days after … attachment".[38] A seizing or garnishing creditor will defeat an optional future advance by a holder of a perfected security interest, who received a written notification of the seizure or garnishment.[39] No specific priority is accorded to a bank, which holds a security interest in a deposit account held on its books.

Under OPPSA Section 25(1), "[w]here collateral gives rise to proceeds, the security interest therein … (b) extends to the proceeds". Under OPPSA Section 25(3), *"A security interest in proceeds is a continuously perfected security interest if the interest in the collateral was perfected when the proceeds arose"*. Both perfection and its priority in original collateral are carried over to the proceeds. The continued priority of a purchase-money security interest holder in the proceeds of the original collateral is specifically provided for.[40]

As defined in OPPSA Section 1(1), "proceeds" are "*identifiable or traceable personal property*[41] *in any form derived directly or indirectly from any dealing with collateral or the proceeds therefrom*". As a matter of general law, funds derived from the sale of the original collateral deposited to a segregated 'proceeds' account are "identifiable" proceeds under the common law.[42] At the same time, funds derived from the sale of the original collateral deposited to a general account and mixed with other funds of the debtor may be "traceable" in equity.[43] By reference to this, the cumulative effect of OPPSA Section 25(1) and (3) is that the existence, perfection and priority of a security interest in an original collateral are carried also to its "identifiable" and "traceable" proceeds in the form of funds deposited in the debtor's bank accounts. In principle, on that count, the OPPSA follows suit article 9 of the Uniform Commercial Code.[44]

OPPSA Section 25(1)(a), provides that where "the secured party expressly or impliedly authorized the dealing with the collateral free of the

[37] See definition in OPPSA Section 1(1).

[38] OPPSA Section 20(3)(b).

[39] OPPSA Section 30(4).

[40] See Section 33(1) and (2), respectively for proceeds of inventory and other collateral.

[41] For the definition of "personal property" under the OPPSA, see, supra, n. 17.

[42] See e. g. Canadian Western Millwork Ltd *v* Royal Bank of Canada, 1964, SCR 631.

[43] See e. g. Flexi-Coil Ltd v Kindersley District Credit Union Ltd., 1993, 107 DLR (4th) 129 (Sask CA).

[44] See in general UCC Section 9-315 in conjunction with Section 9-102(a) (64). Unless indicated otherwise, all UCC references are to the 1999 Official Text.

security interest", a transferee, even with knowledge of the security interest, takes the collateral free of the security interest. Even in the absence of such authorization, a bona-fide payee may be protected under general rules conferring a 'currency' quality on 'bank money'.[45] However, protection provided by the 'currency' quality of 'bank money' may not be comprehensive. Protection may even not be accorded to a taker of cash collateral deposited to the taker's own account competing with a secured creditor of the debtor with an earlier registration. This is so since the 'transfer' or the deposit of funds of which the cash collateral consists is not 'payment'[46] but rather a transaction intended to secure the debtor's obligation to the taker of the cash collateral.[47] As such it is covered by the OPPSA and triggers its priority scheme. Particularly, an earlier registrant claiming under a security agreement covering either the source of the funds or the debt of which they consist will claim priority over the taker of the cash collateral.[48] In some cases, priority may be accorded to a secured party tracing the proceeds of collateral in which the secured party has a purchase money security interest priority.[49]

A conflict may arise between a holder of a security interest in a deposit account and the deposit holding bank's right to withhold payment on the basis of a contractual set-off. Setting aside funds as collateral from a deposit account in the debtor's name to secure the debtor's obligation is in the form of an assignment of a credit balance. Thus, in principle,[50] both absolute trans-

[45] For a general discussion see Crawford, Bradley, *The Law of Banking and Payment in Canada*, vol 1, Toronto, Canada Law Book, Looseleaf-updated to December 2011, at para. 3:20.10(2), 3:30.10 and 3:40.10(4)(d)(i). This conclusion is also drawn from R *v* Canadian Imperial Bank of Commerce, 2000, 51 OR (3d) 257 (CA); Bank of Montreal *v* iTrade Finance Inc, 2009 ONCA 615, 252 OAC 291; Indian Head Credit Union *v* Andrew, 1992, 97 DLR (4th) 462 (Sask CA); Transamerica Commercial Finance Corp, Canada *vs.* Royal Bank of Canada, 1990, 70 DLR (4th) 627 (Sask CA); Flexi-coil Ltd *v* Kindersley District Credit Union Ltd, 1993, 107 DLR (4th) 129 (CA). For a recent American case (citing earlier authorities) on the point see Variety Wholesalers *v* Salem Logistics Traffic Services, 723 SE 2d 744, NC SC, 2012.

[46] So as to benefit a bona fide payee, *Idem*.

[47] For the scope of the OPPSA to cover such a transaction, see OPPSA Section 2(a).

[48] For the priority of the first to register under OPPSA Section 30(1) Rule 1, see text, supra, and n. 29.

[49] The priority of a holder of a purchase security interest in both in the original collateral and its proceeds is provided for in OPPSA Section 33.

[50] Exceptions are set out in OPPSA Section 4(1), providing that the Act does not apply, particularly as follows:

(c) to a transfer of an interest or claim in or under any policy of insurance or contract of annuity, other than a contract of annuity held by a securities intermediary for another person in a securities account;(g) to a sale of accounts or chattel paper as part of a transaction to which the Bulk Sales Act applies;

fers and transfers intended for security of "accounts", including deposit accounts and other balances due from banks, are governed in common law Canada by personal property security legislation.[51]

The assignment of a debt does not prejudice the debtor on the assigned debt, frequently referred to as the 'account debtor'[52] so as to distinguish that person from the assignor, who is the debtor in the transaction in which the assigned debt is the collateral.[53] "The assignee … can acquire no greater rights under the assignment than those enforceable by the assignor, and he therefore, takes subject to all defences existing in respect of the right assigned which would be available against the assignor seeking to enforce the rights assigned".[54] This principle, originally enunciated for equitable assignments,[55] was specifically codified for statutory assignments, describing the assignee's position as "subject to all equities" as "if this section had not been enacted".[56] In the footsteps of the earlier version of UCC Section 9-318(1) in the United States,[57] personal property security legislation in Canada, particularly as clarified recently by a new OPPSA Section 40(1.1),[58] is to the same effect.

Exercised as a contractual set-off, the combination of accounts by the bank is a defence available against a secured party/assignee. Thus, as against a pre-assignment contractual right of set-off, a holder of a security interest

(h) to an assignment of accounts made solely to facilitate the collection of accounts for the assignor; or

(i) to an assignment of an unearned right to payment to an assignee who is to perform the assignor's obligations under the contract.

51 OPPSA Section 2(a) and (b).

52 See e. g. definitions in OPPSA Section 40(1) and UCC Section 9-102(a)(3).

53 See definitions of "debtor" in OPPSA Section 1(1) and UCC Section 9-102(a)(1)(28)(B).

54 White, Frederick T. & Tudor, Owen D., *White & Tudor's Leading Cases in Equity*, 9th ed., London and Toronto, Sweet & Maxwell, 1928, at 136.

55 Equitable assignments are discussed in Chapter 4 of Tolhurst, Greg, *The Assignment of Contractual Rights*, Oxford and Clarendon Oregon, Hart, 2006. Equitable assignment need not be absolute; it may be by way of charge also as a matter of form. As well, it is effective to transfer title to the assignee regardless of the lack of notice to the debtor. See Gorringe v Irwell India-Rubber and Gutta-Percha Works, 1885, 34 Ch D 128.

56 The original provision is Section 25(6) of the English Judicature Act, 1873 (UK), 36 & 37 Vict 66. The present provision to that effect in England is Section 136 of the Law of Property Act, 1925 (UK), Chapter 20, 15 & 16 Geo 5. In Ontario, it is Section 53(1) of the Conveyancing and Law of Property Act, RSO 1990, c C.34. Statutory assignment must be absolute in writing, of the whole balance, and of which express notice in writing is given to the debtor, *Idem*.

57 Official Texts of 1962 and 1972. The present statutory provision in the United States, Official Text, 1999, is UCC article 9-404 which is almost verbatim.

58 2006, c 34, Sched E, s 11 (1).

in the deposit account is defeated by the deposit holding bank. This is so even where the security interest is perfected. At the same time, post-assignment contractual right of set-off is an unwarranted modification of the assigned contract which may not be raised against the assignee.[59]

In the absence of contractual set-off, there is no unanimity in the scholarly view in Canada on the priority of the bank's right to combine accounts.[60] At one end of the spectrum, Cuming asserts that "the rules of equitable set-off provide the most consistent and practical" solution so as to protect the bank combining accounts only when it acts without knowledge.[61] At the other end of the spectrum, Crawford is of the view that the bank's right to combine accounts, being "inherent in the banker-customer relation in the common law" necessarily prevails regardless of other considerations.[62]

Equitable set-off is exercised by the assertion "as a defence to [an] action" of "grounds… which (prior to the *Judicature Act)* would have entitled a defendant to file a bill in Chancery to restrain the plaintiff from proceeding with his action…"[63] Such grounds are based on the breach of a duty arising from a contract sued upon or a matter closely related to it.[64] Hence, I find 'equitable set-off' to be irrelevant. At the same time I am persuaded neither by the "inherent nature" of the bank's right nor by its alleged reach. In my mind the resolution of the set-off priority issue depends on the nature of the banker's right to combine accounts. I thus argue that as long as it is treated as a *right of set-off operating like a legal set-off*,[65] and other than

[59] OPPSA Section 40(3).

[60] For the bank's right to combine account as a set-off right, see e. g. McCracken, Sheelagh, *The Banker's Remedy of Set-off*, 3d. ed., Haywards Heath, Bloomsbury Professional, 2010 and Derham, Rory, *Derham on the Law of Set-Off*, 4th ed., Oxford, OUP, 2010, at 675 – 739. See also TeSelle, John, "Banker's Right of Setoff – Banker Beware", 34 *Oklahoma Law Review*, 40, 1981.

[61] Cuming, Ronald CC., "Security Interests in Accounts and the Right of Set-Off", 6 *Banking and Finance Law Review*, 1991, 299, at 322.

[62] Crawford, supra, n. 45 vol 2 at § 9:60.20(6)(b).

[63] Bankes *vs*. Jarvis, [1903] 1 KB 549, at 552.

[64] See Hanak *vs*. Green, [1958] 2 QB 9 (CA), at 24, where "[t]here was a close relationship between the dealings and transactions which gave rise to the respective claims". Damages suffered by the debtor caused by the breach, whether in a liquidated or unliquidated amount, to which the debtor is entitled at the time of the action, may then be set off against the sum claimed by the creditor. The effective exercise of the equitable set-off by the defendant results in the reduction of the amount owed by the defendant-debtor to the plaintiff-creditor. Reduction is by the amount of damages stemming from the breach by the plaintiff-creditor of a duty flowing out and inseparably connected with the same contract.

[65] Both Baker *vs*. National City Bank, 511 F2d 1016, 1018 (6th Cir 1975) and UCC Section 4-303(a) support this understanding of the bank's right to combine account.

where it could benefit from the authority given by the secured party to the customer to dispose of the collateral free of the security interest, *the bank's right to combine accounts*, is defeated by a security interest. At the same time, where it is characterized as a *current account set-off*,[66] the banker's *right to combine accounts* defeats a competing security interest. I suppose that the result does not depend on whether the security interest is perfected. It is only as a *current account set-off* the right to combine accounts is "inherent in the banker-customer relation"[67] so as to prevail over all adverse claims.

A bank combining accounts, even if it is to be considered as a lien holder,[68] does not qualify under OPPSA Section 31 as "a person [who] in the ordinary course of business furnishes materials or services with respect to goods that are subject to a security interest". Under that provision, such a person defeats even a perfected security interest.[69] At the same time, under OPPSA Section 20(1)(a)(i) an unperfected security interest is subordinate to "the interest of … a person who … has a lien given under any other Act or by a rule of law or who has a priority under any other Act". While no "other Act" specifically gives priority to the right to combine accounts, priority is given under OPPSA Section 20(1)(a)(i) to "a lien given under … a rule of law". Priority continues only until the security interest is perfected. It follows that other than in circumstances governed by OPPSA Section 31, a perfected security interest defeats a lien. Thus, if it is a *lien*, the bank's *right to combine accounts* defeats an unperfected *s*ecurity interest. At least as long as the debtor/customer is not authorized to dispose of the proceeds free of the security interest, the lien is defeated by a perfected security interest.[70] I suppose that as a lien the bank's right to combine accounts also defeats garnishment.

66 Re Charge Card Services Ltd at 307 and see Gullifer, Louise (ed.), *Goode on Legal Problems of Credit and Security*, 4th ed., London, Sweet & Maxwell, 2008, at 307.

67 See text, supra, n. 62.

68 Position rejected in Halesowen Presswork & Assemblies v National Westminster Bank, 1972, 1 AC 785, at 802 and 810 (HL). Rejection was questioned by EP Ellinger, Lomnicka, E. and Hare, CVM. *Ellinger's Modern Banking Law*, 5th ed., Oxford, University Press, 2011, at 251.

69 OPPSA Section 31 reads in full as follows:

Where a person in the ordinary course of business furnishes materials or services with respect to goods that are subject to a security interest, any lien that the person has in respect of the materials or services has priority over a perfected security interest unless the lien is given by an Act that provides that the lien does not have such priority.

70 Under OPPSA Section 25(1), the security interest survives the unauthorized disposition.

PART III
THE SCHEME UNDER REVISED UCC ARTICLE 9

I. COVERAGE

The priority scheme under article 9 of the American Uniform Commercial Code ("UCC article 9") is fundamentally the same as in Canadian provincial personal property security legislation. Since the former inspired the latter, this is of course neither surprise nor coincidence. Briefly stated, a garnishor, a creditor's representative such as a trustee in bankruptcy, or a perfected security interest holder defeats an unperfected security interest.[71] Perfection of a security interest in accounts and general intangibles[72] is by filing.[73] Between two perfected security interests the first to file prevails.[74] Otherwise, between two unperfected security interests, the first to attach gets the priority.[75] Attachment requires value to be given and the debtor to have rights in the collateral and sign a security agreement.[76] Finally, super-priority is accorded to a holder of timely perfected purchase-money interest,[77] in the deposit account to the extent of properly 'identifiable or traceable' proceeds deposited in it.[78]

However, in contrast to Canada, previous versions of article 9 did not cover the deposit account as original collateral. This omission proved to be unfortunate.[79] Accordingly, in 1999 UCC article 9 was revised to provide for

71 UCC Sections 9-317(a)(2) and 9-322(a)(2).

72 Respectively defined in UCC Section 9-102(a)(2) and (42).

73 UCC Section 9-310. 'Filing' under the UCC is the same as 'registering' under personal property security legislation.

74 UCC Section 9-322(a)(1).

75 UCC Section 9-322(a)(3).

76 UCC Section 9-203.

77 See definitions of "purchase-money security interest" and "proceeds" in UCC Sections 9-103(b) and 9-102(a)(64). In principle these definitions are similar to those under the OPPSA set out in, supra, Part II.

78 The "purchase-money security interest" priority in original collateral and proceeds is governed by UCC Section 9-324.

79 See e. g. Zubrow, Luize E., "Integration of Deposit Account Financing into article 9 of the Uniform Commercial Code: A proposal for a Legislative Reform", 68 *Minnesota Law Review*, 1983-1984, 899; McLaughlin, Gerald T., "Security Interests in Deposit Accounts: Unresolved Problems and Unanswered Questions under Existing Law", 54 *Brooklyn Law Review* 45, 1988-1989, and Greene, Dwight L., "Deposit Accounts as Bank Loan Collateral Beyond Setoff to Perfection – The Common Law is Alive and Well", 39 *Drake Law Review* 259, 1989-1990. For pre 1999 law as "a matrix of legal principles unlike any other in the

a specific scheme[80] for the perfection (other than by filing or registration), priority,[81] and enforcement[82] of a security interest[83] in a debt owed by a bank for funds or monetary value credited to a deposit account.[84] The collateral[85] is treated as "deposit account";[86] it is a distinct category of collateral that is specifically excluded from the definition of "general intangible".[87]A security agreement purporting to cover it must reasonable identify it.[88]

"Deposit account" is defined in UCC Section 9-102(a)(29) to mean "a demand, time, savings, passbook, or similar *account*[89] maintained with a bank".

Code", see Harrell, Alvin C.",Security Interests in Deposit Accounts: A Unique Relationship Between the UCC and Other Law", 23:2 UCCLJ 153, 1990.

80 Per the recommendations of Kroener III, William F. (Chair) and Sepinuck, Stephen L. (Reporter), "Report of the Subcommittee on the Use of Deposit Accounts as Original Collateral", Working Document No. M6-44, in Permanent Editorial Board for the Uniform Commercial Code, PEB Study Group Uniform Commercial Code article 9 Appendices to Report (Phil: PEB for UCC, 1992) at 325; as summarized and adopted in Permanent Editorial Board for the Uniform Commercial Code, PEB Study Group Uniform Commercial Code article 9 Report, December 1st., 1992, at 68.

81 Under UCC Section 9-304(a), it is "The local law of a bank´s jurisdiction [which] governs perfection, the effect of perfection or nonperfection, and the priority of a security interest in a deposit account maintained with that bank". Rules determining that jurisdiction are provided in UCC Section 9-304(b). Briefly stated, these rules determine the law applicable according to enumerated factors, ie., the parties' agreement, and in its absence, the location of "the office identified in an account statement as the office serving the customer's account is located", or, as a last resort, the location of "the chief executive office of the bank".

82 The secured party's right to apply the balance of the deposit account to the secured obligation or instruct the bank to pay for its benefit is provided for in UCC Section 9-607(a).

83 Broadly defined in UCC Section 1-201(b)(35) to be "an interest in personal property… which secures payment or performance of an obligation".

84 For the debt relationship created by the deposit of money with a banker, see Foley v Hill (1848), 2 HLC 28, 9 ER 1002. The case is discussed above in Part II.

85 Under UCC Section 9-102(a)(12), "collateral" is defined to mean "the property subject to a security interest …".

86 Principal provisions are listed in Official Comment 16 to UCC Section 9-109.

87 See UCC Section 9-102(a)(42). Accordingly, "a security agreement covering general intangibles will not adequately describe deposit accounts". Official Comment 16 to UCC Section 9-109. "General intangible" is the residual category of personal property "that is not included in the other defined types of collateral". See Official Comment 5(d) to UCC Section 9-102.

88 As required in UCC Section 9-108. See Official Comment 16 to UCC Section 9-109. Note that under UCC Section 9-108(c), a supergeneric description, such as "all the debtor's assets" or "all the debtor's personal property", "does not reasonably identify the collateral".

89 In principle, under UCC Section 9-102(a)(2), "account" is defined to mean "a right to payment of a monetary obligation, whether or not earned by performance". Cf. the narrower definition in UCC Section 4-104(a)(1) under which "account" is defined to mean "any

Investment property[90] or accounts evidenced by an instrument[91] are specifically excluded. In turn, "bank" is defined in UCC Section 9-102(a)(8)[92] to mean "an organization that is engaged in the business of banking" so as not to be limited to commercial banks,[93] but rather to include also "savings banks, savings and loan associations, credit unions, and trust companies". Effectively, this means a deposit account covered by article 9 may be maintained with any deposit-taking institution.[94] However, other than with respect to proceeds and priorities therein, article 9 does not apply to "an assignment of a deposit account in a consumer transaction".[95] The latter are defined to mean "a transaction in which (i) an individual incurs an obligation primarily for personal, family, or household purposes, (ii) a security interest secures the obligation, and (iii) the collateral is held or acquired primarily for personal, family, or household purposes…".[96]

II. Perfection

Other than in connection with proceeds of collateral deposited into a deposit account,[97] "a security interest in a deposit account may be per-

deposit or credit account with a bank, including a demand, time, savings, passbook, share draft, or like account, other than an account evidenced by a certificate of deposit".

90 "Investment property" is defined in UCC Section 9-102(49) to mean "a security, whether certificated or uncertificated, security entitlement, securities account, commodity contract, or commodity account". Accordingly, 'deposit account' "does not include shares in a money-market mutual fund, even if the shares are redeemable by check". Official Comment 12 to UCC Section 9-102.

91 UCC Section 3-104 defines "Certificate of deposit" as a type of "instrument". Official Comment 12 to UCC Section 9-102 confirms that "A deposit account evidenced by an instrument is subject to the rules applicable to instruments generally".

92 Official Comment 12 to the provision acknowledges the derivation of this definition from similar definitions in Sections 4-105(1) and 4A-105(a)(2). See also Section 1-201(a)(4).

93 A point made for a similar definition in both Official Comment 1 to Section 4A-105 and Official Comment 1 to Section 4A-105.

94 'Deposit taking' is at the heart of the 'banking' enterprise. See in general e. g., Commissioners of the State Savings Bank of Victoria *vs.* Permewan, Wright & Co Ltd, 1915,19 CLR 457, at 471 and United Dominion Trust v Kirkwood, 1966, 2 QB 431 at 447. See also Canadian Pioneer Management *vs.* Labour Relations Board of Saskatchewan, 1980, 1 SCR 433 at paras 51-54. As a rule, a deposit-taker is a regulated financial institution.

95 UCC Section 9-109(d)(13), which further provides for the application of UCC Sections 9-315 and 9-322 "with respect to proceeds and priorities in proceeds".

96 UCC Section 9-102(a)(26).

97 Perfection and continuation of perfection of a security interest in proceeds are respectively governed by UCC Sections 9-315(c) and (d) which are stated by UCC Section 9-312(b)

fected *only*[98] by control".[99] Under UCC Section 9-314(b), it "is perfected by control … when the secured party obtains control and remains perfected by control only while the secured party retains control".Requirements for control of a deposit account are set out in UCC Section 9-104(a), under which:

A secured party has control of a deposit account if:

1. the secured party is the bank with which the deposit accountis maintained;[100]

2. the debtor, secured party, and bank have agreed in an authenticated[101] record[102] that the bank will comply with instructions originated by the secured party directing disposition of the funds in the deposit account without further consent by the debtor; or

3. the secured party becomes the bank´s customer[103] with respect to the deposit account.[104]

Under UCC Section 9-342, a bank is not required to enter into a control agreement "even if its customer so requests or directs". This acknowl-

to apply also to proceeds in the form of a deposit account.

98 The exclusion of perfection by registration (as opposed to its subordination to a security interest perfected by control) seems to me unjustifiable.

99 UCC Section 9-312(b)(1) [Emphasis added]. Cf. UCC Section 9-314(a), providing in general, that that "A security interest in investment property, deposit accounts, letter-of-credit tights, or electronic chattel paper may be perfected by control of the collateral".

100 Such a 'security interest' is to be distinguished from the banker's right of set-off. See UCC Section 9-340 further discussed below.

101 Under UCC Section 9-102(a)(7), "Authenticate" means: (A) to sign; or (B) to execute or otherwise adopt a symbol, or encrypt or similarly process a record in whole or in part, with the present intent of the authenticating person to identify the person and adopt or accept a record.

102 Under UCC Section 9-102(a) (69), "Record", except as used in "for record", "of record", "record or legal title", and "record owner", means information that is inscribed on a tangible medium or which is stored in an electronic or other medium and is retrievable in perceivable form.

103 Defined in UCC Section 4-104(a)(5) (incorporated by reference in UCC Section 9-102-b) as "a person having an account with a bank or for whom a bank has agreed to collect items, including a bank that maintains an account at another bank".

104 While in control, the secured party:

1. May hold as additional security any proceeds, except money or funds, received from the collateral;

2. Shall apply money or funds received from the collateral to reduce the secured obligation, unless remitted to the debtor: and

3. May create a security interest in the collateral.

See UCC Section 9-207(c). The duty to terminate control where "there is no outstanding secured obligation and the secured party is not committed to make advances…" is governed by UCC Section 9-208.

edges the bank's rights with respect to the deposit and recognizes its discretion in carrying out its business. Furthermore, under that section, "A bank that has entered into such an agreement is not required to confirm the existence of the agreement to another person unless requested to do so by its customer". This is consistent with UCC Section 9-210 under which only the secured party is under an obligation to provide information regarding the collateral; it is obliged to do so only to the debtor, with whom alone a third party is supposed to inquire. In any event, as indicated, Section 9-342 nevertheless obliges the bank to confirm the existence of a control agreement to a third party when it is "requested to do so by its customer".

Surely, the secured party's 'control' may be exclusive, so as to relate to a blocked account from which the debtor is not allowed to withdraw. At the same time, 'control' needs not necessary be exclusive, and may be shared with the debtor. There is no requirement for the "absolute dominion to the exclusion of the debtor".[105] Rather, according to UCC Section 9-104(b).

A secured party that has satisfied subsection (a) has control, even if the debtor retains the right to direct the disposition of funds from the deposit account.

Stated otherwise, 'control' can even be exercised over an operational account, from which the debtor is allowed to withdraw. Moreover, 'control' may be given on a standby basis, under an arrangement that does not allow the interference by the secured party in the everyday running of the account in the ordinary course of business. Accordingly, from a strictly legal perspective, "control" includes 'the right to control'; the latter is very much like the secured party's right under the English 'floating charge' on assets of a going concern, as well as under the modern 'floating lien' on inventory and other secured assets that a debtor is free to dispose of in the ordinary course of business, free of the security interest.[106]

Thus, where the secured party has a 'mere' right to control, the debtor carries on his or her business as usual, fully exercising dominion over the deposit account, until actual 'control' is assumed by the secured party, as in 'crystallization' in the English 'floating charge'.[107] Depending on the control agreement, such could be the case in each of the options enumerated in UCC Section 9-104(a), namely, whether the secured party (i) is the bank

[105] Official Comment 5 to UCC Section 9-312.

[106] For the floating charge see in general Governments Stock & Other Securities Investment Co *vs.* Manila Ry Co, 1897, AC 81 at 86. For the floating charge not being a "specific mortgage of … assets, plus a licence … to dispose of them" see Evans *vs.* Rival Granite Quarries, Ltd., 1910, 2 KB 979 at 999 (CA).

[107] *Idem*.

on whose books the deposit account is maintained, (ii) became a customer of the bank with respect to the deposit account, or (iii) otherwise became a party to a control agreement with the debtor and the bank.[108]

III. Priority rules

Priority of security interests in a deposit account is provided for in UCC Section 9-327 and can be summarized as follows:

1. A secured party who has control defeats any other secured party.[109] In light of UCC Section 9-312(b), stating that "a security interest in a deposit account may be perfected *only* by control",[110] the competing secured party, to be defeated, may have had an unperfected security interest or be a proceeds claimant, even with a perfected security interest.[111]

2. Among secured parties who have control, the following rules apply:

a. A secured party who became the bank's customer with respect to the deposit-account prevails over the bank with which the deposit account is maintained;[112]

b. Otherwise, "a security interest held by the bank with which the deposit account is maintained has priority over a conflicting security interest held by another secured party",[113] and

c. In all other cases, "security interests perfected by control … rank according to priority in time of obtaining control".[114]

With respect to the debtor's deposit account, the super-priority of the bank where the account is maintained is rationalized in Official Comment 4 to Section 9-327 as a means to enable "banks to extend credit to their depositors without the need to examine either the public record or their own records to determine whether another party might have a security interest in the deposit account". In releasing a bank from the onus of examining their own records, this rationale appears to go too far; and yet it is also too

[108] UCC Section 9-104(a). See text, supra, that follows n. 100.

[109] Subsection (1).

[110] Emphasis added; see text, supra, and notes 97-99.

[111] For the perfection and priority of a security interest in "identifiable or traceable" proceeds placed in a deposit account see, supra, nn. 77-78 and 97.

[112] Subsection 4. Note, however, that the provision does not state that such a secured party prevails over an earlier secured party other than the bank with which the deposit account is maintained.

[113] Subsection 3.

[114] Subsection 2.

narrow in not mentioning the advantage to the customer in having its bank more ready to extend credit.

Protection from the super-priority of the bank where the deposit account is maintained can be achieved by a secured party becoming "the bank's customer with respect to the deposit account" under UCC 9-104(3).[115] As well, a secured party may obtain from the bank a subordination agreement as permitted by UCC Section 9-339. Also, "A secured party who claims the deposit account as proceeds of other collateral can reduce the risk of becoming junior by obtaining the debtor's agreement to deposit proceeds into a specific cash-collateral account and obtaining the agreement of that bank to subordinate all its claims to those of the secured party".[116] Finally, a proceeds claimant can also require a debtor to pay directly to an account under the secured party's control.[117]

Priority accorded to a secured party in a deposit account, including the bank where it is maintained, is however not without exception. Thus, UCC Section 9-332(b) "affords a broad protection to transferees who take funds from a deposit account .."..[118] Thereunder, a transferee of funds from a deposit account takes the funds free of a security interest in the deposit account unless the transferee acts in collusion with the debtor in violating the rights of the secured party.

Citing a policy enhancing "the free flow of funds" the provision does not require the transferee to be without knowledge, to give value, or even to satisfy a reliance requirement. Only a transferee acting in collusion with the debtor is deprived of the protection, which is not conferred on the debtor attempting to move funds from one account to another.[119] Rather, the provision affords protection exclusively to a 'non-colluding' third-party transferee, namely a 'non-colluding' payee,[120] of funds out of the deposit account.[121]

[115] See text, supra, around nn. 104-105.

[116] Official Comment 4 to Section 9-327.

[117] Per UCC Section 9-104(a)(3). See text, supra, at nn. 104-115.

[118] Official Comment 2 to UCC Section 9-332.

[119] For these points see Official Comments 2-3 to UCC Section 9-332. The quote is from Official Comment 3.

[120] Strictly speaking, a funds transfer is not a transfer. Rather, it is the extinction (or reduction in the amount of) of a debt owed to one person and its replacement by (or increase in the amount of) another debt owed to another person. A leading modern case to that effect is Libyan Arab Foreign Bank *vs*. Banker's Trust Co, 1988, 1 Lloyd's Rep 259, at 273 (QB), specifically rejecting "dicta in one American case" to the contrary, apparently from Delbrueck *vs*. Manufacturers Hanover Trust Co, 609 F 2d 1047, at 1051 (2nd Cir. 1979).

[121] "Bad actors" and "transferee who does not take free" are respectively discussed in Official Comments 4 and 5 to UCC Section 9-332.

Since control trumps all other modes of perfection, control would have defeated perfection by registration. This would have been so regardless of the knowledge of the competing registration by the secured party taking control. Such would have been the case had there been perfection by registration for a deposit account as original collateral. This would be consistent with the principle that unless stated otherwise for a specific rule,[122] knowledge does not play a role in the priority scheme under article 9.[123] For sure then, a secured party taking control of a bank deposit beats an earlier unperfected security interest in the deposit account, regardless of knowledge. However, where funds deposited in a deposit account subject to control, are impressed with trust, a security interest, or otherwise an adverse claim, the analysis differs. Certainly, the secured party assuming control will defeat a security interest in the funds that was created under a security agreement authorizing the debtor to dispose of them free of the security interest.[124] Otherwise, the secured party assuming control may be protected, at least as against a holder of a security interest in the funds, as a non-colluding transferee of funds under UCC Section 9-332(b). As against another adverse claim, protection is under general principles of law, arguably in circumstances requiring lack of knowledge.[125]

Nonetheless, "the free flow of funds through the payment system"[126] purports also to underlie the rule provided for in UCC Section 9-341. Thereunder, in principle, "a bank's rights and duties with respect to a deposit account maintained with the bank" are "unaffected by the creation or perfection of a security interest or by the bank's knowledge[127] of the security interest".

This general rule of UCC Section 9-341 is stated in the Section to be subject to two exceptions:

[122] See e.g. UCC Sections 9-317(b), buyer receiving delivery, and 9-323(b)(1) (in connection with future advances).

[123] See e.g. UCC Section 9-322 (Residual priorities rule).

[124] For the disposition of collateral free of the security interest, see UCC Section 9-315(a)(1).

[125] See e.g. Greenwood Teale *(T & H) v* William *Williams, Brown & Co* (1894), 11 TLR 56.

[126] Official Comment 2 to UCC Section 9-341.

[127] Official Comment 2, *idem*, acknowledges UCC Section 4-303(a) dealing with the time notice to the bank concerning a competing interest becomes effective. However, the Official Comment goes on to provide that UCC Section 4-303(a) "does not determine whether a timely notice is otherwise effective" and thus does not provide for the effectiveness of knowledge in circumstances governed by UCC Section 9-341. Rather, UCC Section 4-303(a) deals with the ineffectiveness of notice received after the bank acted to the contrary. It ought not necessarily to be read as providing for its effectiveness prior to that.

1. The first exception relates to circumstances governed by UCC Section 9-340(c), under which the exercise by the bank of a set-off against a deposit account is ineffective against a secured party who is the account holder. Such is the case (in which the bank's right of set-off against the debtor is defeated) where the secured party obtained control of the deposit account by becoming "the bank's customer with respect to the deposit account" under UCC Section 9-104(a)(3).[128]

2. The second exception pointed out in UCC Section 9-341 is where "the bank otherwise agrees in an authenticated record".

Only in both such cases the rights of the bank in which the deposit account is maintained are affected by the creation, perfection or knowledge of a security interest as well as instructions given to it by the secured party. Otherwise, under Official Comment 3 to UCC Section 9-341, until the bank is served with judicial process, or until it receives instructions with respect to the fund on deposit from a secured party in control, the bank is entitled to follow the debtor-customer's payment instructions.

According to Official Comment 2 to UCC Section 9-341, this means that the bank may "ignore the instructions of the secured party unless it had agreed to honor them or unless other law provides to the contrary". However, this language goes beyond a restatement of the two exceptions premised on the agreement of the bank; rather, it adds a third exception to the general rule of UCC Section 9-341, that of "another law provid(ing) to the contrary". This third exception is elaborated by Official Comment 4 to UCC Section 9-341, effectively explaining that lack of termination, suspension or modification of a bank's rights by the creation, knowledge, or receipt of instructions with respect to a security interest in a deposit account, is only so far as article 9 is concerned. At the same time, Official Comment 4 explains, possibly depending at least in part on whether the secured party has control and on the manner in which it was achieved, "whether a bank that pays out funds from an encumbered deposit is liable to the holder of the security interest" may be determined according to a rule derived from a non-uniform state law. Such a rule, "[o]ften… found in a non-UCC adverse claim statute", "applies generally when a bank pays out funds in which a third party has an interest".

I am perplexed by this third exception, that of another "law provid(ing) to the contrary", per Official Comment 2. In elaborating on this exception, Official Comment 4 refers to "a non-UCC adverse claim statute" and to the scope and contents of a control agreement. The rule is, however,

[128] See text, supra, at nn. 104 and 105.

possibly narrowed down by Official Comment 3, insofar as it requires the service of judicial process. Yet, as an alternative, without the further elaboration of the scope and contents of the exception as in Official Comment 4, Official Comment 3 points at the receipt of instructions from a secured party in control, as something that precludes the bank from complying with the account holder's instructions.

Indeed, that the scope of this third exception is not adequately clear. Furthermore, whatever its scope, the exception is not mentioned in UCC Section 9-341. For sure, rules governing the position of a bank in which a deposit account is maintained and which is advised of a third-party's adverse claim to the deposit account exist outside article 9. Thus, under the common law, generally speaking, a bank with knowledge of an adverse claim has lost its right to set-off the amount reflecting the claim against a debt due from the customer to the bank.[129] However, according to "a growing number of jurisdictions" in the United States, the bank is precluded from exercising its set-off right even when the bank acts without knowledge of an adverse claim by a secured party as long as the bank did not suffer a detrimental loss.[130] As well, under the common law, the bank is released from its duty to comply with payment instructions given by the customer/account holder to pay out of the deposit account, where these instructions conflict with the claim to the funds by the adverse claimant, who could be a secured party, who instructs the bank to either freeze the account, or transfer funds to him or her. Rather, the bank should file an interpleader action, or give a reasonable time to the adverse claimant to file his or her claim. In most jurisdictions in the United States, an 'adverse claim' statute gives the bank further protection by allowing it to ignore the adverse claim in two situations. The first one is where the bank has not been served with a court order restraining it from complying with its customer instructions. The second situation is where the bank accepted from the adverse claimant what the bank considers to be an adequate indemnity against liability to the customer.[131]

[129] See, supra, n. 126.

[130] John TeSelle, supra n. 60 at 44 and 45. See also Stephen L Sepinuck, "The Problems with Setoff: A Proposed Legislative Solution" (1988), 30 Wm & Mary L Rev 51 at 73. An earlier, exposition is by Robert H Skilton, "The Secured party's Rights in a Debtor's Bank Account Under article 9 of the Uniform Commercial Code", 1977, 2 S Ill U LJ 120 at 190-207.

[131] For a succinct discussion of adverse claims to a deposit account – both under the common law and adverse claims statutes, see e. g. B. Clarke, Barkley and Barbara, *The Law of Bank Deposits*, *Collections and Credit Cards*, Volume I, Revised Edition, Arlington, Va. Pratt, Updated through December, 1999, at 3.09.

Certainly, upon the default of the customer-account holder on the security agreement, the secured party, as an adverse claimant, may pursue the issuance of a restraining order against the bank. UCC Section 9-341 ought not to be read as precluding this, even in the absence of an agreement between the bank and the secured party. In fact, I would have read UCC Section 9-341 to be a uniform 'adverse claim statute' on its own so as to displace and supersede any non-uniform state law, whether or not embodied in an 'adverse claim statute'.[132] Hence I find the reference to "another law provid(ing) to the contrary", per Official Comment 2, as elaborated by Official Comment 4 by reference to non-article 9 law, to be perplexing.

In any event, other than in the unusual case where the bank in which the deposit account is maintained breaks its agreement to comply with a secured party's instructions, the power of a secured party to seek the issuance of a restraining order against that bank is relevant only in limited circumstances. This power may be used by a holder of a security interest that is junior to a security interest perfected:

i. by a secured party becoming a customer,

ii. by a secured party entitled under the control agreement with the bank to direct payments out of the deposit account of the customer (being the secured party's debtor), or

iii. by the bank maintaining the deposit account.

Circumstances where such a power is to be invoked are likely to arise only infrequently; this is so since perfection of a security interest in a deposit account can be accomplished only by means of control,[133] which in turn, requires the consent of the bank maintaining the deposit account.[134] A prudent bank is likely to have the conditions for complying with the secured party's instructions specifically stated in the agreement with the secured party. A dispute among competing secured parties in control, in which resort to the issuance of a restraining order may also be made, is therefore equally likely to be rare. It is thus particularly a holder of an unperfected security interest, who may resort to the issuance of a restraining order, usually with no real benefit, due to the junior position of the security interest.[135]

[132] Cf. UCC Section 1-103(b), addressing the possible displacement "by the particular provisions" of the UCC of contrary "principles of law and equity.."..

[133] UCC Section 9-312(b)(1). See text, supra, & nn. 97-99 and 111.

[134] UCC Section 9-104(a). See text, supra, at nn. 101-105.

[135] For the junior position of an unperfected security interest in relation to a perfected one and a 'lien creditor' (defined in UCC Section 9-102(a)(52) to include an enforcing judgment creditor and a trustee in bankruptcy), see respectively, sections 9-322(a)(2) and 9-317(a)(2)(A).

IV. Recoupment and set-off

"Security interest" in a "deposit account" governed by article 9 is to be distinguished from "a right of recoupment[136] or set-off". With respect to both these rights, article 9 does not apply, other than in two cases. The one relevant for our purposes, discussed immediately below, is "with respect to the effectiveness of rights of recoupment or set-off against deposit accounts" governed by UCC Section 9-340.[137]

UCC Section 9-340 resolves the conflict between a security interest in a deposit account and the rights of recoupment and set-off of the bank maintaining the deposit account. It contains two rules, each applicable other than where the deposit account is in the name of the secured party.

First, subsection (a) states, "a bank with which a deposit account is maintained may exercise any right of recoupment or set-off against a secured party that holds a security interest in the deposit account". This means that in case of a contest between the bank maintaining the deposit account and a secured party, priority is conferred on the bank's right of recoupment or set-off; the secured party takes the deposit subject to the rights of the bank. At least for recoupment, this is quite logical; as collateral, the deposit

[136] 'Recoupment' is American law term meaning the right of a defendant in a lawsuit to demand deduction from the amount awarded to plaintiff of a sum due the defendant from the plaintiff in the transaction which was the subject of the lawsuit. See e. g. Black's Law Dictionary s. v. "recoupment" and s. v. "equitable recoupment". It roughly covers 'abatement' and 'equitable set-off' in Anglo-Canadian law. In the common law, under the doctrine of abatement, damages resulting in the diminution of the value of the subject matter may be "set up" as a defence, and not as a matter of set-off, against an action for the payment of the value of that subject matter. See Smith, Marcus, *The Law of Assignment: The Creation and Transfer of Choses in Action*, Oxford, OUP, 2007, at 13.89. For equitable set-off see, supra, n. 64. Common law abatement and equitable set-off are compared in Cam-Net Communications *vs*. Vancouver Telephone Co, 1999, 182 DLR (4th) 436 at para 33 (BCCA) as follows: The law recognizes a distinction between what may be termed abatement and equitable set-off. The former, a product of the common law, applies to cases in which a defendant can show that as a result of the plaintiff's breach, the goods, services, or work provided by the plaintiff are diminished in value. The latter, a product of equity, refers to cases in which a defendant raises a cross-claim which goes directly to impeach the plaintiff's demands, i. e., which is so closely connected with the plaintiff's claim that it would be unjust to allow the plaintiff to enforce payment without taking into account the cross-claim. The latter involves damages other than a diminution of the value of the goods or services provided.

[137] See UCC Section 9-109(d)(10). The other exception is "with respect to defenses or claims of an account debtor", under Section 9-404 which is effectively to the same effect as to the rights of an assignee vis-à-vis an account debtor, except that it does not apply to a party liable on a 'deposit account', which under article 9 is neither 'account' nor 'general intangible' on which an 'account debtor', whose rights are governed by Section 9-404, is obligated. See UCC Section 9-102(a)(2), (3) (29) and (42).

account is the customer's right against the bank, so that the size of the amount claimed by the customer under the right is reduced by the size of the amount claimed under the bank's recoupment right. No special provision to that effect exists in personal property security legislation in Canada. This is so because the point is covered by OPPSA Section 40(1.1)[138] providing in general for the account debtor's right to assert against an assignee defences available to the account debtor against the assignor/creditor.[139] The UCC has such a general provision[140] but nevertheless a special provision is required, because unlike under personal property legislation in Canada, the bank deposit is not an 'account;' hence, the general provision applicable to the rights of an account debtor does not apply to a bank owing on a bank deposit.[141]

However, the priority under UCC Section 9-340(a) of the bank exercising a set-off by combining account over a third-party secured party may not be justified, at least as a universal principle applicable under all circumstances. It may go too far when the security agreement was made with the consent of the bank. More generally, priority of set-off over the third-party secured party's adverse claim appears to undermine the mutuality required for a set-off.[142] I suppose then that the provision ought not to be read literally. Stated otherwise, the provision ought not to be read as overriding the inherent or built-in limitations to the right of set-off. Indeed, it is recognized that UCC Section 9-340 purports to deal with "rights of set-off and recoupment that a bank may have under other law" and "does not create" such rights; "nor is it intended to override any limitations or restrictions that other law imposes on the exercise of those rights".[143] Rather, as pointed out, it deals with the priority to the funds on deposit between such rights and those of the secured party. At the same time, suffice it to say then that UCC Section 9-340(a) would have benefited from some refinement.

[138] As well as by parallel provisions elsewhere in Canada.

[139] See text, supra, at nn. 52-58. Note that in this framework the bank is the account debtor, the secured party is the assignee, and the customer is the assignor/creditor.

[140] UCC Section 9-404 (restating the earlier UCC 9-318-1) as pointed out, supra, in text and n. 57.

[141] In contrast to Canada, (see text, supra, and n. 21) "Deposit account" is specifically excluded from the definition of "account" in UCC Section 9-102(a)(2).

[142] Mutuality is premised on the principle that "the claim and cross-claim must be between the same parties in the same right", *Goode on Legal Problems of Credit and Security*, Louise Gullifer (ed), 4th ed., London, Sweet & Maxwell, 2008, at 331, so that "one's man money shall not be applied to pay another man's debt", Jones *vs*. Mossop, 3 Hare 568, 1844, at 574, 67 ER 506.

[143] Official Comment 2 to UCC Section 9-340.

The second rule of UCC Section 9-340 is contained in subsection (b). Thereunder, "a right of recoupment or set-off of the secured party as to a deposit account maintained with the secured party" is not affected by "the application of [UCC article 9] to a security interest in a deposit account". According to Official Comment 3 to Section 9-340, this means that a bank "may hold both a right of set-off against, and an article 9 security interest in, the same deposit account". Furthermore, "[b]y holding a security interest in a deposit account, a bank does not impair any rights of set-off it would otherwise enjoy". Stated otherwise, in the hands of the bank in which the deposit account in maintained, set-off and security interests may overlap; one does not exclude the other, and each is available to the bank at its pleasure.

However, as indicated,[144] these two rules do not apply where the secured party obtained control of the deposit account by becoming "the bank's customer with respect to the deposit account" under UCC Section 9-104(3).[145] According to Section 9-340(c), against a secured party holding a security interest perfected by control by becoming the bank's customer under Section 9-104(a)(3), the bank may not exercise a set-off right "based on a claim against the debtor". However, Comment 2 proceeds to state that consistently "with the priority rule in Section 9-327(4)", under which a secured party customer under UCC Section 9-104(3), "has priority over a security interest held by the bank with which the deposit account is maintained",[146] even in this situation, that of a secured-party customer with perfection under Section 9-104(3), the bank may "exercise its recoupment rights effectively". This Comment merely clarifies the language of UCC Section 9-340(c) which precludes only the availability of set-off, and not recoupment, against a secured party-customer with perfection under Section 9-104(3).

The result is that, contrary to a set-off, a recoupment right available to a bank against its customer may be exercised by the bank even against funds belonging to the customer, securing the customer's obligation to a secured party, and held in the bank in a deposit account in the name of the secured party. The secured party-account holder[147] will not benefit from Section 9-332(b), and will not defeat the maintaining deposit account bank's recoupment right based on a claim against the customer (the secured party's debtor). As "A transferee of funds from a deposit account" of the customer/

[144] See text, supra, that follows n. 138.

[145] See text, supra, at nn. 104 and 105.

[146] The priority rule under UCC Section 9-327(4) is set out in text, supra, that is at n.113.

[147] In fact, both the debtor and secured party are customers and account holders with the bank. In this paragraph for convenience and ease of identification, the debtor is refereed to as customer and the secured party as the account holder.

debtor, the secured party-account holder acting without collusion with the customer-debtor may purport to take "the funds free of a *security interest* in the deposit account…",[148] and yet not of a *recoupment* right by the bank where the deposit is maintained.

IV. Conclusion

As the law under personal property security legislation in Canada stands now, a taker of cash collateral does not enjoy automatic priority. Rather, to secure priority, the taker has to seek subordination agreements.[149] Otherwise, the taker's claim to the 'cash' deposited in the debtor's account will be defeated by a competing secured party's claim to that account covered by an earlier registration.[150] This is so even if the debtor's account was specifically opened for the deposit of the cash collateral.[151] To a similar end, a deposit of cash collateral to the taker's own account is a transaction intended to secure the debtor's obligation to the taker of the cash collateral. As such it is covered by the OPPSA.[152] This means that the taker's claim to the cash collateral deposited to the taker's account may be defeated by a security interest covered by earlier registration against the debtor. In either case, where a purchase-money security interest was timely registered, a claim tracing its proceeds will defeat the security interest in the cash collateral.[153]

Regardless, there is uncertainty in connection with the priority scheme among competing claims to a deposit account. A key point of contention is the characterization of the bank's right to combine accounts.[154] As a matter of agreement, albeit implied by law, between the bank and the customer, the most appropriate treatment may be that of a legal or independent set-off. However, this characterization does not suit the bank in its endeavour to achieve maximum protection with the view of facilitating the objective of the right. This objective is to the mutual benefit of the bank and the customer, in the form of credit extension by the bank to the customer. Such credit is either in the form of fresh new value, or the deferral of collection

[148] See text, supra, that follows n. 119. Emphasis added.

[149] As provided by OPPSA Section 38.

[150] See text, supra, n. 29.

[151] In which case it may nevertheless fall under an after-acquired property clause (permitted under OPPSA Section 12) of the security agreement of the earlier registrant.

[152] For the scope of the OPPSA, see in general text, supra, at nn.13-17.

[153] See text, supra, nn. 46-49.

[154] See text, supra, nn. 65-70.

of an existing debt. As well, in light of the lack of clarity in connection with the bank's right to combine accounts, third parties cannot find certainty in taking an effective security interest in bank accounts. For the deposit holding bank the taking of a security interest is an available option; yet relying on this option is a blessing in disguise for both the deposit holding bank and potential searchers in the Registrar under personal property security legislation. This is so as long as perfection requires registration which effectively means the inundation of the Registration system with financing statements by banks taking security interests in accounts held with them. Searches aimed at finding competing registrations may be lengthy and costly. Finally, reliance on contractual set-off may not take the deposit holding bank any further as long as the set-off contract may be construed to be a security agreement.

Under UCC article 9, in *Caisse populaire Desjardins de l'Est de Drummond v Canada*,[155] the bank would have had a security interest in the deposit account perfected by control and would also have been able to effectively exercise its right of set-off over the positive balance in that account. Regardless, a statutory treatment of security interests in bank deposits inspired by UCC article 9 is a good model to go forward in Canada. Particularly attractive is the mode of perfection by 'control' and the fundamentals of the resulting priority scheme. The secrecy counter-argument can be met by the fact that secrecy underlies the way bank accounts are handled anyway as well as by the existing precedent of the perfection and priorities in relation to security entitlements deposited in securities accounts.[156]

This is not to say that every detail of the article 9 scheme in relation to deposit account merits a slavish adoption. For sure, I do not think that introducing perfection by control ought to lead to the exclusion of perfection by registration or filing as it is now the situation in the United States.[157] As well, issues to be thought through include priorities in "identifiable or traceable" proceeds deposited to a deposit account, which is original collateral for a secured party.[158] A clearer scheme is required to cover the knowledge by the bank in which the deposit account is held of a security interest and

[155] Supra, n. 24.

[156] According to OPPSA Sections 19.1(1), 22.1(1), and 1(2), by reference to the Securities Transfers Act, SO 2006, Chapter 8 ("OSTA"), Sections 25 and 26. See also definitions of "security entitlement" and "securities account" (as well as "financial asset") in OSTA Section 1(1).

[157] See text, supra, nn. 98 and 99.

[158] For the perfection and priority of a security interest in "identifiable or traceable" proceeds placed in a deposit account, see, supra, nn. 77-78, 97, 112 and 117-118.

the standard of proof required for having the bank's rights with respect to it "affected".[159] Such a scheme ought specifically to address restraining orders, interpleaders, and the inquiry obligations of a bank.[160] Also, the effect of a security agreement between the customer and a third-party, to which the bank has not consented, ought to be dealt with more clearly and directly.[161] As well, the availability of recoupment,[162] or its Canadian equivalents, namely, the abatement and equitable set-off,[163] against a secured party in whose name the deposit account is held,[164] requires a re-examination. Finally, the range of circumstances in which the bank's right of set-off prevails over that of a third party-secured party ought to be re-examined.[165]

In the final analysis, it is the perfection by 'control' and the priority given to it that ought to guide law reform in Canada. Specific details of the revised UCC scheme ought to be seriously considered and either followed or rejected on an issue-by-issue basis.[166]

[159] UCC Section 9-341. See text, supra, that follows n. 127.

[160] See text, supra, n. 132. Cf. the difference between the (higher) standard of knowledge of fraud required by a bank in order not to dishonour a letter of credit and the (lower) standard of proof required by a court for issuing an interlocutory injunction requiring a bank not to honour the letter of credit. BNS *vs*. Angelica Whitewear Ltd., 36 DLR (4th) 161 (SCC), 1987.

[161] See text, supra, nn. 127-136.

[162] See text, supra, n. 137.

[163] See supra, nn. 64 and 137.

[164] See text, supra, nn. 148 and 149.

[165] See text, supra, nn. 139-144.

[166] Official Comment 16 to UCC Section 9-109 points at the 'control' requirement, together with the designation of the "deposit account" as a separate category of collateral, as examples to the "several safeguards" contained in article 9 designed "to protect debtors against inadvertently encumbering deposit accounts and to reduce the likelihood that a secured party will realize a windfall from a debtor's deposit account".

LA EVOLUCIÓN DEL SISTEMA ECONÓMICO GLOBLAL EN LOS ÚLTIMOS 30 AÑOS

Leonardo Lomelí Vanegas

Los últimos treinta años de la evolución del sistema económico internacional se han caracterizado por la acelerada intensificación del proceso de globalización, que ha rebasado la capacidad de los organismos internacionales y los mecanismos multilaterales para hacer frente a la creciente inestabilidad económica y financiera. La más reciente crisis económica, que dista mucho de haber sido superada como lo demuestra el bajo crecimiento económico global de los últimos dos años y la crisis que afecta a varias economías de la Unión Europea, hizo evidente la necesidad de revisar las instituciones económicas internacionales y de alcanzar una mejor coordinación entre los estados nacionales para reducir los riesgos sistémicos y gobernar la globalización.

Durante la crisis económica internacional de 2008-2009 comenzaron se publicaron libros y artículos de varios economistas destacados que analizaban las semejanzas y diferencias con respecto a la otra gran crisis anterior, la depresión de los años treinta. Las diferencias son muchas: el número de países independientes en la actualidad en contraste con un mundo en el que aún persistían los grandes imperios coloniales europeos, sobre todo el inglés y el francés; el gran avance tecnológico en materia de comunicaciones y transportes que favorece una mayor interdependencia económica y tecnológica; y sobre todo, la intensificación de la globalización económica, que hoy se traduce en economías nacionales mucho más abiertas y dependientes de sus relaciones con el exterior que hace ocho décadas. Pero las semejanzas son escalofriantes: la restauración de una ortodoxia económica que a pesar de los avances de la economía como disciplina, en términos generales se basa en las mismas ideas que predominaban antes de la gran depresión. Y de manera relevante, una concentración del ingreso en las principales economías desarrolladas y a nivel mundial muy similar a la que existía antes de la crisis, después de un período de redistribución del ingreso que estuvo asociado a la construcción de los estados de bienestar en los países desarro-

llados y de sistemas segmentados de protección social en el resto del mundo, pero que comenzó a revertirse a partir de las reformas de mercado promovidas a partir de los años ochenta.

La evolución reciente del actual sistema económico internacional tiene como su antecedente directo el final de la larga expansión económica de la segunda posguerra, que desembocó en las perturbaciones económicas de los años setenta del siglo XX. La crisis del sistema monetario y financiero internacional diseñado en Bretton Woods, los choques petroleros de esa década asociados a la creación de la OPEP y a la revolución islámica en Irán y la aparición de fenómenos de estancamiento con inflación, asociados al peligroso incremento de los déficit gemelos (el del gobierno y el del sector externo) en varios países desarrollados, en particular en Estados Unidos, desembocó en una profunda revisión de las políticas económicas que se habían seguido a partir del final de la Segunda Guerra Mundial.

Las críticas al keynesianismo que había inspirado las políticas económicas durante las tres décadas de crecimiento económico que siguieron a la segunda gran guerra habían existido desde el principio, pero adquirieron notoriedad e influencia en los años setenta. El aumento de la intervención del Estado en la economía y el crecimiento del sector público fueron señalados como la causa principal de los problemas económicos que estaba enfrentando el mundo. Primero en el Reino Unido y después en los Estados Unidos llegar al poder gobiernos que adoptaron estas críticas como elemento fundamental de sus plataformas electorales y las tradujeron después en políticas económicas. Los gobiernos de Margaret Thatcher y Ronaldo Reagan impulsaron una importante ofensiva contra la intervención estatal y a favor de la reducción de los impuestos (sobre todo a los ricos y a las empresas) y de la desregulación de los mercados. Los organismos financieros internacionales hicieron suya esta agenda e impulsaron reformas en esta dirección a partir de las décadas siguientes, promoviendo un cambio estructural en dos direcciones: reducción de la intervención estatal en la economía, eliminación de las restricciones al libre comercio, al flujo de capitales y desregulación financiera. La apuesta era lograr una asignación más eficiente de los recursos a través del mercado, que propiciara un mejor funcionamiento de la economía que permitiera, entre otras cosas, aumentar el crecimiento.

Menos Estado y más mercado fue la tesis principal que enarbolaron los defensores de reformas que tenían como propósito elevar la eficiencia económica y la competitividad en cada país, pero que también requerían de cambios globales que propiciaran una mayor interdependencia económica internacional. Aunque no se llevó a cambio una reforma integral de las principales instituciones financieras multilaterales (el Fondo Monetario

Internacional y el Banco Mundial) se impulsó la transformación del Acuerdo General sobre Aranceles y Comercio (el GATT) que dio lugar a la Organización Mundial de Comercio. Se intensificaron también las rondas de negociación entre los países miembros para avanzar en la liberalización del comercio internacional. Los resultados obtenidos fueron sido muy desiguales, poniendo de manifiesto el doble discurso de los países desarrollados, que piden a los demás que abran sus mercados pero se niegan a reducir la protección de la que gozan sus productores agropecuarios.

El desplome del socialismo real en Europa del este al final de los años ochenta y la desintegración de la Unión Soviética al principio de la década siguiente fueron acontecimientos que reforzaron la confianza en la economía de mercado y aceleraron la globalización. En el plano ideológico, el capitalismo salió victorioso al quedarse sin un sistema económico alternativo. En los ámbitos geopolítico y económico, los países donde se desplomó el socialismo real se incorporaron de lleno a los mercados de bienes y capitales, convirtiéndose en destinos muy atractivos para la inversión extranjera. Incluso los países que formalmente siguieron siendo socialistas, desde China hasta Cuba, introdujeron reformas para liberalizar algunos mercados. En el caso particular del gigante asiático, su progresiva incorporación a los flujos mundiales de comercio e inversión constituyó uno de los procesos más importantes de cuantos tuvieron lugar en las últimas tres décadas, hasta el punto de convertirse en una gran potencia económica global, solo superada en producto interno bruto como país por los Estados Unidos de América.

En la última década del siglo XX alcanzó su clímax la confianza en los mercados autorregulados y en las bondades de la globalización. Las ideas que habían impulsado y justificado las reformas promovidas desde la década anterior para reducir los controles gubernamentales sobre la actividad económica y la privatización de empresas públicas fueron resumidas en el llamado Consenso de Washington, en el cual podemos encontrar un conjunto de medidas encaminadas a mejorar la eficiente asignación de los recursos por la vía de la eliminación de los obstáculos al funcionamiento de los mercados. Apertura comercial, reducción de restricciones a la inversión extranjera y al libre flujo de capitales, desregulación financiera, política monetaria basada en objetivos de inflación, reducción de impuestos al capital y flexibilización de los mercados de trabajo, son algunas de las medidas que recomienda el Consenso que toma su nombre de la capital estadounidense ya que en ella tienen su sede el Fondo Monetario Internacional, el Banco Mundial y el gobierno de los Estados Unidos, promotor de este Consenso aunque rara vez aplique al pie de la letra sus recomendaciones.

Paradójicamente, el Consenso de Washington repetía en su mayoría los preceptos en los que se había basado el funcionamiento del sistema económico siete décadas antes, en los dorados años veinte, justo antes de que se produjera el crack bursátil de 1929 al que siguió la gran depresión de los años treinta. La crisis de aquellos años puso en evidencia la necesidad de la intervención estatal para regular los mercados, promover el pleno empleo y garantizar la provisión de un conjunto de bienes públicos y servicios sociales necesarios para el buen funcionamiento del sistema económico, para su estabilidad política y para la regulación de los conflictos sociales. El aumento de la participación del Estado en la economía se complementó con la ampliación y el perfeccionamiento de los sistemas de protección social que se habían comenzado a construir en algunos países, en una primera etapa vinculados directamente al empleo formal, pero que después serían ampliados al conjunto de la población por aquellos estados que lograron llevar a cabo el esfuerzo fiscal que requería este objetivo.

La utilización de las políticas monetaria y fiscal como instrumentos para estimular la actividad económica y regular el ciclo fue en gran medida un factor clave para permitir la larga expansión de la posguerra. Los cambios promovidos a partir de la década de los ochenta y que permitieron intensificar el proceso de globalización, también tuvieron como elemento relevante cambios significativos en la política económica. Se trató de estimular a la inversión a través de la disminución de impuestos; los regímenes de tipo de cambio fijo fueron abandonados a favor de sistemas de flotación controlada con bandas cambiarias o de libre flotación; en algunos países, entre ellos México, se impuso como único objetivo de la política monetaria el control de la inflación, en contraste con otros países, como Estados Unidos, en donde el banco central tiene un mandato dual, ciertamente no fácil de administrar, para procurar crecimiento económico con estabilidad de precios.

En el ámbito de la macroeconomía, las posiciones que cuestionan la eficacia de la política económica para influir en las variables reales de la economía (la producción y el empleo, principalmente) fueron cuestionadas. El ascenso del monetarismo primero y posteriormente de aquellas corrientes que parten del supuesto de que los individuos son tan racionales al tomar decisiones económicas y evaluar el contexto y las tendencias, que anulan la eficacia de cualquier política económica encaminada a promover el crecimiento y el empleo, fueron determinantes para que predominaran en los últimos años las posiciones más conservadoras en materia de política económica. La nueva macroeconomía clásica o escuela de las expectativas racionales es probablemente el mejor ejemplo de estas tendencias y ha ejercido una influencia perdurable en el diseño y la ejecución de la política económica.

La intensificación de la apertura comercial en la mayor parte de los países y el sorprendente vuelco hacia la economía mundial de economías que habían estado altamente protegidas durante el período de expansión económica previo, sobre todo en Asia y en América Latina, permitió profundizar la división internacional del trabajo, una de las bondades del libre comercio que siempre habían destacado sus defensores. Los flujos de inversión, la tecnología y la desregulación del comercio internacional aceleraron la globalización de la producción, profundizando la especialización de países y regiones. Como ha señalado Jeffry Frieden, "*los factores de la producción huían de los de los lugares y usos menos rentables para dirigirse a los más rentables*".[1]

En muchos casos, la mayor rentabilidad se debía al menor costo de la mano de obra. En teoría, la relocalización de la producción debió tener como efecto benéfico un aumento en los salarios en los países a los que migró la producción. En la práctica, las barreras a la libre circulación global de la mano de obra han sido determinantes para que prevalezcan y en algunos casos se acrecienten las enormes brechas salariales entre los países desarrollados y los países en desarrollo, provocando que los trabajadores de los primeros se vean afectados por este proceso de reubicación de la producción industrial y los trabajadores de los países en desarrollo no se hayan visto beneficiados por un aumento en las remuneraciones proporcional a la productividad del trabajo. En ese sentido, la globalización del último cuarto del siglo XX perjudicó a los trabajadores de los sectores industriales tradicionales de los países desarrollados y benefició a sus empresas, mediante una especialización de la producción en las economías emergentes que llevó a descomponer la producción en componentes cada vez más pequeños, fabricados en diferentes países para ser incorporados al producto final en los países con menores costos de mano de obra.

Aunque el crecimiento económico global fue más lento e inestable en las últimas tres décadas que en el período previo de expansión de la segunda posguerra, es innegable que hubo países que se beneficiaron más que otros y que registraron un mejor desempeño económico. Fue claramente el caso de China, como ya se ha señalado, pero también de otras economías emergentes como India, Corea o Brasil, o de las economías de Europa occidental que se integraron en la década de los ochenta a la Unión Europea, como Grecia, Irlanda, España y Portugal, aunque estas últimas enfrentan en la actualidad severos problemas económicos. Lo cierto es que las economías emergentes que más se beneficiaron de la globalización fueron aquellas que supieron

[1] Frieden, Jeffry A., *Capitalismo global: el trasfondo económico de la historia del siglo XX*, Barcelona, Editorial Crítica, 2007, p. 548.

administrar mejor su inserción en la misma, sin aplicar al pie de la letra las recomendaciones del Consenso de Washington. En particular, resultaron más beneficiadas aquellas que aplicaron políticas industriales activas y promovieron una integración más eficiente de sus aparatos productivos. Por el contrario, los países que más se apegaron a dichas recomendaciones, como México, han tenido un desempeño económico menos satisfactorio en el mismo período, por lo que resulta importante insistir en la necesidad de lograr un adecuado equilibrio entre regulación estatal y economía de mercado para poder lograr resultados económicos más satisfactorios.

El crecimiento del comercio internacional estuvo acompañado de un incremento aún mayor de los flujos financieros internacionales. La inversión extranjera directa creció menos que la inversión especulativa, que con su volatilidad provocó o bien amplificó crisis financieras en economías emergentes a partir de los años noventa. Esto se debió en gran medida al crecimiento de los intermediarios financieros no bancarios, desde las casas de bolsa hasta las arrendadoras, financiadoras, aseguradoras y sociedades hipotecarias. Los mercados de derivados tuvieron un crecimiento explosivo en las dos décadas previas al estallido de la crisis de 2008-2009, lo que explica en gran medida la creciente vulnerabilidad de la economía internacional al mismo tiempo que el Consenso de Washington insistía en promover la desregulación financiera como un mecanismo para incrementar el flujo de capitales y con ello, al menos en teoría, estimular el crecimiento económico por la vía de la inversión. Sin embargo, como se ha señalado anteriormente la mayor parte de estos flujos no han consistido en inversión productiva, sino especulativa.

La desregulación financiera promovida por el Consenso de Washington tuvo efectos muy negativos sobre la estabilidad del sistema financiero internacional. La desregulación se dio además al mismo tiempo que el crecimiento y el fortalecimiento del sistema financiero no bancario, que prosperó al amparo de una regulación aún más benigna que la de los bancos, cuando no inexistente. En palabras del Premio Nobel de Economía 2009, Paul Krugman:

A medida que el sistema bancario en la sombra crecía para competir en importancia con la banca convencional, o incluso superarla, los políticos y los funcionarios gubernamentales deberían haber advertido que estaban resucitando la misma vulnerabilidad financiera que había propiciado la gran depresión, y deberían haber decretado una mayor regulación y ampliado la red de seguridad financiera para proteger también a esas nuevas instituciones. Las voces más influyentes deberían haber manifestado algo tan sencillo como que todo aquello que se comporte como un banco, y todo aquello que deba ser rescatado

durante una crisis como se rescataría a un banco, debe estar sujeto a la misma regulación que un banco.[2]

Sin embargo, estas medidas cautelares no se tomaron y fue el crecimiento desproporcionado de los llamados activos tóxicos, en particular aquellas hipotecas difíciles de cobrar, el que propició el inicio de la crisis financiera de 2008 que al igual que en 1929, rápidamente se propagó al sector productivos de la economía. Aún hoy, después de la crisis, las nuevas regulaciones distan mucho de haber eliminado de todo los riesgos sistémicos asociados a este tipo de actividades financieras. Esto se debe a que más allá de los esfuerzos que han realizado los estados nacionales para mejorar la regulación financiera, la casi perfecta movilidad de capitales y la interdependencia de los mercados financieros de la mayor parte del mundo hacen necesaria una nueva y más amplia regulación internacional, que solamente es concebible a partir de una reforma profunda de los organismos financieros internacionales creados en Bretton Woods.

La necesidad de una regulación más estricta del sector financiero también ha enfrentado una fuerte oposición no solo por parte de las empresas que se dedican a estas actividades, sino por aquellos economistas que defienden las bondades de la liberalización de todos los mercados, incluidos los financieros. Los defensores de la desregulación financiera y, en general, del Consenso de Washingron, dejan de lado dos hechos fundamentales: que los beneficios atribuibles al libre mercado como el mecanismo más eficiente de asignación de los recursos solamente se producen en el caso de los mercados competitivos, no en aquellos donde existe competencia imperfecta, y que los seres humanos no actuamos de acuerdo con el modelo de elección racional en el que se basa la economía neoclásica. George Akerlof, Premio Nobel de Economía 2001, ha insistido en la importancia de los *animal spirits*, formas de comportamiento irracional a las que ya se había referido John Maynard Keynes y que explican las actitudes que están detrás de los auges y las crisis financieras, muchas veces con independencia del comportamiento del resto de las variables económicas:

*Existe una razón fundamental para que discrepe*mos —sostiene Akerlof— *de los que opinan que la economía debería ser un espacio desregulado libre para todos (free for all), que el mejor gobierno es el gobierno mínimo y jugar el papel más mínimo en el establecimiento de normas y reglamentaciones. Discrepamos de su visión diferente de la economía. En realidad, si creyéramos que la gente es totalmente racional y actúa solo siguiendo motivos económicos, también creeríamos que el gobierno debería desempeñar un*

[2] Paul Krugman, *El retorno a la economía de la depresión y la crisis actual*, Editorial Crítica, Barcelona, 2009, p. 173.

papel menor en la regulación de los mercados financieros y quizá en la determinación del nivel de demanda global. Pero por el contrario, los espíritus animales tienden a dirigir la economía siguiendo un camino unas veces y otras, otro. Sin la intervención del gobierno, la economía sufrirá oscilaciones masivas que se reflejarán en el desempleo y los mercados financieros seguirán cayendo, de vez en cuando, en el caos.[3]

A pesar de los evidentes desafíos que enfrenta el sistema económico internacional, no parece inminente una reestructuración de las instituciones económicas que permita reducir los riesgos sistémicos y aumentar la capacidad de respuesta global ante la eventualidad de una nueva crisis. Por el contrario, estamos presenciando en la actualidad respuestas locales a problemas globales y falta de coordinación ente las principales economías del mundo, a pesar de que la creación del Grupo de los 20 constituye un gran avance cuyo potencial no ha sido aún plenamente explorado. Hasta ahora, ha faltado acuerdo y voluntad política para tomar medidas que permitan reducir la volatilidad de los mercados financieros internacionales y evitar que los mecanismos de propagación de la crisis puedan conducir a una nueva gran depresión. No obstante, el Grupo de los 20 puede ser el punto de partida para una discusión más amplia sobre la reestructuración del sistema económico internacional, que revise el papel y las atribuciones del Fondo Monetario Internacional, el Banco Mundial, la Organización Mundial de Comercio, los bancos regionales de desarrollo y las agencias de fomento y cooperación económica del Sistema de Naciones Unidas.

Es evidente que la globalización impone mayores restricciones a las políticas económicas de los estados nacionales, de ahí que las estrategias del pasado no puedan ser replicadas tal cual en las actuales circunstancias. Pero también resulta innegable que los estados no pueden renunciar a diseñar y administrar mecanismos globales de supervisión, regulación y coordinación de los mercados, pues una decisión de ese tipo abriría la puerta a un largo período de crecimiento lento e inestable en la economía mundial. A este desafío hay que añadir el que nos plantea el que se deriva de las consecuencias del cambio climático actualmente en curso. En ausencia de mecanismos de coordinación efectivos para reducir las emisiones de gases invernadero a escala planetaria y transitar hacia patrones de crecimiento más sustentables desde la perspectiva ambiental, el horizonte de nuestra civilización se acotará dramáticamente y pondremos en peligro la viabilidad de la vida en el planeta, por lo menos tal como la conocemos. Por si fuera poco, tenemos pendiente en todos los países, pero por supuesto más aún en aquellos menos

[3] Akerlof, George y Shiller, Robert J., *Animal spirits: cómo influye la psicología humana en la economía*, Barcelona, Ediciones Gestión, 2009, p. 285.

desarrollados, una agenda social que permita eliminar la pobreza y reducir la desigualdad. Es necesaria una nueva institucionalidad internacional, adecuada a las nuevas realidades de una economía más globalizada e interdependiente pero con viejos y nuevos rezagos sociales y un formidable desafío ambiental, y entre más nos tardemos en construirla, mayores serán los costos que habremos de pagar en términos de estabilidad global, crecimiento económico y bienestar social.

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COMMENTARIES ABOUT THE UNITED NATIONS CONVENTION ON USE OF ELECTRONIC COMMUNICATIONS IN INTERNATIONAL CONTRACTS

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I. INTRODUCTION

During 38th period of meetings of United Nations Commission on International Trade Law Meeting at Vienna in 2005, approve the United Nations Convention on the Use of Electronics Communications in International Contracts (after the Convention), prepared by the Working Group IV on Electronic Commerce.

The work that I'm going to expose will concern only in a series of commentaries about article 4 in Definitions, article 5 about Interpretation and article 6 in Location of the parties.

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Before the explanation of my work, we must remember the objectives, the director's criteria for the elaboration of this international instrument, which is the convention.

II. Objectives of this convention

The Convention is an international instrument whose fundamental purpose is to facilitate international trade by removing possible legal obstacles or uncertainty concerning the use of electronic communications in connection with the formation or performance of the contracts concluded between parties located in different countries.

The use of electronic means in connection with the formation or performance in contracts may be an important help to development of commerce, but, at the same time, generate problems and juridical uncertainty.

Through United Nations it has been tried to cause juridical safety, which facilitate the development of electronic commerce in an international area, and, at the same time, in a local and national scope. That's the reason by which the Commission has been elaborate texts that we have mentioned before, giving origin to an uniform law about electronic commerce.

It is tried to eliminate uncertainty as far as the effectiveness of electronic communications, through the creation of a juridical instrument directly applicable, which is precisely the Convention that we analyze. It is been hope that principles and rules contain by the UNCITRAL Model Law on Electronic Commerce (UMLEC) and the UNCITRAL Model Law on Electronic Signature (UMLES) form now part of an international juridical text, that has the nature of Objective Law, directly apply for countries to subscribe and ratified this convention.

In synthesis, "*the purpose of the Electronic Communications Convention is to offer practical solutions for issues related to the use of electronic means of communication in connection with international contracts*".[1]

III. Governing criteria in the elaboration of the convention

The first basic criteria consist of which by means the Convention is not intended to establish a set of uniform rules for substantives contractual issues

[1] See A/CN.9/608, para. 3, Explanatory Note of the Secretariat of the Commission on the international text matter of this study.

that are not specially related to the use of electronic communications. The settlement of substantives rules concerning the contracts belong to the local laws of the different countries, with the goal of the Convention having more possibilities of being adopted by a great number of states and Regional Economic Integration Organizations. However, the Convention contains a few substantive rules with the purpose of extends the application of the principle of functional equivalence, where substantive norms are needed in order to ensure the effectiveness of electronic communications.

A notable exception to the maintenance of the first general criteria is constituted by the provisions concerning the offers addressed to non-determined targets through electronic means, that consider simple invitations to make offers, unless it clearly indicates the intention of the party making the proposal to bound in case of acceptance. Another exception to this basic criteria is the validity or enforceability of a contract formed by the interaction of an automated message system and a natural person, or only by the interaction of automated message system.

The second governing criteria it consist in which the Convention is not confined to a determined contract, like the United Nations Sales Convention, but that is formulated norms with a very general character, which they do not imply change, in no country, of the right noun of contracts in general nor of any contract in special. At the terms of the Convention the word "*contract*" should be understood broadly so as to cover any form of legally binding agreement between two parties that is no explicitly or implicitly excluded from the Convention, whether or not the word "contract" is used by the law or the parties to refer to the agreement in question. For instance, the arbitration agreements in electronic form are included into broad sense of word "contract" according to the Convention, even though the Convention on the Recognition and Enforcement of Foreign Arbitral Awards and most national laws do not use the word "contract" to refer them.

The third governing criteria followed in the elaboration of the international instrument that occupies to us, it consisted of returning to take some solutions already given by UNCITRAL respect to the main matters of the electronic commerce and, at the same time, to be filling the emptiness that these had by means of the incorporation of new dispositions, such us the use of automated message systems for contract formation and the error in electronic communications.

SECTION II
GENERAL PROVISIONS

IV. Definitions of concepts in the convention

The article 4, of the international instrument defines the main concepts that form the essential matters of their content.

The article 4 of the Convention is structured on the base of article 2, of the UNCITRAL Model Law on Electronic Commerce, whose basic concept was the one of "*data message*", but in the case of the Convention, assuming the idea of data message, turns around a well formed concept but, that is the one of "*electronic communication*", notion that, by the others serves to give the name to the international text which we analyzed.

First the communication idea is defined, to define but ahead the electronic communication, the one that is constructed on the base of the idea of *data message* removed from the UNCITRAL Model Law on Electronic Commerce (UMLEC), like the others definitions of article 4 of the Convention.

V. Concept of communication

According to the tenor of article 4 in its letter a): "*Communication" means any statement, declaration, demand, notice or request, including an offer and the acceptance of an offer, that the parties are required to make or choose to make in connection with the formation or performance of a contract".*

It can show that it is not a generic concept of communication. The definition of "communication" is intended to make clear that the Convention applies to a wide range of exchanges of information between parties to a contract, whether at the stage of negotiations, during performance or after a contract has been performed, to be coherent with the objective of this international instrument.

VI. The notion of electronic communication

The letter b) of the same article, said that "*Electronic communication means any communication that the parties make by means of data messages*". In consequence, the definition of "electronic communication" establish a link between the purposes of which electronic communication may be used and the notion of "*data message*" contained in the UNCITRAL Model Law

on Electronic Commerce and has been retained in view of the wide range of techniques it encompasses, beyond purely "electronic techniques".[2]

At terms of letter c) of the article 4, of the Convention: "*Data message means information generated, sent, received, or stored by electronic, magnetic, optical or similar means, including, but not limited to, electronic data interchange, electronic mail, telegram, telex or telecopy*". This definition is removed from the literal tenor of the article 2 of UNCITRAL Model Law on Electronic Commerce.

It is possible to be noticed that one is a very ample definition that gets to include until the telegram, as it became in 1996, when the UNCITRAL Model Law on Electronic Commerce was elaborated, although it thought it to have excluded in the Convention of 2005, in the end was considered to maintain it not to introduce uncertainty elements changing the idea that had taken from the alluded to model law.

The definition of "*data message"* is aimed to encompass all class of messages that are generated, stored, or communicated in essentially paperless form. For the effects of the Convention the word "*similar"* connote "functionally equivalent". The reference to "*similar means"* indicates that the international instrument is not intended only for application in the context of existing communications techniques but also to accommodate futures technical developments.[3]

VII. The definitions of originator and addressee

After the definitions of electronic communication, immediately article 4, of the Convention made position defining concepts of "*Originator*" and "*Addressee*" that are basic respect to all electronic communications, and those communications in connection with the formation or performance in international contracts, are the means matters of the Convention.

In general sense we could say that the "originator" is the one that generates the information that is object of the communication. However, the concept of "originator" should cover not only the situation where information is generated and communicated, but also the situation where such information is generated and stored without being communicated.[4] Lastly the definition of originator is intended to eliminate the possibility

[2] See A/CN.9/571.para. 80.

[3] See Explanatory Note of UNCITRAL secretariat for this Convention, para. 92.

[4] See Explanatory note by UNCITRAL Secretariat on the United Nations Convention on the Use of Electronic Communications in International Contracts para. 97.

that a recipient who merely store a data message might be regarded as an originator.

The "*addressee*" is the person to whom the originator intends to communicate by transmitting the electronic communication, as opposed to any person who might receive, forward or copy it in the course of the transmission. The originator is the person who generated the electronic communication even if the communication was transmitted by other person. The definition of "addressee" contrasts with the definition of "originator", wish is no focused on intent.

Under the definitions of "originator" and "addressee" in the Convention, the originator and the addressee of a given electronic communication could be the same person, for instance in the case where the electronic communication was intended for storage by its author.

However, the addressee who store an electronic communication transmitted by someone else is not intended to be covered by the definition of "originator".

The focus of the international instrument that we commented is on the relationship between the originator and the addressee, and not on the relationship between either the originator or the addressee and any intermediary, such as servers or web hosts. The Convention not ignore the role of the intermediaries in receiving, transmitting or storing data message on behalf of the other persons. Nevertheless, the Convention is not conceived as a regulatory instrument for electronic business, it does no deal with the rights and obligations of intermediaries.[5]

To the literal tenor of article 4, letter d) "*Originator of an electronic communication means, a party by whom, or on whose behalf, the electronic communication has been sent or generated prior to storage, if any, but it does not include a party acting as an intermediary with respect to that electronic communication*".

Lastly at literal terms of article 4, letter e): "*Addressee of an electronic communication, means a party who is intended by the originator to receive the electronic communication, but does not include a party acting as an intermediary with respect to that electronic communication*".

VIII. The concept of information system

According to article 4 section f) of the Convention: "*Information system" means a system for generating, sending, receiving, storing or otherwise processing data messages".*

[5] See Explanatory note by UNCITRAL secretariat on the Convention, para. 99, p.39.

The defined concept was extracted of the UMLEC, and it is intended to cover the entire range of technical means used for transmitting, receiving and storing information. The notion of "information system" could refer to a communications network, and in the other instances could be include an electronic mailbox or even a telecopier.

The concept defined by the article 2 letter f), of the UMLEC is different of the idea defined at the Convention, because the UNCITRAL Model Law on Electronic Commerce tour around on the basic idea of "*data message*", whereas the Convention makes respect to the notion of "*electronic communication*".

IX. Definition of automated message system

A newness of the Convention respect to UMLEC, is the introduction of the concept of "*Automated message system*", where this notions is not defined. At the terms of article 4, letter g): "*Automated message system*, *means a computer program or anelectronic or other automated means used to initiate an action or respond to data messages or performances in whole or in part, without review or intervention by a natural person each time an action is initiated or a response is generated by the system*".

This definition facilitates the understanding of the case anticipated in article 12 of the Convention, relative to the use of automated systems in connection with the formation or performance of a contract. The notion of "automated message system" concern essentially to a system for automatic negotiation and conclusion of contracts without intervention of a person, at least on one of the end of the negotiation chain. It differs from "information system in that its primary use is to facilitate exchanges leading to contract formation. An automated message system may be part of an information system, but that need no necessarily be the case.

The essential element in definition of automated message system is the lack of an human actor on one or both sides of a transaction. For instance, if a party orders goods through a website, the contract would be an automated transaction because the vendor took and confirmed the order via its machine. Another case of an automated transaction will be the situation when both parties do the business through Electronic Data Interchange (EDI).

X. Concept of place of business

The definition of "Place of business is very important fort the effects of the anticipated thing in articles: 1, scope of application; 6, location of

the parties; 10, time and place of dispatch and receipt of electronic communications; 17, paragraph 4, participations by Regional Economic Integration Organizations; and 18, effect in domestic territorial units.

At the terms of article 4 letter h) "*Place of business" means any place where a party maintains a non-transitory establishment to pursue an economic activity other than the temporary provision of goods or services out of a specific location".*

This is a concept that emphasizes the space character, that is to say, the physical and geographic location, like thus also the development of a stable, non-transitory economic activity.

The notion "*Place of business*, is a basic concept specially in relation to article 6, of the Convention, that regulates the criteria to determine the location of the parties that communicate through electronic means.

The idea of "*no transitory*" qualifies the word "*establishment*", whereas the words "*other than temporary provision of goods or services*" qualify the nature of the "*economic activity*".

Lastly the definition of "*place of business*" reflects the essential element of the notion on "place of business", as understood in international practice, and "*establishment*", as used in article 2, subparagraph f), of the UNCITRAL Model Law on Cross-Border Insolvency. The definition is not intended to affect other substantives law relating to place of business.

XI. Interpretation of the convention

According to article 5, of the international instrument that we analyzed:

1. *In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.*

2. Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.

Those same norms of interpretation have appeared in most of the UNICITRAL texts, such as Model Laws or International Conventions. Its formulation mirrors article 7 of United Nations Sales Convention.

The provision is aimed at facilitating uniform interpretation of the provisions in uniforms instruments on international commerce law.

It is a practice followed in private law conventions to provide self-contained rules of interpretation for to avoid the use of general rules of public

international law on interpretation of the treaties wish are not suitable for the interpretation of private law provisions.

Good faith is a principle with special relevance in the scope of the electronic communications in connection with the formation or performance in international contracts, for that reason the Convention considers it like the angular stone on which the development of the international trade is sustained, demanding that are guarded by their concrete application. In effect, by fact which in our days it exists a preoccupation by the security in contracts or operations made by electronic means, he is advisable that the principle of the good faith stays next to the credit as essential foundations of the development of the commerce.

Nevertheless, the Convention does not intend to prevent nor to prevent the commission of frauds or crimes in general in the scope of the international trade; it is not either function because this matters belong to the Penal Law.

XII. The matters where are not expressly settled at the Convention

In paragraph 2 of the article 5, Convention alludes not only to its interpretation but of is application. In effect questions concerning matters governed by the instrument which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in absence of such principles, in conformity with the law by virtue of the rules of private international law.

The principle of the good faith had been gathered long ago in the Code of Spanish Commerce, article 57 and in the article 1536, of the Chilean Civil Code, that inspired by the French civil Code of 1804, indicate with identical literal tenor that:

"*Contracts will be formed and fulfilled of good faith, according to the terms in which they are written up*...".

Following this same direction, article 26 of Law 34/2002, 11 of July, on Services of the Society of the Information and of Electronic Commerce, it establishes very textually that:

"*For the determination of the law applicable to electronic contracts one will be to the arranged thing in the norms of the Private International Law of the Spanish legal ordering, having to take in consideration to its application the established thing in articles 2 and 3 from this Law*".

XIII. The location of the parties

The location of a party's place of business is an essential element to determine the scope of application of the Convention, in conformity of article 1. As the purpose of the Convention, the word "parties" includes both natural persons and legal entities. However, a few provisions of the international instrument refer specifically to "natural person", like the case of the location of a natural person who have not place of business.

The international instrument does not contemplate a duty for the parties to indicate their places of business, but establishes a certain number of presumptions and default rules aimed at facilitating a determination of party's location.

According to the article 6: *"For the purpose of this Convention, a party's place of business is presumed to be the location indicated by that party, unless another party demonstrate that the party making the indication does not have a place of business at that location.*

XIV. Nature of presumptions of location

This first presumption is a *iuris tantum* presumption, that can be rebutted by the demonstration of the another party that the party making the indication does not have a place of business at that location. At the terms of the Explanatory note by the UNICITRAL secretariat on the Convention: "The article 6 is not intended to allow parties to invent *fictional places of business* that do not meet the requirements of article 4, subparagraph (h). The presumption, therefore, is not absolute and the Convention does not uphold an indication of a place of business by a party even where such an indication is inaccurate or intentionally false.[6]

In article 6, relative to the location of the parties, the Convention adopts the criterion of a *reallocation of the party's place of business*, in against position of one tried *virtual location* in the "*cyberspace*", derived from the fact that the parties are using electronic communications in connection with the formation or performance in international contracts.

XV. Plurality of places of business

When a party has not indicated a place of business and has more than one place of business, then the place of business for the purposes of the

[6] See A/CN.9/509, para. 47.

Convention it that has the closest relationships to the relevant contract, having regard to the circumstances know to or contemplated by the parties at any time before or at the conclusion of the contract.

Paragraph 2 of article 6 is based on article 10, subparagraph (a) of the United Nations Sales Convention. Nevertheless, unlike that provision, wish refers to place of business that has "*the closest relationship to the contract and its performance*", article 6, paragraph 2 of the Electronic Communications Convention refers only the closest relationship *to the contract*. At the United Nations Sales Convention the cumulative reference to the contract and its performance had given rise to uncertainty, since there might be situation where a given place of business of one of the parties more closely connected to the contract, but another of that party's places of business is more closely connected to the performance of the contract. The Electronic Communications Convention would not generate a duality of regimes in view of their limited scope.[7]

XVI. Place of business of natural persons

However, if the contracting part is a natural person who does not have establishment, for the effects of its location, considers *the place of its residence.*

XVII. Limited value of communications technology and equipment for establishing place of business

At the terms of article 6, paragraph 4, a location is not a place of business merely because that is:

a. *where equipment and technology supporting an information system used by a party in connection with the formation of a contract are located; or*

b. *where the information system may be accessed by other parties*.

Given the circumstance of the use of computers as electronic means in connection with the formation or performance in international contracts, the sole fact that a party use of a domain name or electronic mail address connected to a specific country, does no create a presumption that its place of business is located in that country. However, nothing in the Convention prevents a court of justice or arbitrator from taking into account the assignment of a domain name as a possible element, among others, to determine a party's location, where appropriate.[8]

[7] See A/CN.9/571, para.101.

[8] See: A/CN.9/571, para. 113.

The Law on Services of the Society of the Information and on Electronic Commerce of Spain, uses the same realistic criterion of the place of business or residence in the case of natural person, for the location of the parties, whenever in them the management or direction of the businesses is carried out and also establishes a presumption when an inscription in the Mercantile Registry or another public registry exists, but the situation of technological means by itself does not represent an element sufficient to determine the place of business.

The Explanatory note by UNCITRAL secretariat on the Convention, said that "*the purpose of article 6 is to offer elements that allow the parties to ascertain the location of the places of business of their counterparts, thus facilitating a determination, among other elements, as to the international o domestic character of a transaction and the place of contract formation. As such, this article is one of the central provisions in the Electronic Communications Convention*".[9]

XVIII. Conclusions

The definitions of the concepts that we have analyzed are essential to determine the sense and reaches of the text of the Convention, because they must be understood in the meaning that agree with the objectives and with the principles by which she is inspired.

The jurisdiction of a determined State adopting this Convention, in its interpretation must be regard its international character and to the need to promote uniformity in it application and the observance of the good faith in the international trade.

Concerning the application of the international instrument, matters that are governed by the Convention which they are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in absence of such principles, in accordance with the applicable law by virtue of the rules of private international law.

As far as the location of the parties it seems to us suitable that the Electronic Communications Convention does not contemplate a duty of the parties to disclose their places of business, but establishes a certain number of presumptions and default rules aimed at facilitating a determination of a party's location. A primary importance is attributed to the party's indication of its relevant place of business, unless another party demonstrates that the party who made this indication does not have place of business at this location.

[9] See: Explanatory note by UNCITRAL secretariat for this Convention, para.108.

Moreover those presumptions established into article 6, are one of the central provisions for the scope of application of the Convention in connection with the formation of performance of a contract between parties whose places of business are in different States.

Finally we reiterated that the essential objective of the Convention is to establish uniform rules intended to remove obstacles to the use of electronic communications in international contracts, including obstacles that might result from the operation of existing international trade law instruments, with a view to enhancing legal certainty and commercial predictability.

CLASS ACTIONS IN CANADA – THE CONSUMER'S BEST FRIEND?

Jacob ZIEGEL*

SUMMARY: I. *Introduction*. II. *Class actions to the rescue*? III. *North American Developments*. IV. *Canadian Developments*. V. *Impact of the Legislation*. VI. *Structure of the Legislation*. VII. *The Answer to the Title of this Paper.*

Canada has a federal system of government. In the consumer protection area, jurisdiction is divided between the federal government (located in Ottawa) and the provinces. Canada has ten provinces, with constitutionally entrenched powers, and three Territorial units with powers of self government delegated by the federal government. In the post-World War Two era, much consumer protection legislation has been adopted at the federal and provincial levels.[1] The major problem has been not lack of legislation but serious lack of enforcement of the legislation. Canadian consumers are poorly organized and have little political clout. As a result, federal and provincial governments have little incentive to establish properly funded consumer protection agencies with effective powers.[2] The agencies that exist are seriously underfunded and are usually not encouraged to exercise their powers aggressively.

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[1] For the details see Ziegel, Jacob "*Canadian Consumer Law and Policies 40 Years Later: A Mixed Report Card*", 2010, 50 Canadian Business Law Journal (CBLJ) 259.

[2] Quebec is an exception to the general rule and has had an active programme of consumer protection since the 1980s when a left wing government was in power under the premiership of René Lévesque. The programme was (and probably remains) partly politically motivated because of Quebec's special status in the Canadian federation and an ongoing separatist movement.

II. Class actions to the rescue?

Starting in the 1970s, Canadian consumer activists and law teachers working and writing in the area turned to class actions as a promising remedy for the lack of enforcement by government agencies. In common law jurisdictions, class actions have their origin in the remedies long provided by Equity courts in England where a class of complainants was adversely affected by a defendant's wrongful conduct. However, the equitable remedies were very limited and did not include an award of damages to the members of the aggrieved class. Damages could only be awarded by common law courts and common law courts did not recognize class actions.

In England, the fusion of common law and Equity courts in 1873 conferred on all courts the power to grant common law and equitable remedies. However, the courts construed very narrowly their powers to grant damages in class actions.[3] As a result, prior to the modest reforms introduced in England in the late 1990s, class action damage claims never took root. The English rules of practice were also very deficient in providing rules for the actual conduct of class actions.

III. North american developments

In the United States, the position changed significantly with the adoption of class actions rules in the Federal Rules of Procedure in 1939, and still more so with the extensive revision of the Rules in 1966.[4] These rules still govern class actions in federal US courts and have been widely copied in state class action rules. Consequently, class actions in the US have become a major social, economic and legal phenomenon at both the federal and state levels.

IV. Canadian developments

In Canada, in 1978, Quebec, a civil law jurisdiction, was the first province to adopt class action rules and these were heavily influenced, in con-

[3] A leading case was *Markt & Co*. vs. *Knight Steamship Co.* [1910] 2 K.B. 1021 (C.A.), which held that damage claims were personal to each member of the alleged class and therefore could not be the subject of a class action. The English courts took this position even though the losses suffered by members of the class in this case were readily assessable and could have been ascertained in subsequent proceedings once the issue of liability was determined.

[4] Legislation restricting the use of state actions was adopted by the US Congress in 2005 See Elizabeth J. Cabrasee, Fabrice Vincent and Paulia do Amaral, "The Class Action Fairness Act of 2005: The Federalization of U.S. Class Action Litigation" (2006) 43 CBLJ 398.

cept if not in structure, by the US Federal Rules.[5] However, for the first ten years or more there was little class action activity in Quebec and the Quebec initiative attracted little attention outside Quebec.

The changing interest in class actions in common law Canada resulted from the 1982 release of the three volume seminal report on Class Actions by the Ontario Law Reform Commission (OLRC).[6] The Report strongly supported class actions on three principal grounds: 1. Consumer Justice. 2. Economy of Judicial Resources, and 3. Behavioral modification of potential defendants. The Commission perceived the need for consumer class actions because of the rapid changes in the Canadian market place since World War II, the sophistication of many of those goods and services in the market place, and the disparity in bargaining powers between the typical consumer and the powerful (and often multinational) corporations offering those goods and services. The two other rationales offered in the Report for the need for a class action remedy were really subsidiary to the first. Economizing on judicial resources only comes into play if class actions are made possible and easy to invoke. Behavioral modification of potential defendants is a worthy goal though difficult to prove in practice. Price fixing and other antitrust behavior seems to continue to flourish in both Canada and the United States despite the existence of class action legislation, so does insider trading in securities markets and false advertising by large and small corporations.

Despite the powerful reasoning of the Ontario Report, class action legislation in Ontario was only enacted in 1992,[7] and then only because there had been a change of governments since the publication of the OLRC Report in 1982 and because of the appointment of an attorney general, Iain Scott, who was very sympathetic to consumer issues. Since 1993 (and especially during the past decade) substantially similar class action legislation has been adopted in the other common law provinces, with the exception of Prince Edward Island (Canada's smallest province).[8] At

[5] Quebec, Code of Civil Procedure, R.S.Q. 1977, c.C-25, art 999-1051, enacted by S. Que. 1978, c.8, s 3, as am. Since Quebec is a civil law jurisdiction, its willingness to embrace a quintessentially common law procedural device seems to contradict the view of some comparativists that legal systems are deeply rooted in the culture and history of their societies and that concepts and doctrines peculiar to one system cannot readily be transplanted to a different cultural milieu.

[6] Ontario Law Reform Commission, *Report on Class Actions*, 3 vols., 1982. See also the follow-up report commissioned by Attorney General Ian Scott, Ontario, *Report of the Attorney General's Advisory Committee on Class Action Reform*, 2 vols., Toronto, February, 1990.

[7] Stat. Ont. 1992, c. 6.

[8] The Uniform Law Conference of Canada also adopted a Model Class Actions Act in 1996 and amended it in 2006. For further detail, see: *http://www.chls.ca/en/us.* There are now

the federal level, class action rules of procedure have been adopted by the Federal Court without the benefit of substantive legislation.[9]

V. Impact of the legislation

The class action legislation has proved immensely popular with plaintiffs' lawyers across Canada as a challenging and potentially very profitable source of new business. Defence counsel have also benefitted greatly, and perhaps even more, because they do not have to worry about being paid for their services.[10] Although official statistics are not available,[11] it is reasonable to assume than more than five hundred class actions have been initiated

several ongoing commentaries on the provincial legislation and the case law interpreting the legislation. The main differences among the common law Acts are the following: 1. About half the provincial Acts do not permit the inclusion in the action of extraprovincial members of the class without the consent of those members ("opt-in" provision); the Ontario and other acts impose no such restrictions but leave the issue to be decided by the courts. 2. Awarding of costs. Under the Ontario Act, the normal cost rules apply, i.e., that the losing party must pay the costs of the other party. However, s. 31(1) of the Ontario Act allows the court to relieve an unsuccessful plaintiff from having to pay to pay the defendant's costs if the court finds that the case raised issues of public importance or novel and difficult points of law. Under the Quebec legislation, an unsuccessful plaintiff is only liable to pay costs on the Small Claims Court scale, which is very modest.

9 This difference in approach arose because of the remarkable decision of the Supreme Court of Canada in *Western Canada Shopping Centres* Inc. vs. *Dutton* 2001 SCC 46 holding that Canadian superior courts had inherent jurisdiction to alter the rules of practice to facilitate class actions. The Supreme Court had previously reached the opposite conclusion in *Naken v. General Motors of Canada* [1983] 1 S.C.R. 72. Arguably the two decisions can be justified on the following grounds. In *Naken* the plaintiffs did not argue that the trial court had an inherent jurisdiction to change the rules of practice but contended that their claims could be accommodated within the existing jurisprudence governing class actions. The Ontario Court of Appeal accepted the argument but the Supreme Court of Canada disagreed. In *Dutton*, the Alberta Court of Appeal followed N*aken*, but the issue of the Court's inherent jurisdiction to adapt the rules of practice *ex mero motu* does not appear to have been raised. It was raised in the Supreme Court of Canada and was accepted in the Court's unanimous judgment. What the Supreme Court of Canada did not make clear in *Dutton* was whether a trial or appellate court could change the rules of practice to fit the needs of a particular case or whether the change had to be effected by following the appropriate statutory procedure for changing the rules of practice.

10 As explained below, overwhelmingly plaintiffs' class counsel work on a contingency fee basis and only get paid if the action is successful.

11 Counsel are not required to notify a public agency, other than the court registry in which the action is started, when starting a class action. The Canadian Bar Association has agreed to serve as a depository for new filings, but there is no sanction against firms that do not comply.

since 1992, most of them in Ontario, British Columbia and Quebec.[12] Only about ten percent have ever gone to trial; the rest have been settled (with the courts' approval) or have been discontinued by the plaintiffs. One leading Canadian class action commentary has identified sixteen different types of claim.[13] Many of the cases have involved consumer interests e.g., defective products or services, injurious drugs, false representation in the sale of goods or services, usurious rates of interest charged by payday loan companies, undisclosed or unauthorized fees by banks, telephone companies and other service providers, price fixing, emission of dangerous substances from industrial enterprises and other environmental hazards.[14] An equally significant feature of Canadian class actions is that a significant number of them have been brought against the federal or provincial government and local governments, and public institutions such as hospitals and institutions for handicapped children.[15]

VI. Structure of the legislation

The class action legislation of the common law provinces is not uniform[16] but they all share the following features: 1. Except in one case,[17] there

[12] Saskatchewan has also become an active player largely because of the entrepreneurial ambitions of a Regina based lawyer, who has also established an office in many of the other provinces.

[13] See Ward K. Branch, *Class Actions in Canada* (loose-leaf publication), L-1 et seq. (Canada Law Book Inc.).

[14] In a survey distributed among 29 leading plaintiffs' class counsel at 21 firms across Canada, Prof. Jasminka Kalajdzic found that consumer class actions, as the term was defined in her paper, were the most numerous of class actions being litigated. Actions involving defective drugs, medical devices and other products, including tainted food; securities and price fixing comprised 219 of the 332 cases reports by the survey recipients. Jasminka Kalajdzic, "Consumer (Injustice: Reflections on Canadian Consumer Class Actions" (2010) 50 Can. Bus. L. J. 356 (CBLJ).

[15] The common law rule protecting federal and provincial governments from actions in delict were generally abolished after World War Two. They still appear to remain in force, at least to some extent, at the federal and state levels in the US.

[16] Half of the provinces have adopted the Ontario model; the other common law provinces adopted the draft law prepared by the OLRC as parts of its Report on Class Actions or have adopted the Model Act prepared by an ad hoc group of class actions specialists under the aegis of the Uniform Law Conference of Canada.

[17] Under the Ontario Securities Act, as amended in 2005, Part XXIII.1, defendants cannot be sued without leave of the court and the court must be satisfied that the prospective plaintiff has a strong prima facie case. This restriction differs from the requirement in section 5 of the Ontario CPA, as interpreted by the courts, that the plaintiff must have a reasonable cause of action and "reasonable" has been interpreted very elastically. The special require-

are no restrictions about the types of plaintiffs that may initiate class actions and the types of person that may be sued as defendants and both are governed by the general provincial rules governing the types of person who may sue and be sued. 2. However, the action cannot proceed[18] without the court first certifying that the action is appropriate for class action treatment, that the members of the class have been properly identified, that the claims or defences raise common issues, that the named plaintiff and plaintiff's counsel are suitable persons to conduct the action, that the plaintiff has presented the court with a plausible plan for the conduct of the action, and, most important, that the court is satisfied that a class action is the "preferable" means for addressing the plaintiff's complaint.[19] Once the action has been certified, the court is given very broad and flexible powers to supervise the conduct of the action, to admit statistical evidence, to divide the class into subclasses, and to grant a *cy-pres* award in lieu of individually assessed damages where, in the court's opinion, individual assessments would be too time consuming and expensive and the amounts too small to justify the exercise.

To a non-Canadian and especially to a civilian lawyer, it may seem therefore that Canadian class actions provide an efficient and effective answer to the non-enforcement of consumer legislation and private law principles by traditional means. Undoubtedly, consumers have won some very significant class action victories but they do not represent the norm and, among many other hurdles, Canadian consumers and their counsel continue to face the following substantive and procedural hurdles:

1. Doctrinal and Substantive Barriers. Generally speaking, Canadian consumer law has not caught up with the realities of the modern market place. For example, the implied warranties and conditions in the provincial Sale of Goods Acts only apply as between the immediate seller and buyer and do not bind the manufacturer or producer of the goods unless the consumer buyer can show that the manufacturer had made a direct representation to the consumer *and* that the consumer saw and relied on the representation at the time the consumer purchased the goods.[20]

ment in securities cases was adopted as a quid pro quo of class members being able to sue without being required to show that they had seen and relied on the security issuer's allegedly false representation.

[18] See e.g., Ontario Act, s. 5.

[19] The preferability test is less demanding than the test required under the US Rules, which requires the plaintiff to prove that a class action is a "superior" means to other alternatives for addressing the class members' complaints.

[20] It was on this ground that the Newfoundland & Labrador Court of Appeal denied a class action brought by consumers against tobacco manufacturers for misleading representa-

2. Mandatory Arbitration Clauses. With a view to avoiding the headaches of class actions, many large corporations in Canada and the US have resorted to boiler plate provisions in their written and online contracts requiring consumers to arbitrate any disputes that the parties have not been able to resolve amicably. Quebec and Ontario have outlawed such provisions and Alberta law requires the province's consent before such clauses can be enforced. In most of the other provinces without such provisions (or previously without such provisions), the courts have been divided about the enforceability of mandatory arbitration provisions. This has been particularly true of the conflicting decisions of the Supreme Court of Canada in *Dell Computer Corp. v. Union des Consommateur,*[21] *Rogers Wireless Inc. v Muroff,*[22] and *Seidel v. Telus Communications Inc.*[23] It goes without saying that, unless all the other provinces fall into line or the Supreme Court reverses its position, a wide range of class actions will be jeopardized in many of the provinces.[24]

1. Financial Barriers. Class Actions are enormously expensive and, with rare exceptions, plaintiff counsel work on a contingency fee basis. This means that counsel will not be paid unless the action is successful or is settled out of court - both outcomes that counsel cannot predict in advance. At a minimum, counsel will wish to be satisfied that the prospective gains will outweigh the risks or, put more concretely, that a judgment or settlement in the plaintiff's favour will at least run to a million dollars or other substantial amount.[25]

tions concerning the safety of their products. In Ontario, a similar conclusion was reached with respect to a class action brought by students against a private vocational school with respects to the students' prospects of securing employment once they had obtained their diplomas. The buyers of life insurance from an insurance company, who complained of misrepresentations by the company's agents, were more fortunate because the court was satisfied that the same representations had been made to all the buyers.

21 [2007] 2 S.C.R. 801.

22 [2007] 2 S.C.R. 921.

23 (2011) 329 D.L.R. (4th) 577. See further Shelley McGill, "Consumer Arbitration After *Seidel v. Telus* (2011) 51 CBLJ 187.

24 National class actions, discussed below, will also be put in jeopardy because plaintiff's counsel will always have to worry whether an arbitration clause will be enforceable against members of the class who entered into their contracts in a province without invalidating legislation.

25 In Ontario, plaintiff's counsel can apply for financial support from the Class Proceedings Committee, a statutory body established at the same time as enactment of the Class Proceedings Act. If the application is granted, the grant will cover counsel's disbursements and also indemnify counsel and the plaintiff against a costs award if the action is unsuccessful. As a *quid pro quo,* if the action is successful 10 per cent of the award must be paid to the Fund. The Committee only has limited funds at its disposal and, once those funds have been disbursed, the Committee will cease to function unless the Ontario government agrees to renew its funding, an unlikely event.

2. Financing of Class Actions. This is another very considerable worry plaintiff's counsel has to contend with. The disbursements of mounting and maintaining a large class action can easily run into the hundreds of thousands of dollars. Not only that, but Ontario courts have held that if counsel knows that the named plaintiff is impecunious he is obliged to indemnify the plaintiff against any cost award rendered by the court if the action is unsuccessful. To address both these concerns, plaintiff's counsel in important cases are increasingly turning to funding by outside commercial enterprises specializing in this type of funding.

1. Problematic National Class Actions. Class action complaints frequently cover victims in more than one province; from the plaintiff counsel's point of view, therefore, it looks very attractive, financially and otherwise, to frame the action on behalf of all consumers in Canada who are similarly affected by the defendant's conduct. However, this approach encounters two difficulties. The first is that about half the provinces do not permit national class actions but require non-residents to *opt-in* into the provincial action before they can be bound by the outcome. The other difficulty is that there is still uncertainty whether a province has class action jurisdiction over non-residents. In Ontario, the majority of the courts that have considered the issue have upheld the provincial jurisdiction but there is weighty scholarly opinion in the opposite direction.[26]

2. Concurrent Class Actions in Several Provinces. This is the reverse side of the coin involving the validity of national class actions. Obviously, if a province has jurisdiction over non-provincial class members, the same must be true of the jurisdiction of other provinces that can show a close connection between the plaintiff and the defendant. From the defendant's point of view, this creates a dilemma, especially if both provinces insist on retaining their jurisdiction. In practice, reasonable counsel will try to reach a compromise, but counsel are not always reasonable! The ideal solution would be for the provinces to follow the US precedent of establishing the Canadian equivalent of Multidistrict Litigation Panels (MDLP) that would have jurisdiction to decide which of several competing federal district courts should be given the nod. However, the analogy is not entirely apt. In the US, the choice is

[26] See the collection of materials in Watson, Gary D. (ed.), *Class Actions and Materials*, Spring term 2011, Vol. 1, pp. 256-93 (Univ of Toronto, Faculty of Law). The Supreme Court of Canada had an opportunity to address the issue in *Canada Post Corp*. vs. *Lepine*, 2009, S.C.R. 216, but LeBel J., who wrote the Court's opinion, sidestepped the issue and said he hoped the provinces would collaborate in finding a common solution. The issue has arisen again in the context of securities class actions brought in Ontario where the action purports to represent aggrieved securities holders, including those outside Canada.

made among competing courts within the same judicial system and all are bound by the same Federal Rules of Procedure. This is not true in Canada where, constitutionally, each province is autonomous within its sphere of jurisdiction.

3. Settlement of Class Actions and the Cy-Pres *Doctrine.* Section 24 of the Ontario Act allows the loss and/or damages suffered by members of the class to be calculated on an aggregate basis where individual assessment of the loss or damages would be too difficult or expensive e.g., with respect to the losses suffered by cardholders where a bank has levied unauthorized charges.[27] However, Section 24 does not answer the question how the aggregate amount is to be disbursed and whether the courts can order the assessed amount to be paid *cy-pres* to a charitable agency or other philanthropic institution where the cost of calculating the amount to which each member of the class would be entitled is out all proportion to the potential benefits. The Ontario courts have said yes and the *cy-pres* doctrine is now well established in Canadian jurisprudence. However, Canadian and US scholars[28] have questioned whether the *cy-pres* doctrine has always been wisely applied and whether, somewhat perversely, the defendant may come out spelling like a rose because of its close connection with the beneficiary of the *cy-pres* award and because of the tenuous connection between the *cy-pres* award and the losses suffered by members of the class.

VII. The answer to the title of this paper

To the question are class actions in Canada a consumer's best friend, the answer must be: it depends. If enough consumers are involved and class action counsel feel confident that a multimillion dollar award is likely if the action is successful, then a class action will be the consumer's best friend; in other cases the question must be no. The status quo will continue and aggrieved will either have to seek other remedies or take their lumps.

For civilians and comparativists at large, he question will be a different one. For them the question will be whether their legal culture is compatible with the entrepreneurial model of class actions practiced in Canada and the United States. So far almost all civil law jurisdictions, and most common law jurisdictions outside Canada and the United States, have found

[27] See e.g., *Markson* vs. *MBNA Canada Bank*, 2007, O. J. No. 1684 (OCA) and cf. *Cassano* vs. *Toronto-Dominion Bank*, 2007, No. 4406 (OCA).

[28] With respect to Canada, see the criticisms voiced in the article by Prof Kalajdzic, *supra*, n. 14.

the price too high and have resisted making the conversion. For them, he question must be what alternative regimes they have developed to ensure that consumer legislation is effectively enforced and remains more than an aspiration.

CHAPTER II

THE EVOLUTION OF THE GLOBAL FINANCIAL SYSTEM

OVER THE LAST THIRTY YEARS

LA EVOLUCIÓN DEL SISTEMA FINANCIERO GLOBAL EN LOS ÚLTIMOS 30 AÑOS: LAS CRISIS FINANCIERAS Y SU IMPACTO EN EL SISTEMA FINANCIERO INTERNACIONAL

Juan Alberto Adam Siade

SUMARIO: I. *Antecedentes*. II. *Características del sistema financiero internacional*. III. *Las crisis financieras globalizadas*. IV. *La globalización de la información financiera*. V. *¿El ser humano se encuentra considerado como eje central dentro del engranaje de la integración internacional*? VI. *Bibliografía*.

I. Antecedentes

Cuando uno revisa el estado del arte del sistema financiero internacional y su evolución surgen diversas dudas, la primera de ellas se desprende de la orientación que se le ha dado a los trabajos de investigación que abordan el tema y que invariablemente tocan el tópico de las crisis o de los problemas financieros. Y en este sentido la pregunta que surge es, ¿Por qué siempre que se habla de la evolución del sistema financiero internacional se aborda forzosamente el tema de las crisis o los problemas financieros?

La respuesta a esta interrogante nos ilustra que no podría ser de otra forma. En realidad las finanzas son una disciplina joven comparada con los cientos de años que tienen otras áreas del saber que la humanidad ha construido en el transcurso de su historia.[1] El sistema financiero internacional se formó a la par que se construyó el conocimiento financiero en el mundo, y para resolver las necesidades sociales que surgieron en él. Sólo después de

[1] Sin dejar de formar parte de la economía, las finanzas se empezaron a enseñar formalmente de manera independiente en el año 1900 en la Universidad de Nueva York, y fue hasta después de la Segunda Guerra Mundial cuando la cultura financiera empezó estructurarse y extenderse al mundo.

una crisis o un problema financieros se hacían patentes las debilidades estructurales del sistema financiero que se tenían que normar y corregir.

De esta forma, es que después de la Gran Depresión y al término de la Segunda Guerra Mundial nace en 1944 el sistema financiero conocido como *Bretton Woods*, y con él la creación del Fondo Monetario Internacional que fue fundado en 1945, cuyos objetivos eran los de promover la cooperación monetaria internacional, impulsar la estabilidad de los tipos de cambio, facilitar el comercio internacional y promover el crecimiento económico de todos los países. Tanto el Banco Mundial en 1944 como el Acuerdo General sobre Aranceles Aduaneros y Comercio en 1947 también tuvieron sus orígenes en este sistema.

II. Características del sistema financiero internacional

Después del sistema financiero conocido como el patrón oro, el sistema *Bretton Woods* estableció una política monetaria que permaneció vigente hasta 1971, que consistía en mantener el tipo de cambio fijo en los diferentes países del mundo en relación con el dólar de los Estados Unidos de América, y también un precio fijo de la onza de oro.

Después de dos años en 1973 se estableció en el mundo un sistema de tipos de cambio flexibles que no fue adoptado en forma directa por todas las economías, lo que contribuyó a provocar desajustes en los propios tipos de cambio y, en consecuencia, a vivir períodos de amplias devaluaciones principalmente en países en vías de desarrollo hoy llamados países con mercados emergentes. Economías que pasaron por un proceso de transición lento al meter control gubernamental sobre los tipos de cambio para que, años después en la década de los noventa, los flexibilizaran en función de la oferta y la demanda.

También las tasas de interés dejaron de ser estables para hacerse flexibles en función de las características de la economía, lo que impulsó el deseo de los inversionistas de mover sus inversiones a países que les ofrecieran un mejor rendimiento por sus inversiones.

La necesidad de mover las inversiones de un país a otro que ofreciera mejores rendimientos, es uno de los antecedentes de la creación del sistema financiero internacional que rige hoy en día, y que necesitaba romper las barreras financieras a través de una integración internacional.

La integración financiera constituye una mayor interrelación entre los mercados financieros internacionales, lo que permite aumentar la captación de inversión extranjera directa y especulativa.

Se caracteriza por ofrecer rendimientos aceptables internacionalmente para mantener y aumentar la inversión extranjera directa, y por ser altamente volátiles en lo que respecta a los flujos relacionados con la inversión especulativa que se caracteriza por la salida y el abandono repentino del país cuando se presentan situaciones de riesgo.

La integración también implica la propensión al contagio internacional de situaciones financieras desfavorables.

Para ilustrar un ejemplo de los beneficios que trae la integración financiera, se señala el caso de América Latina y el Caribe en donde la inversión extranjera directa en 2011 representó el 10% del los flujos mundiales, lo que sin duda fomenta el desarrollo de la región.

Inversión extranjera directa en América Latina	
Año	Millones de dólares
2000 a 2005	67,468
2006	74,866
2007	116,869
2008	137,001
2009	81,589
2010	120,880
2011	153,448
Fuente: elaboración propia con datos de la CEPAL	

Esto también es una muestra de que en la medida en que la inversión extranjera directa se recupera en el mundo en donde se estima que en 2012 se alcanzarán los niveles que se tenían en 2007, en América Latina y el Caribe tan sólo en 2011 ya se había superado lo captado en el propio 2007. También significa que los países con mercados emergentes son una buena alternativa de inversión.

Inversión extranjera directa en el mundo	
Año	Millones de dólares
2005 a 2007*	1,472,000
2007	1,971,000
2008	1,744,000
2009	1,185,000
2010	1,244,000
2011	1,500.000**
2012	1,900.000**
*Promedio **Estimado Fuente: elaboración propia con datos de la UNCTAD, *World Investment Report* 2011.	

III. Las crisis financieras globalizadas

1. *Ley Sarbanes-oxley*

Un problema financiero que se globalizó en el año 2001 dio origen a la ley Sarbanes-Oxley[2] que regula las funciones financieras contables y de auditoría. Surgió a raíz de delitos cometidos por malas prácticas financieras y administrativas relacionadas con fraudes, corrupción, negligencia y conflictos de intereses. Los casos de *Enron* y de otras empresas como *Xerox* son el ejemplo de un problema internacional que se globalizó y que como consecuencia provocó la desaparición de una de las firmas financieras, contables, de auditoría y de consultoría más importantes del mundo. Seguido de este caso, la declaratoria de bancarrota de *Worldcom* provocó que el Congreso Americano aprobara el proyecto de ley de la Cámara de Representantes, para que posteriormente fuera firmado por el presidente de los Estados Unidos de América y se convirtiera en ley el 30 de julio de 2002.

Con esta ley se crearon nuevos organismos para supervisar la contabilidad, para normar la auditoría de los estados financieros, para regular las finanzas corporativas y para proteger a los inversionistas. De igual forma, se aumentaron las penas criminales y civiles por delitos cometidos contra los mercados de valores.

2. *La crisis de 2008 y los acuerdos de Basilea*

Los mercados de valores del mundo caían la semana del 15 de septiembre de 2008 cuando se anunciaba la quiebra de *Lehman Brothers* y el rescate que hacía *Bank of America* con la compra de *Merrill Lynch*. Al final de la semana los mismos mercados volvían a subir en forma estrepitosa cuando el presidente de los Estados Unidos de América anunciaba un plan de emergencia después de que el presidente de la Reserva Federal convocara una reunión con miembros del Congreso para estudiar un plan de medidas contra la crisis.

De la misma forma, los mercados de valores volvían a caer dramáticamente cuando el Congreso de los Estados Unidos no aprobaba el plan, hasta unos días después de que fuera ajustado el mismo. Aún así los mercados siguieron bajando presagiando graves problemas futuros en la economía mundial.

Así suben y bajan los mercados cuando el riesgo, que se refleja en una alta volatilidad, es grande internacionalmente, como producto de la integración de los mercados financieros.

[2] Véase: U. S. Congress Sarbanes-Oxley Act of 2002 U.S. InterAmerican Community Affairs.

El origen de todo esto fue la crisis inmobiliaria que desató una crisis de crédito aunada a una burbuja en los precios de los energéticos y de los alimentos. Las inyecciones de liquidez que han hecho los bancos centrales de las principales economías del mundo han evitado y siguen evitando una crisis mayor.

En noviembre de 2010, dos años después de la crisis financiera que inició con la quiebra de *Lehman Brothers*, el grupo de los líderes del G20 dieron forma a una nueva arquitectura financiera internacional en la cumbre de Seúl, al adoptar los acuerdos de Basilea III que fueron alcanzados dos meses antes por el Comité de Basilea para el Control Bancario, sobre las reformas del sector financiero, que en términos generales establecen que los bancos del mundo tienen que generar reservas de capital superiores a las ya existentes, para poder enfrentar las posibles y eventuales crisis con sus recursos propios.

Anteriormente se habían firmado dos acuerdos en el mismo sentido y, de esta forma, en el año de 2004 en los acuerdos de Basilea II se establecieron estándares internacionales para determinar los requerimientos de capital mínimos necesarios que los reguladores bancarios debían observar, para proteger a los bancos ante los riesgos financieros. Basilea I en 1974 con los gobernadores de los bancos centrales del G-10 estableció un conjunto de recomendaciones relacionadas con el mismo tema, es decir, sobre el capital mínimo que debía tener un banco en relación con los riesgos que enfrentaba.

3. *Las crisis bursátiles desde 1929 y su efecto internacional*

Desde 1929 se recuerdan cinco grandes crisis bursátiles previas a la que vivimos en 2008 y una después en 2011. Todas las crisis son diferentes y no podemos igualar una con la otra porque las situaciones financieras, económicas, políticas y sociales entre una y otra crisis son diferentes.

29 de Octubre de 1929 "el martes negro". El promedio del índice Industrial *Dow Jones* (DJI por sus siglas en inglés) cayó poco más de un 11% y con un volumen récord de acciones negociadas. La caída se prolongó hasta 1932 perdiendo aproximadamente el 80%. El desplome del mercado de valores anunciaba el comienzo de la gran depresión económica de la década de los años treinta que culminó con la Segunda Guerra Mundial.

En aquellos días la industria de la construcción daba señales de estancamiento desde inicios de 1929, además, de 1926 a 1929 había un desfase entre la actividad bursátil y la economía real. Los valores inmobiliarios de

Estados Unidos y la Gran Bretaña se desplomaban después de haber vivido una burbuja que los había inflado demasiado. En aquel entonces, una burbuja en el sector inmobiliario principalmente en los estados de Florida y California fue una de las causas de la recesión que, posteriormente, se tradujo en la mencionada depresión.

La crisis de 1987 "el lunes negro". El 14 de octubre se dio a conocer la noticia de un enorme déficit comercial mensual de la economía de los Estados Unidos de Norteamérica que provocó una fuerte caída de la bolsa de valores. Esa crisis provocó en el caso de México que muchos capitales perdieran aproximadamente el 80% de su inversión. En Estados Unidos de América el 16 de octubre el DJI se hundió 100 puntos por primera vez en su historia y, después, el 19 de octubre, llamado el lunes negro la bolsa perdió más de 500 puntos que representaron un desplome de más del 22%.

La crisis de 1997. La volatilidad financiera que inició en Asia en julio de 1997 propició que el 27 de octubre de ese mismo año se diera la mayor pérdida diaria en puntos del DJI. Ese mismo día los mercados de valores de Argentina, de México y de Brasil caían entre un 13 y un 15%. Al día siguiente, 28 de octubre, el contagio llegaba a Europa y, en Asia, el mercado de Japón perdía más del 4%.

*La crisis del 2001***.** Las bolsas del mundo entero se desplomaron ante los ataques terroristas del 11 de septiembre del 2001 en Estados Unidos de América.

El aviso del 2007. El mercado de valores de Nueva York reflejado en su Índice Industrial Dow Jones cayó un 3,3% el 27 de febrero del 2007, provocado por el derrumbe de las bolsas chinas que cayeron casi un 9% y las débiles cifras de manufacturas en los Estados Unidos. La bolsa de Japón bajó más de 3% y la de México más del 4%, previo a *la caída del 2008* ya comentada.

La crisis de 2011. Por primera vez en la historia la calificación del crédito estadounidense fue degradada de "AAA" a "AA+" por la agencia *Standard & Poor´s*, por el enorme peso de su deuda y su fuerte déficit presupuestario. Esta situación provocó una caída en todas las bolsas de valores del mundo, seguida de una volatilidad extrema de más de seis meses en los mercados financieros mundiales.

4. *La crisis en Europa*

Muchos de los problemas que en Estados Unidos de América dieron origen a la crisis de 2008, ahora se están replicando en Europa como si se siguiera la inercia de la interrelación, y como si fuera un aviso al mundo de

que la crisis que empezó hace cuatro años no ha terminado, ya que lo que ha sucedido en 2011 y 2012 en España, Grecia, Irlanda y Portugal ha tambaleado y seguirá tambaleando a los mercados financieros internacionales, ya que cuando adoptaron al Euro como moneda, lanzado en 1999, tuvieron acceso a créditos en condiciones sumamente favorables y que no correspondían al crecimiento verdadero de sus economías.

Estos países se vieron con una liquidez enorme y en lugar de modernizar sus economías, invertir en innovación tecnológica e impulsar su desarrollo con maquinarias y equipos que los pusieran a la altura de los países más desarrollados de la zona, decidieron sobre invertir en la construcción de bienes inmuebles, lo que provocó una burbuja inmobiliaria similar a la de los Estados Unidos de América, con las consecuencias que conocemos.

Esta situación contribuyó a desajustar sus sistemas financieros por sobre endeudamientos de los beneficiarios de los créditos que ya no podían hacer frente a sus pagos; y por manejar tasas y plazos que no correspondían a su realidad, lo que provocó desajustes en las finanzas bancarias y, con ello, la necesidad de rescatar a los bancos que estaban en peligro de desaparecer.

Desde hace dos años, es decir, en 2010 cuando los problemas crediticios de los bancos irlandeses y griegos se empezaron a ver en crisis de solvencia y liquidez, se puso en duda su permanencia en la eurozona que se caracteriza por agrupar a los países que adoptaron al Euro como moneda.

PAISES QUE CONFORMAN LA UNIÓN EUROPEA					
País	Entrada	Moneda	País	Entrada	Moneda
Luxemburgo	Marzo 57	Franco Luxemburgués	Suecia	Ene-95	Corona Sueca
Alemania *	Marzo 57	Marco Alemán	Estonia *	Enero 04	Corona Estonia
Bélgica *	Marzo 57	Franco Belga	Hungría	Enero 04	Fortín Húngaro
Francia *	Marzo 57	Franco Francés	Chipre *	Abril 04	Libra Chipriota
Italia *	Marzo 57	Lira	Eslovaquia *	Abril 04	Corona Eslovaca
Holanda *	Marzo 57	Florín Holandés	Eslovenia *	Abril 04	Tolar Esloveno
Dinamarca	Enero 73	Corona Danesa	Letonia	Abril 04	Lats
Irlanda *	Enero 73	Libra Irlandesa	Lituania	Abril 04	Litas
Inglaterra	Enero 73	Libra Esterlina	Malta *	Abril 04	Lira Maltesa
Gracia *	Enero 81	Dracma	Polonia	Abril 04	Zloty
España *	Enero 86	Peseta	República Checa	Abril 04	Corona Checa
Portugal *	Enero 86	Escudo	Bulgaria	Enero 07	Lew
Austria *	Enero 95	Chelín Austriaco	Rumania	Enero 07	Leu
Finlandia *	Enero 95	Marco Finlandés			
*Países que adoptaron el euro como moneda. Elaboración propia con datos de IXE análisis					

Una de las críticas que surgieron cuando se creó y se lanzó el Euro como moneda de los países que la adoptaron, fue que se había creado la unión monetaria sin una unión fiscal. Ante la unión monetaria se autorizó la creación de un banco central denominado Banco Central Europeo que es el que regula las políticas monetarias y crediticias. El problema se presentó cuando los países integrantes de la eurozona no consideraron unificar las políticas fiscales orientadas a mantener niveles equilibrados en cuanto a los presupuestos públicos, los niveles de recaudación fiscal y la orientación al gasto público. Después de más de 10 años del lanzamiento del Euro como moneda, las diferencias en los sistemas financieros de cada país se han hecho cada vez más notorias.

En la siguiente tabla se ilustra un ejemplo de las diferencias tan enormes que hay en una pequeña muestra de nueve países europeos, algunos de ellos de la eurozona, en relación con el rendimiento del bono gubernamental a 10 años. Cabe mencionar que los países con tasas más bajas, en estos mementos tienen economías más estables que los que se vieron en la necesidad de subirlas para captar recursos financieros, al ofrecer mejores rendimientos, para poder hacer frente a sus problemas de liquidez.

País	Rendimiento del bono a 10 años en porcentaje
Reino Unido	1.65
Francia	2.47
Alemania	1.38
Grecia	24.74
Italia	5.95
España	6.70
Suecia	1.38
Holanda	1.82
Suiza	0,52

Fuente: elaboración propia con datos de *Bloomberg*, julio de 2012.

Esto claramente nos muestra que las políticas monetarias se siguen ajustando a las necesidades particulares en función de lo que dicta cada banco central, aunque se pertenezca a la eurozona. Si a esto le sumamos una falta de unificación de cuestiones fiscales, entendemos por qué fueron algunos de los factores que desajustaron los sistemas financieros.

Por otra parte, en una muestra de ocho países de América y Asia Pacífico se observan tasas estables.

País	Rendimiento del bono a 10 años en porcentaje
Estados Unidos de América	1.58
Canadá	1.72
México*	3.13
Brasil*	3.12
Colombia*	3.28
Japón	0.81
Australia	3.10
Nueva Zelanda	3.51

*Bono global
Fuente: elaboración propia con datos de *Bloomberg*, julio de 2012.

IV. La globalización de la información financiera

Ante la globalización de las finanzas la regulación ha tenido que cambiar y en este sentido en el mundo estamos viviendo un cambio de paradigma con todo lo que ello representa. Ya nos decía Thomas S. Kuhn, cuando hablaba de la estructura de las revoluciones científicas, que se presentan resistencias al cambio cuando el conocimiento evoluciona y se modifica un paradigma.

Este cambio, que si bien no es estrictamente científico, lo estamos viviendo con la necesidad de integrar internacionalmente la información financiera que las entidades generan y que se traducen en la adopción o en la adaptación de las Normas Internacionales de Información Financiera, para unificarla mundialmente y para hacerla comparable horizontal y verticalmente. Sin duda alguna ha costado mucho trabajo integrar al mundo en este sentido.

Hace treinta años y por mucho tiempo hablábamos de los Principios de Contabilidad Generalmente Aceptados, que se enseñaban en el primer semestre de las Licenciaturas de Contaduría y de Administración que curricularmente se estructuraban en un tronco común, y que no tenían ninguna complicación, ya que aproximadamente en diez páginas se explicaban todos ellos con lujo de detalles y se entendían muy bien. Ahora, las Normas de Información Financiera se tienen que enseñar en el transcurso de toda la licenciatura en diversas asignaturas en forma transversal, ya que abarcan un sinnúmero de temas que sería prácticamente imposible y antipedagógico intentar explicar en tan sólo un semestre.

Además, es un cambio tan importante en la normatividad financiera internacional que entró en vigor en este 2012, que las universidades estamos enfrentando el reto de educar a los responsables de la información financiera de las entidades para que se sumen a este cambio de paradigma a través de cursos, talleres y diplomados.

V. ¿El ser humano se encuentra considerado como eje central dentro del engranaje de la integración internacional?

Los rescates bancarios, que conocemos en México desde las crisis de 1982 y 1994, como característica común de las crisis del sistema financiero internacional, se han hecho patentes en los Estados Unidos de América en 2008, en Irlanda y Grecia desde 2010, y en España en 2012. Estos rescates y los que se sigan sumando, forzosamente tendrán que ser implementados con fuertes medidas de austeridad que tendrá que asimilar la sociedad y que impactará en una disminución en su calidad de vida.

El problema de tener que adoptar medidas de austeridad de enorme magnitud nos hace pensar si ¿serán humanamente aguantables?

El desempleo sigue creciendo en Europa y recientemente en el mes de mayo de 2012 tocó máximos históricos en la zona euro del 11.1% y en el conjunto de la Unión Europea, UE, del 10.3%, cuando en mayo de 2011 las cifras eran del 10% en los diecisiete países de la eurozona y del 9.5% en los veintisiete de la UE.

Estas cifras son las más altas en la eurozona desde 1995 y en la UE desde el 2000, alcanzando un número de desempleados de 17.5 millones y de 24.8 millones respectivamente.

El caso más grave lo tenemos en España con un desempleo del 24.6%, mientras que en Grecia es del 21.9%. Este hecho se agrava aún más con el desempleo juvenil que en ambos países supera el 50% en menores de 25 años. Aun en los países europeos que presentan las mejores cifras la situación es alarmante por su magnitud, ya que en Holanda es de 9.2%, en Austria de 8.3% y en Alemania de 7.9%.

La tasa de desempleo juvenil mundial es del 13%. En la escala internacional el desempleo en 2011 era de 75 millones de jóvenes con edades de entre 15 y 24 años, de los cuales el 6.4% ha perdido la esperanza de tener un empleo. Se estima que esta proporción se mantendrá o aumentará en este 2012.

Por otra parte, en América Latina el desempleo en los jóvenes se agrava continuamente al grado de que en Argentina, Colombia, Costa Rica, El Salvador, Honduras y México sólo el 60% de los que consiguen trabajo lo encuentran en el empleo informal, mientras que en Bolivia, Paraguay y Perú el porcentaje es del 85%.

Además, sólo el 37% de los que se logran contratar en un empleo formal no cuentan con seguro social.

Ante estos datos de esta única variable analizada nos preguntamos ¿hasta dónde el ser humano se ha quedado fuera del engranaje financiero internacional? ¿de qué forma las autoridades financieras internacionales tendrían que actuar para reinsertar al ser humano en el centro de este engranaje?

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INVOLUNTARY CREDITORS AND CORPORATE BANKRUPTCY

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SUMMARY: I. *The Law of Involuntary Creditors: A Comparative Account*. II. *Involuntary creditors in the "new" corporate bankruptcy*. III. *Adjusting to the New Reality*. IV. *Conclusion.*

The problem of involuntary creditors in corporate bankruptcy has been long recognized, with little actual effort expended toward solving the matter.[1] Instead, the issue of tort, environmental, and tax creditors is typically acknowledged and the swept to the side by observing, "they should have a priority".[2] No effort is actually made to give them a priority —although tax creditors typically already have a priority in both the United States and Canada[3]—

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1 See Bebchuk, Lucian Arye and Fried, Jesse M., "The Uneasy Case for the Priority of Secured Claims in Bankruptcy", 105 *Yale L. J.*, 1996, 857 at 883 ("It is by now a familiar point in the law review and finance literature that according full priority to secured claims permits a firm to divert value from its tort creditors").

2 Rasmussen, Robert, "Resolving Transnational Insolvencies Through Private Ordering", 98 *Mich. L. Rev.*, 2000, 2252 at 2269. *See also* Adler, Barry E., "A World Without Debt", 72 *Wash. U. L. Q.*, 1994, 811 at 826; Heidt, Kathryn R., "Cleaning Up Your Act: Efficiency Considerations in the Battle for the Debtor's sAssets in Toxic Waste Bankruptcies", 40 *Rutgers L. Rev.*, 1988, 819 at 851-63; Note, "Switching Priorities: Elevating the Status of Tort Claims in Bankruptcy in Pursuit of Optimal Deterrence", 116 *Harv. L. Rev.*, 2003, 2541 at 2562; Dagan, Hanoch, "Restitution in Bankruptcy: Why All Involuntary Creditors Should Be Preferred", 78 *Am. Bank. L. J.*, 2004, 247 at 277.

3 This is not always so, for example, in Australia, the taxing authority has a general unsecured claim, coupled with strong rights against directors who fail to act in response to growing financial distress.

rather the observation simply removes an annoying problem with the larger theoretical point being made about corporate bankruptcy.[4]

Moreover, the repeated use of this tactic ignores the ways in which corporate bankruptcy has changed over the years, rendering even this solution of limited value. In particular, the growth of secured credit means that a priority claim, which simply bumps the creditor to the front of a large group of unpaid unsecured creditors, is little more than a token, with no real value.[5] And more importantly, the trend of selling the corporate debtor's assets before consideration of a reorganization plan means that even the limited power that a priority creditor has will often be focused in the wrong place.[6] In particular, once the debtor's assets are sold, powers to vote on a plan are of little import in a case that could just as easily be resolved by liquidation under either the BIA, in Canada, or chapter 7, in the United States.

In this paper we focus on the particular concern that the preference for quick sales over traditional reorganization cases might allow the debtor's management to work with secured lenders to extract assets from the debtor in a way that would not be possible in a "normal" bankruptcy case. In particular, we examine how a quick sale can be used to cleanse assets of their association with environmental claims.[7]

We also consider how the insolvency systems in our respective countries might adapt to address this problem. Ultimately, the best protection for involuntary creditors, including environmental creditors, is to maximize the value of the debtor's assets. That counsels for improving stakeholders' ability to monitor the sale process and ensure that the sale process in not rushed for the sole benefit of senior creditors.

Throughout the paper we examine the issue of quick sales and involuntary creditors in both the United States and Canada. These two economies are closely linked, and thus have corporate bankruptcy systems that, while still unique, are amongst the most comparable of any two among the devel-

[4] Halpern, Paul *et al.*, "An Economic Analysis of Limited Liability in Corporation Law", 30 *U. T. L. J.,* 1980, at 117-18.

[5] For a discussion of the growth of secured creditor power in US chapter 11 cases, see Baird, Douglas G. and Rasmussen, Robert K.,"Private Debt and the Missing Lever of Corporate Governance", 154 *U. Pa. L. Rev.*, 2006, 1209 at 1236-37. See also Mann, Ronald J., "Explaining the Pattern of Secured Credit", 110 *Harv. L. Rev.*, 1997, 625 at 629; Warren, Elizabeth and Westbrook, Jay Lawrencen "Contracting Out of Bankruptcy: An Empirical Intervention", 118 *Harv. L. Rev.*, 2005, 1197 at 1222.

[6] For a detailed comparative discussion of quick sales see Ben-Ishai, Stephanie and Lubben, Stephen, "Sales or Plans: A Comparative Account of the 'New' Corporate Reorganization", 56 *McGill L. J.*, 2011, 591 (Ben-Ishai & Lubben, "Sales or Plans").

[7] 11 U.S.C. § 363(f). In re Trans World Airlines Inc., 322 F.3d 283 (3d Cir. 2003).

oped world. More generally, as shown throughout the paper, the strengths and weaknesses of each jurisdiction can inform the solutions we propose. Thus, we ultimately suggest that Canada would be well served by adopting certain aspects of U. S. law, and conversely the U. S. would increase the efficiency of its corporate bankruptcy system by taking insights from the Canadian system.

We begin by considering the U. S. and Canadian law on involuntary creditors, particularly environmental claims, in corporate reorganization proceedings. As we show, the law in Canada is somewhat underdeveloped and vague, which leaves open the possibility of abuse by the controlling parties in a CCAA proceeding. On the other hand, while the law in the United States is more developed, it is not much clearer. This again puts the onus on environment regulators and other involuntary claimants to protect their interests.

As we ultimately show, to the extent these creditors are separately considered by U. S. or Canadian bankruptcy systems, the focus is typically on the involuntary creditor's status as a claimholder in the proceeding. But in a world where debtors routinely pledge all of their assets to senior creditors before bankruptcy, and those assets are frequently liquidated before consideration of a bankruptcy plan, this puts the emphasis too late in the process.

We develop this argument in the second part of the paper, showing how the move to heavily pledged assets in turn facilitates creditor control of quick sales in corporate reorganization proceedings. These quick sales allow for the sale of assets free from involuntary claims in a way that would not be possible outside of bankruptcy, or often even under a formal reorganization plan. The risk that we identify is that this heightened power to sell assets also undermines the leverage of involuntary creditors, increasing the possibilities for senior lenders to transfer wealth to themselves.

In the third part of the paper, we consider how U. S. and Canadian procedures could be improved to guard against this risk.

We ultimately conclude that revising the U. S. and Canadian procedures to outlaw quick sales or limit them to cases where the debtor's assets are perishable is unlikely to be met with political approval in either jurisdiction or necessarily improve the outcome for involuntary creditors. However, as we have argued elsewhere in a more general comparison of the two regimes, this is another instance where it would be helpful to draw on key aspects of both systems. That is, the greater clarity provided for by the quick sale regime under chapter 11 and the more flexible newly developed test under the Canadian CCAA regime for approving quick sales. A more transparent version of the new CCAA test —that requires judicial balanc-

ing of interests— would provide a framework that involuntary creditors can begin to adjust to in the new reality of quick sales versus plans.

I. The Law of Involuntary Creditors: A Comparative Account

In this part, we develop an understanding of the law of involuntary creditors, with a particular focus on environmental creditors, whom we use as the prototypical example for the rest of the paper. But first, a definition: what is an involuntary creditor? Throughout the paper we use the term "involuntary creditor" to refer to any creditor that lacks the ability to protect itself ex ante. This inability is typically the result of a lack of information — tort creditors do not know they are or will be injured, environmental creditors do not have full information about the conditions on private property, and taxing authorities rely on debtors to provide information, and may only obtain the right to question that information years after liability has been created.

For purposes of this paper we do not consider creditors that do not contract to protect themselves as involuntary, even if the failure to contract is the understandable result of information or transaction costs.[8] These "mal adjusting" creditors are likely to be the collateral beneficiaries of many of the reforms we propose in Part III, but they are not are primary focus, inasmuch as we focus on those parties that are affirmatively harmed by modern corporate reorganization practices.

In both the United States and Canada operating firms are subject to a variety of federal and state or provincial environmental regulations. In the U. S., CERCLA is the principal federal statute concerning the cleanup or remediation of historical environmental contamination. The statute gives the Environmental Protection Agency numerous administrative and judicial tools to address risks posed by historical contamination.

In addition to providing EPA with the authority to undertake response actions, CERCLA creates liability, based on a "polluter pays" principal. First, if EPA, or any other party, cleans up a property, that party can recover its costs from four categories of responsible parties: the present owner and operator of the facility from which the hazardous waste were released, the past owners and operators of those facilities at the time the release occurred, generators of hazardous substances who arranged for disposal of their wastes at the site, and haulers who took wastes to the site.[9] In addition, EPA has authority to

[8] Lucian Arye Bebchuk & Jesse M. Fried, "The Uneasy Case for the Priority of Secured Claims in Bankruptcy", 105 *Yale L. J.*, 1996, 857 at 880-92. See also Lynn M. LoPucki, "The Unsecured Creditor's Bargain", 80 *Va. L. Rev.*, 1994, 1887 at 1897.

[9] 42 U. S. C. A. § 9607(a).

require responsible parties to perform cleanup actions themselves.[10] Other federal statutes are generally similar in coverage, but sometimes provide for different or more limited remedies. For example, under the Resource Conservation and Recovery Act, the EPA can only seek injunctions or administrative orders requiring the responsible party to take action — monetary damages are not available.

The Canadian approach is somewhat similar, insofar as there are checks in place designed to make the debtor company liable for the environmental damage and contamination it causes. Specifically, provincial and federal environmental protection statutes provide that a person who is in control of premises is liable for the costs of environmental remediation.[11] This is what is known as the "polluter pays" principle in Canada, whereby the person who is responsible for the damage is held accountable.

Moreover both of Canada's principal insolvency statutes —the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act*— incorporate rules governing environmental claims; however, within the insolvency context, it is worth noting that the usual environmental liability rules in federal and provincial legislation are modified, as will be discussed below. This contrasts with the United States, where environmental claims are not expressly mentioned in the Bankruptcy Code.

And despite the initial similarity between the Canadian and US regimes, the two jurisdictions differ in subtle ways with regard to how these cleanup obligations are treated upon insolvency. In the United States the debtor's liability for past cleanup work conducted by somebody else, whether the EPA or a private party, is a general unsecured claim that can be treated as such during the reorganization case.[12] On the other hand, orders directing the debtor to clean up property are typically not considered claims, and as such are not discharged at the end of the debtor's case.[13] This latter rule can apply to property that the debtor owned in the past, but no longer owns by the time of bankruptcy, and clearly gives the EPA a strong incentive to avoid taking on the cleanup work themselves.[14]

In Canada, the environmental authorities have somewhat better protection for past remediation. This is because costs are secured by a security interest on the real property affected by the environmental conditions as well

[10] 42 U. S. C. A. § 9606(a).

[11] See, for example, *Environmental Protection Act*, R. S. O. 1990, c. E-19.

[12] *Ohio* vs. *Kovacs*, 469 U. S. 274 (1985).

[13] *United States* vs. *Apex Oil Co*., 579 F. 3d 734 (7th Cir. 2009); In *re Chateaugay Corp.*, 944 F. 2d 997 (2d Cir. 1991).

[14] *In re Torwico Electronics*, *Inc*., 8 F. 3d 146 (3d Cir. 1993).

as on any contiguous real property and that interest is given super-priority status over any other claim, right, charge or security against the property.[15] The source for this super-priority status is found in Canada's two principal insolvency and restructuring statute, the *Bankruptcy and Insolvency Act* (the "BIA") and the *Companies' Creditors Arrangement Act* (the "CCAA").

Specifically, under these Acts, any federal or provincial governmental claim against the debtor for the costs of remedying any environmental damage affecting the real property of the debtor is secured by a charge on that real property and any contiguous real property related to the activity that caused the damage.[16] Under the Canadian Acts, the charge is enforceable in the same way as a mortgage or other security on real property, and is given super-priority over any other claim, right, charge or security on the property.[17] Essentially, this amounts to a governmental "super-lien" on the debtor's property and provides these involuntary claimants with a better priority status than what they would have received if the ordinary priority rules were applied.[18]

Under this scheme, the environmental condition or damage may occur before or after the date that the debtor files for bankruptcy or the date of filing a plan under the CCAA.[19] It is worth noting that if the environmental damage is extensive, the costs of the clean up may be in excess of the value of the property; in such cases, compliance with the remediation order will diminish the value of the assets available to the other creditors who have a claim.[20] However, the policy rationale behind these provisions is that the party in control of a property should be liable for the costs of any environmental remediation necessitated by their occupancy. Accordingly, the environmental remediation provisions in the BIA and CCAA reflect the "polluter pays" principle entrenched in federal and provincial incorporation legislation.[21]

With regard to presently contaminated property, the tables turn yet again, as the United States prohibits the abandonment of contaminated

[15] See s.11.8(8), CCAA.

[16] *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 at s. 14.06(7) [BIA]; and *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 [CCAA].

[17] BIA, *idem*; CCAA, *idem*; and Wood, Roderick, *Bankruptcy and Insolvency Law*, Toronto, Irwin Law, 2009, at 415-16 (Wood).

[18] Alexandria Pike, "Environmental Issues in Insolvency: Recent Developments", Davies, Ward, Phillips & Vinerberg LLP, 13 December 2010 (Pike) and Wood, *ibidem,* at 488.

[19] BIA, supra note 16, at 14.06(8) and CCAA, supra note 16, at 11.8(9).

[20] Wood, supra note 12 at 169.

[21] Wood, *ibidem*, at 141.

property in liquidation,[22] and abandonment would seem to be pointless in a traditional reorganization, because all property revests in the debtor at the end of the chapter 11 case.[23] Whist in Canada, the trustee in bankruptcy or the CCAA monitor may abandon environmentally damaged property, subject to certain rules,[24] and if this is done the monitor is not required to comply with a remediation order.[25] Moreover, under the Canadian system, the trustee/monitor is not personally liable for any environmental condition that occurred either before their appointment, or even after, unless the damage or condition arose as a result of their gross negligence or misconduct.[26]

The Superior Court of Justice decision in *General Chemical Canada Ltd., Re*,[27] provides an example of the Canadian approach. The Court considered the issue of environmental cleanup costs in the context of the bankruptcy of a chemical company.[28] Although the Ministry of the Environment ("MOE") of Ontario had claimed entitlement to costs related to environmental clean-up of the debtor's property, the interim receiver for the bankrupt estate had also brought a motion of the interim distribution of the estate's assets. It is worth noting that the funds that the interim receiver sought to distribute came from the operation of the debtor's business, as opposed to real estate holdings.[29] The Minister opposed the receiver's motion; specifically, despite conceding that any secured claim it had attached only to General Chemical's real property, it nevertheless maintained that both the debtor and the receiver had an obligation to take care of the cost of environmental cleanup before any funds were paid out to creditors.[30]

However, the court disagreed and granted the receiver's motion to distribute the assets, holding that the Minister was, in effect, an unsecured

[22] *Midlantic National Bank* v *New Jersey Department of Environmental Protection*, 1986, 474 U. S. 494.

[23] Lawton, Anne M. and Oswald, Lynda J., "Scary Stories and the Limited Liability Polluter in Chapter 11", 65 *Wash. and Lee L. Rev.*, 2008, 451, 475.

[24] Specifically, the trustee must elect to abandon the property by providing notice to the authority who issued the order and, unless some other period is specified in the order, the election to abandon must occur within ten days after the order is made. See Wood, supra note 12 at 169.

[25] BIA, supra note 11 at s. 14.06(4); and CCAA, supra note 11 at s.11.8(5).

[26] BIA, *ibidem* at s.14.06(2); and CCAA, *ibidem* at s.11.8(3).

[27] *General Chemical Canada Ltd., Re*, (2006) 22 C.B.R. (5th) 298 [*General Chemical Canada*].

[28] *General Chemical Canada*, *ibidem*, at para. 17 and 18.

[29] *General Chemical Canada*, *ibidem*, at para. 1.

[30] *General Chemical Canada*, *ibidem*, at para. 34.

creditor who was not entitled to special priority for cleanup costs.[31] This was especially so given that the assets that generated funds were not connected to the property that had created the environmental damage; accordingly, the Minister had no lien or priority over these funds. In its decision, the court observed that the *Environmental Protection Act* permits the MOE to issue orders to a polluter to clean up polluted property. However, absent exceptional circumstances or gross negligence or misconduct on the part of the trustee or receiver, the MOE is prevented from issuing orders to trustees or receivers.[32]

Accordingly, this case established that the powers of the government to make environmental orders in the context of a bankruptcy is, in fact, limited. It also bears mentioning that in its decision, the Court observed that the MOE's right to review General Chemical's financial assurance and require changes to it was stayed by the CCAA order — as General Chemical had first tried to reorganize under the CCAA, before failing to do so and filing for bankruptcy.[33]

In the appeal of *General Chemical Canada Ltd., Re*,[34] the debtor's interim receiver proposed a plan that was opposed by the MOE, on the grounds that the debtor failed to comply with provincial environmental safety requirements. As a result of this failure, the MOE claimed that there would be significant cleanup costs that exceeded the debtor's financial assurance under the *Environmental Protection Act*.[35] In this case, it was the MOE's position that the "polluter pays" principle for environmental remediation required that no distribution take place until there is an assurance that the debtor's assets are sufficient to effect a cleanup.[36] However, the Court found that in the face of BIA s.14.06(7) —which provides for priority to be accorded to environmental clean up costs— and s.14.06(8) —which establishes that environmental cleanup costs are provable claims in bankruptcy— the provincial environmental legislation was of no effect.[37] Specifically, the federal bankruptcy legislation was held to be paramount over the provincial regulations that the MOE was seeking

[31] *General Chemical Canada*, *ibidem*, at para. 46. The court went on to specify that, apart from its security, the MOE was an unsecured creditor like any other and "must prove its claim in the General Chemical bankruptcy. To permit the MOE to delay distribution to a secured creditor would give the MOE a quasi-priority to other unsecured creditors, and would defeat or delay the legitimate interests of secured creditors." *Ibidem* at para. 46.

[32] *General Chemical Canada*, *ibidem*, at para. 40 (emphasis added).

[33] *General Chemical Canada*, *ibidem*, at para. 21.

[34] *General Chemical Canada Ltd.*, *Re*, 2007 ONCA 600, O.A.C. 385. *General Chemical Appeal.*

[35] *Environmental Protection Act,* R.S.O. 1990, c.E.19.

[36] *General Chemical Appeal*, *supra* note 35 at para. 43.

[37] *General Chemical Appeal*, *ibidem*, at para. 46.

to enforce. The Court went on to hold that MOE was merely an unsecured creditor — albeit one that had security over the debtor's real property, as provided for in the BIA.[38] As such, the interim receiver was allowed to proceed with distributing the assets of the estate.

Before reaching the facile conclusion that the Canadian approach favours past cleanup, while the American approach is better suited to protect unaddressed contamination, let us provide a few complicating factors. First, the inability of a liquidating American debtor to abandon contaminated property is of little consequence if the debtor has no ability to pay to clean up the property. Second, the Canadian super-priority lien is simply that — a super-priority lien in a contaminated property. The ability to foreclose on such a property is unlikely to be attractive.

Thus, the utility of each of these protections is apt to turn on the debtor's need for the contaminated property, and the environmental claimant's ability to turn that need into leverage in the reorganization process. But as we discuss in the next section, new developments in corporate reorganization practice in both the U.S. and Canada tend to undermine this power.

II. Involuntary creditors in the "new" corporate bankruptcy

Traditional corporate reorganization involves the acceptance of a plan by creditors, with a concomitant reduction of the debtor's fixed claims and realignment of its operations. In the United States, this process is facilitated by an automatic stay of actions against the debtor,[39] and a similar stay is typically entered in Canadian CCAA proceedings.[40] In chapter 11 unsecured creditors are typically represented by a committee,[41] while in CCAA this role is taken up by the monitor.[42] The debtor formulates a plan, and the creditors then vote on the same.[43] After the creditors approve the plan, the court will consider the plan and, if it meets the provisions of the statute, sanction it and it becomes binding on all claimants.[44]

38 *General Chemical Appeal*, *ibidem*, at para. 47.
39 11 U.S.C. § 362.
40 CCAA, s. 11.03.
41 11 U.S.C. §§ 1102-1103.
42 CCAA s.11(7).
43 CCAA, s. 6(1); 11 U.S.C. §§ 1121, 1126.
44 CCAA, s. 6(1); 11 U.S.C. § 1129.

This traditional form of corporate bankruptcy is increasingly rare in larger corporate insolvency cases.[45] Instead, debtors utilize their power to sell their assets first, and then proceed to formulate a plan that distributes the sale proceeds to creditors.[46]

Take, for example, the well-known case of Lehman Brothers. The Lehman holding company filed under chapter 11 in New York on September 15, 2008, and sold office buildings and the North American investment-banking business to Barclays one week later. It continues to work toward a plan that will distribute the proceeds of this and other asset sales.

This change in approach has been attributed to the growing power of secured lenders.[47] This is particularly true in the United States, where it is argued that secured lenders have learned the lessons of the Eastern Airlines case —an major airline case from the 1980s that is said to typify debtor control, and which ultimately resulted in the eventual liquidation of Eastern— and now understand how they can use their pre-bankruptcy power over the debtor's liquidity to control the chapter 11 process.[48]

But this is more a story of how, than why. Aside from the implicit benefits of avoiding a lengthy reorganization process,[49] the reasons for why this turn to quick sales has happened, and whether it benefits anyone besides the senior lenders, is still open to debate.[50] And some argue that the trend is affirmatively harmful to the goal of maximizing the value of the debtor.[51]

The nearest thing to a normative justification for quick sales has been Baird and Rasmussen's argument that current American chapter 11 debtors generally lack substantial debtor-specific value, and thus sale of these

[45] Ben-Ishai & Lubben, supra note 6. *See also In re Chrysler*, 576 F.3d 108, 115 (2d Cir. 2009), citing Douglas G. Baird & Robert K. Rasmussen, "The End of Bankruptcy", 55 *Stan. L. Rev*., 2002, 751, 751-52, vacated as moot, 130 S.Ct., 2009, 1510.

[46] CCAA. s. 36; 11 U.S.C. § 363. *See* Stephanie Ben-Ishai, *Bankruptcy Reforms: 2008*, Toronto, Thomson Carswell, 2008, at 59.

[47] Westbrook, Jay Lawrence, "The Control of Wealth in Bankruptcy", 82 *Tex. L. Rev*., 2005, 795.

[48] See, e.g., Douglas G. Baird & Robert K. Rasmussen, "The End of Bankruptcy", 55 *Stan. L. Rev*., 2002, 751.

[49] *But see* Lynn M. LoPucki and Joseph W. Doherty, *Professional Fees in Corporate Bankruptcies: Data, Analysis, and Evaluation*, Oxford University Press, 2011 (finding that §363 do not actually cost much less in terms of professional fees).

[50] Lubben, Stephen J., "The 'New and Improved' Chapter 11", 93 Ky. L. J., 2005, 839; *See also* George W. Kuney, "Hijacking Chapter 11", 21 *Emory Bankr. Dev. J*. 19, 2004, 111.

[51] LoPucki, Lynn M. and Doherty, Joseph W., "Bankruptcy Fire Sales", 106 *Mich. L. Rev*., 2007, 1.

assets is apt to realize as much as any reorganization of the same.[52] This "no harm, no foul" argument was very likely a product of the specific time when Baird and Rasmussen wrote their papers: during the early part of this century the American bankruptcy system was still dealing with the remnants of the "tech bubble" of the late 1990s, meaning that many debtors of that era had fewer fixed assets than before, and, as we now know all too well, there was also a simultaneous credit bubble that allowed for purchasers to easily finance the acquisition of distressed assets, which no doubt reduced the risk that quick sales would result in reduced prices.[53]In this paper we present a new justification for quick sales that turns on the presence of involuntary creditors, especially environmental claims. Especially in the United States, as we develop further below, the existing case law on environmental claims in reorganization proceedings strongly encourages the breakup of the firm: with untainted assets transferred to a new owner, while the old debtor liquidates the contaminated property along with a distribution of the sale proceeds.

In Canada a similar set of issues are at stake, although the law is less developed on this point, especially since the asset sale provision of the CCAA is relatively new, its current form only coming into being with the 2009 reforms to the CCAA. In the past, without any express provisions dealing with asset sales in the CCAA, Canadian courts relied on their powers to impose terms and conditions under a stay order.[54]

The tendency to move toward sales as opposed to reorganization plans is driven by two related factors: the focus on environmental obligations' status as "claims," and the development in both chapter 11 and the CCAA of a strong ability to sell assets "free and clear" of charges on those assets.

The question of whether an environmental obligation is a claim has been particularly significant in the United States, but the apparent victory of environmental regulators on this point is apt to be hollow, for it depends on the debtor's continued operations post-insolvency. And the growing strength of sale orders, transferring assets free and clear of obligations, means that the debtor and its controlling creditors are increasingly unconcerned about the ability to obtain a discharge at the end of the reorganization process. As the discharge losses it significance, the power of involuntary creditors is apt to dwindle.

[52] Baird, Douglas G. and Rasmussen, Robert K., "Chapter 11 at Twilight", 56 Stan. L. Rev., 2003, 673.

[53] Harvey R. Miller & Shai Y. Waisman, "Is Chapter 11 Bankrupt?", 47 *B. C. L. Rev.*, 2005, 129, 156.

[54] Under s.11 of the CCAA.

1. *Environmental "Claims"*

The U.S. Bankruptcy Code provides that the confirmation of a chapter 11 plan "discharges" the debtor from any debt —defined as "liability on a claim"— that "arose" before the date of confirmation.[55] A "claim" in turn is defined to include both a "right to payment" and a "*right to an equitable remedy for breach of performance if such breach gives rise to a right to payment*."[56] Under the Bankruptcy Code, a discharge "*operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor*".[57]

In the environmental context, a court must therefore determine whether an obligation for environmental cleanup liability constitutes a pre-petition "claim".[58] As noted, the result of more than thirty years of litigation tells us the pre-bankruptcy obligations to pay for past cleanup are dischargeable,[59] so long as the discharge comes after the enactment of the relevant environmental statute,[60] while the duty to comply with environmental regulatory laws and cleanup currently contaminated property is not dischargeable.[61] Thus cleanup obligations imposed on owners of contaminated land under CERCLA run with the land and will not be discharged in bankruptcy.[62]

In Canada, both the BIA and CCAA establish that environmental claims constitute "provable claims" in bankruptcy. Specifically, under s.14.06(8) of the BIA and s.11.8(9) of the CCAA, a claim against the debtor company for the costs of remedying any environmental conditions or environmental damage affecting real property or an immovable of the debtor shall be a provable claim, regardless of whether the condition arose or the damage occurred before or after the date of the filing under which proceedings were commenced under both those Acts.[63]

55 11 U.S.C. § 101(12).

56 11 U.S.C. § 101(5).

57 11 U.S.C. § 524.

58 Frank, Robert P., "*Liability without end? The discharge of CERCLA liability in bankruptcy after Atlantic Research*", 21 *Fordham Envtl. L. Rev.*, 2010, 559, 564-66.

59 *Ohio v. Kovacs*, 469 U.S. 274, 1985. *See also Boston and Maine Corp.* vs. *Mass. Bay Transp. Auth.*, 587 F.3d 89, 1st Cir., 2009.

60 *In re Penn Central Transportation Co.*, 944 F.2d 164, 3d Cir., 1991.

61 *In re Torwico Electronics, Inc.*, 8 F.3d 146, 3d Cir., 1993.

62 *In re CMC Heartland Partners*, 966 F.2d 1143, 7th Cir., 1992.

63 BIA, *supra* note 11 at s.14.06(8); and CCAA, *supra* note 11 at s.11.8(9). See also, *General Chemical Canada Ltd., Re*, 2007 ONCA 600, 228 O.A.C. 385 at para. 46.

The provability issue was explored in *Newfoundland and Labrador* vs. *Abitibibowater Inc.*,[64] where the topic of environmental cleanup costs was broached by the Quebec Court of Appeal. Here, the Minister of Environment and Conservation of Newfoundland and Labrador issued five ministerial orders ("EPA orders") against the debtor, mandating the complete environmental remediation of sites where it had conducted large-scale industrial activities.[65] At the time when the orders were issued, however, the debtor had already filed for protection under the CCAA. A claims procedure order was then made, directing the debtor's creditors to file their proofs claim by the claims bar date. In response, the province argued that the statutory duty to remediate contaminated property could not be considered a "claim" under the claims procedure or the CCAA; thus, the EPA orders were not affected by the claims bar process. However, the provincial superior court and court of appeal both dismissed the province's motion. Most recently, the Supreme Court of Canada granted the province leave to appeal in this matter.[66]

In the US, non-dischargability of environmental orders means that orders to clean up property can continue to be enforced during,[67] and after the debtor's reorganization case. [68]Moreover, as an ongoing obligation, the duty to remediate may be entitled to be characterized as an expense of administering the reorganization.[69] Under chapter 11, such expenses must be paid in full, in cash before a reorganization plan can be confirmed by the court.[70]

In Canada, this is not necessarily the case. Rather, Canadian courts have held that environmental cleanup costs can be compromised during the restructuring process, and therefore do not have to be paid in full before a plan of arrangement or compromise can be approved the court. For example, in *AbitibiBowater Inc.*, *Re*,[71] the Quebec Court of Appeal upheld a lower court decision that provincial environmental claims against the debtor were

64 *Newfoundland and Labrador* vs. *Abitibibowater Inc.*, 2010 QCAA 965 [*AbitibiBowater Appeal*].

65 *AbitibiBowater Appeal*, *ibidem*, at para. 10.

66 *Newfoundland and Labrador v. Abitibibowater Inc.*, [2010] S.C.C.A. 269.

67 *Safety-Kleen, Inc.* vs. *Wyche*, 274 F.3d 846, 4th Cir. 2001; *United States* vs. *Nicolet, Inc.*, 857 F.2d 267, 3d Cir., 1988.

68 *Chateaugay Corp.* vs. *LTV Corp., In re Chateaugay Corp.*, 944 F.2d 997, 2d Cir. 1991. *See also U.S.* vs. *Apex Oil Co., Inc.*, 579 F.3d 734, 7th Cir., 2009, cert. denied, WL 752322, 2010.

69 *In re Wall Tube* and *Metal Products Co.*, 831 F.2d 118, 6th Cir., 1987. The "actual, necessary costs and expenses of preserving [the] estate," are entitled to administrative expense status and have a first priority in payment. 11 U.S.C. §§ 507(a)(1), 503(b)(1)(a).

70 11 U.S.C. §1129(a)(9)(A).

71 *AbitibiBowater Inc. Re*, 2010 QCCA 965, 68 C.B.R. (5th) 57 [*AbitibiBowater Appeal*].

simply financial in nature and should therefore be treated as ordinary claims under the CCAA, which are subject to compromise under the Act.

In that case, the debtor —Abitibi— was one of the world's largest publicly traded pulp and paper companies, and had carried on industrial activities at several locations in Quebec.[72]Shortly after the debtor filed under the CCAA,[73] the province, pursuant to the *Environmental Protection Act*, issued several ministerial orders requesting the company perform remediation on the land the where the company had carried on industrial activities. The province brought a motion seeking a declaration that the orders were not affected by the CCAA proceedings and not stayed the initial order under the CCAA.[74] Yet, the judge who heard the motions hearing held that the orders were financial in nature and should therefore be treated as claims under the CCAA and subject to compromise.[75] The province appealed this decision, but the appellate judge upheld the motion judge's findings, holding that his decision did not immunize the company from compliance with environmental orders; rather, his decision merely characterized them in the context of the restructuring process engaged pursuant to the CCAA.[76] Although this case did not specifically touch on the ability to discharge environmental claims under the CCAA, the Court's insistence that these claims be treated as any other financial claims under the Act —and be subject to compromise accordingly— hints that these claims would also be discharged in the same manner as other financial claims under the Act. The manner in which environmental remediation claims are treated in Canada is distinct from the way they are dealt with in the U. S., insofar as these claims do not necessarily have to be paid in full in Canada.

In short, having won the battle to determine that environmental obligations are not pre-bankruptcy "claims," environmental regulators in the U. S. seemly obtained a privileged position for these types of involuntary claims. The claims continue to be enforceable against the debtor, despite the bankruptcy, and must be paid in full before the debtor can leave chapter 11.[77]The

[72] *Ibidem*, at paras. 2-3.

[73] *Ibidem*, at paras. 4, 7.

[74] *Ibidem*, at paras. 14-15.

[75] *Ibidem*, at para. 22.

[76] *Ibidem*, at para. 33.

[77] *In re General Motors Corp.*, 407 B.R. 463 at 505 (Bankr. S.D.N.Y. 2009), "the purchaser would have to comply with its environmental responsibilities starting with the day it got the property, and if the property required remediation as of that time, any such remediation would be the buyer's responsibility".

situation is more uncertain in Canada and *Abitibi* suggests that such claims would not continue to be enforceable against the debtor.

But this assumes that the debtor's goal is to leave reorganization and resume normal operations, and that the only way to do that is at the end of its case. But a sale of the debtor's assets to a new entity —less any contaminated assets— can achieve the same result, without implicating the "victory" environmental regulators seemingly won when they avoided having their claims subjected to the bankruptcy process.

Indeed, it would seem that American environmental regulators placed too much focus on the continued existence of the debtor as a specific legal entity. The ability to assert an administrative claim that is entitled to be paid in full only matters if the debtor intends to propose a plan, and the ability to assert a claim against the debtor after bankruptcy only works if the debtor will be around after bankruptcy.

But if the debtor can achieve the equivalent of reorganization by selling its uncontaminated assets to a new legal entity, that will quickly adopt the debtor's old name, then there is no need to follow all the steps of a traditional reorganization. Instead, the debtor will happily leave the remnant bits of its former self to face liquidation or even abandonment.

The key to the debtor's ability to do this turns on the CCAA and Bankruptcy Code's provisions providing for sales "free and clear" of prior claims, which we turn to next.

2. *Sale as a Discharge Substitute*

If a debtor stays largely intact during its reorganization, the scope of its discharge at the end of the CCAA or chapter 11 process is key. But if the debtor sells most of its assets, discharge wanes in importance. And if the debtor can create a new entity to buy its assets, then the distinction between "normal" reorganization and sale vanishes from an operational perspective, and the only question is which process better rids the assets of past errors, thus maximizing the value of the same.

Outside of reorganization, the general rule is that an asset sale does not result in a transfer of liabilities, unlike a merger.[78] But several other doctrines limit the general rule. For example, in many jurisdictions in the United States, courts have developed successor liability doctrines that lead to continued liability for a purchaser for products defects. Moreover, a

[78] Compare Delaware General Corporation Law §271 with §253.

buyer outside of reorganization takes subject to the risk that the transaction will be challenged ex post as a fraudulent transfer, if the debtor is deemed to have sold its assets "too cheap."

Thus, in the chapter 11 or CCAA sale context, the vital feature of reorganization law is the ability to sell assets free and clear of claims to the buyer. For example, section 363(f) of the Bankruptcy Code authorizes the trustee or a debtor in possession to sell property of a debtor "*free and clear of any interest in such property*". An interest in property includes "claims" that arise from the assets being sold.

Essentially, § 363(f) authorizes the bankruptcy court to grant relief similar to the discharge enjoyed by debtors under the Code, exonerating a buyer from successor liability, including liability for the debtor's environmental claims that are unrelated to the purchased assets. The CCAA allows for similar protection, authorizing a court to order that the property be sold to the purchaser free and clear of charges, liens and restrictions.[79]

This includes the environmental claims that the debtor owes, so long as the purchased assets do not include contaminated assets. Thus, General Motors sold its "good' assets to a newly created company and its surviving business is now free of any obligations for its formerly owned contaminated properties. Creditors could file claims in the bankruptcy case and perhaps get small distributions, but the new company called GM is free of these obligations.[80] Accordingly, it is possible —as long as the debtor company does not sell its contaminated property— for a debtor subject to environmental claims to effect a sale of its assets, largely free and clear for charges liens and restrictions.

In Canada, this has been held to mean that an interim receiver can distribute the assets of the debtor's estate, as long as those assets are business assets, as opposed the real property subject to contaminated-related liens by the federal or provincial government. For instance, as discussed earlier, in *General Chemical*, the Ontario Court of Appeal examined the issue of selling the debtor's assets when they are subject to an environmental claim.[81] Here, the interim receiver sought approval for a sale of the debtor's assets, while the MOE opposed the distribution on the grounds that the debtor had contaminated the site of one of its plants, and the remediation costs for cleaning up this contamination were estimated to be quite high; ac-

79 CCAA, s. 36(6).

80 The US EPA filed a claim for more than $2 billion in the "old" GM chapter 11 case.

81 *General Chemical Canada Ltd., Re* 2007 ONCA 600, 228 O.A.C. 385.

cordingly, the province was anxious to have the assets of General Chemical available to pay for this clean up.[82]

However, in this instance, the assets that the receiver was looking to sell were those from the operation of debtor's business and not the debtor's contaminated real property, over which the province has super-priority under the *BIA* and *CCAA*. As such, the court held that the province did not have a security interest in General Chemical's operating assets.[83] Accordingly, the sale of the debtor's assets was allowed on the facts of this case.

In contrast, part of the *AbitibiBowater* case dealt with the sale of several contaminated waste disposal sites. In a factum by the Province of Ontario, submitted to the Quebec Superior Court, the province opposed Abitibi's motion for an order authorizing the sale of these contaminated sites, on the basis that it was not in the public interest to do so.[84] Specifically, the Province argued that the sale was contrary to the public interest since the effect of the sale would be to authorize the debtor to shed its regulatory environmental responsibilities in respect of its waste disposal sites; moreover, the Province alleged that there was no evidence that if the sale was disallowed that the CCAA reorganization of Abitibi would fail. This is important in light of the fact that section 36 of the CCAA now requires a debtor company to obtain the authorization of a court before selling its assets outside of the ordinary course of business; one of the key factors to be considered by the court is making such a determination is "*the effect of the proposed sale or disposition on the creditors and other interested parties,*" including the public.[85] Accordingly, this factum not only hints that the test upon which asset sales should be judged is whether, if denied, there is a reasonable prospect that the restructuring will fail; the Province's claims also imply that there should be a distinction between the sale of real property and the sale of operating assets when a debtor is subject to environmental claims.

Notice, however, that this case reverses the typical structure, particularly in the United States, where the debtor wants to sell everything but the contaminated property. In such a situation, the environmental claimant has two options: object to the sale or seek to obtain a priority claim against the sale proceeds. The first strategy is often the reflexive position of environmental claimants, but is only useful if the claimant considers the question of what will happen if it succeeds. In particular, blocking

[82] *General Chemical*, *ibidem*, at para. 38.

[83] *General Chemical*, *ibidem*, at para. 42.

[84] *In the Matter of the Plan of Compromise or Arrangement of AbitibiBowater Inc.* (Court File No. 500-11-036133-094) at paras. 1 and 2 [*Abitibi Factum*].

[85] *Abitibi Factum, ibid.* at para. 14; and CCAA, s. 36.

a sale to force a liquidation of the debtor is both socially inefficient and unlikely to benefit the objecting claimant. The second strategy, seeking priority access to the sale proceeds, will likely place the environmental creditor in competition with senior, secured creditors. Both these strategies are examined in the larger context of modern corporate reorganization practice, in the next part of the paper.

III. Adjusting to the New Reality

If debtors with environmental obligations and other involuntary obligations increasingly turn to quick sales to realize the value of their assets, then strategies designed to exempt environmental claims and other involuntary debt claims from the bankruptcy or insolvency process are no longer viable. Environmental claimants and other involuntary creditors will increasingly have to work within the insolvency system to protect their interests. Any attempt by the judiciary to continue to operate under the "old regime" will distort the current framework and have significant implications for the lending market as well as the ultimate objective of maximizing value available to all creditors.

But before proceeding, it makes some sense to consider if the solution to the problem of involuntary creditors under a regime of quick sales might not be addressed by simply prohibiting quick sales or limiting them to cases were the debtor's assets are literally perishable, an idea that traces back to the United States Bankruptcy Act of 1867 and was the rule in the United States before the enactment of the current Bankruptcy Code in 1978: pre-plan assets sales were only permitted in cases involving debtors with inventory of dairy products or vegetables, or where some other similar factor prevented the debtor from selling the assets as part of a full plan.[86]

Such a rule might make sense if we assume that the bulk of the current quick sales are substitutes for full reorganization cases. If, however, many current quick sales substitute for liquidations, the desirability of such a rule becomes rather suspect. And for a court faced with a debtor that asserts it will have to liquidate if it does not sell key assets quickly, the question of which type of debtor this might be is fraught with serious consequences, particularly if the court guesses wrong. Moreover, adopting a blanket rule against quick sales without understanding the larger empirical question of which type of debtor predominates would seem to be equally problematic.

[86] *In re Solar Mfg. Corp.*, 176 F.2d 493 (3d Cir. 1949); *In re V. Loewer's Gambrinus Brewery Co.*, 141 F.2d 747, 2d Cir., 1944.

In this context, we argue that the naïve solution of preventing quick sales is unlikely to prevail, and creditors, including involuntary creditors, thus need to adapt to the new reality.[87]And the reorganization process itself needs to adapt to ensure that the process is being used to maximize the value of the debtor's assets, and not merely to transfer wealth among claimants.

To understand the necessary adaptions, it helps to begin with an exposition of precisely how a reorganization scheme based around quick assets sales could harm involuntary creditors. It is not a harm to creditors, voluntary or involuntary, that a sale results in little or no recovery for unsecured creditors, or shareholders. Rather the key issue is whether the sale results in the realization of less value by junior claimants than a traditional reorganization or liquidation.

A sale thus could result in the realization of equal value, but see that value diverted to senior creditors. This is a problem of redistribution. Some of the more nefarious versions of this problem have already been well ventilated in the literature, particularly in the United States. Thus, there is real concern that the sale process might facilitate collusion between management and senior creditors to squeeze out junior creditors and shareholders.

But the sale process also reduces the holdout powers that junior creditors have in a more formal reorganization. For example, a chapter 11 plan can only be confirmed —even under the "cramdown" power that allows plans to overcome creditor objections— if the plan has been accepted by one class of impaired creditors.[88] A plan that pays secured creditors in full but leaves unsecured creditors with little or nothing might be rejected by the unsecured creditors, leaving the plan without an accepting impaired class.[89] But the same transaction conducted as a sale could well be approved over the objection of creditors.

Similarly, if a clean-up obligation is a post-petition "administrative claim," the claimant has the right to demand payment in full before the debtor's plan can be confirmed.[90] On the other hand, it is possible for the debtor to sell its assets without providing for full payment of administrative claims — although conversion to chapter 7 or dismissal of the case might be a likely result post-sale.

[87] See Stephen J. Lubben, "No Big Deal: The GM and Chrysler Cases in Context", 83 *Am. Bank. L. J.*, 2009, 531, 535-538.

[88] 11 U.S.C. §1129(a)(10).

[89] 11 U.S.C. §1126(f).

[90] 11 U.S.C. §1129(a)(9).

In both instances, the junior creditors loose power, and thus value, by the move from plans to sales. It may be that from a policy perspective the value junior claimants loose in these latter examples result in a net efficiency gain — for example, if the junior creditors' right to impede a plan is nothing more than the power to extort rents for senior creditors, the ability to sidestep the holdup power through a sale is a good thing.

But a system of corporate reorganization is a system of checks and balances, and one should be hesitant to throw away one of those checks on the simple grounds of expediency. Whether the junior creditors are simply extracting value they are not entitled to, or whether they are putting the stop to senior creditor overreaching, is an unanswered empirical question. And while some junior creditors can price senior creditor expropriation ex ante, involuntary creditors like environmental claimants cannot.

At this point it is also important to consider efficiency from a somewhat broader perspective than is typical in much of the bankruptcy literature. In particular, while a particular creditor's decision to block the debtor's plan might seem inefficient within the internal context of insolvency law, from a broader societal perspective it might be that reorganization in the face of unpaid and unaddressed environmental claims is actually overall inefficient. At the same time, and as will be discussed more fully below, it might be that these larger issues are better served in some way other than a power to block the debtor's reorganization.

A sale might also result in lost value if the structure of the sale is such that is depresses the value of the debtor's assets. For example, if the sale is rushed or conducted in a way that discourages competitive bidding, the sale might not realize full value for the claimants. Value is not being redirected, rather it is simply lost to the parties to the reorganization. Presumably the buyer of the assets realizes the value by obtaining a bargain price.

Senior lenders arguably do not have an incentive to control this issue unless the structural problems are so severe that they threaten senior claimants' recoveries.[91]However, it is important in this context to distinguish between depressed value that results from generally distressed asset prices in the industry, as opposed to debtor-specific asset price depression caused by the sale itself.

The senior lender's ability to "credit bid" their secured claim as sale consideration will provide some check against a sale that undervalues the

[91] A. Mechele Dickerson, "Words That Wound: Defining, Discussing, and Defeating Bankruptcy *Corruption*", 54 *Buff. L. Rev.*, 2006, 365, 370 n. 14.

debtor,[92] but it also suggests that in some cases the distinction between value diversion and value loss will be hard to perceive. If the debtor sets up a faulty sale process, that allows the senior lender to take the debtor's assets at a discount, the two flavours of sale problems meet in the middle.

Thus an involuntary creditor, like an environmental claimant, needs to consider two related types of harm that comes from the use of a sale in place of a plan: the sale to an outsider at less than full value and the sale to the senior creditor at less than full value. An involuntary creditor might also worry about their loss of holdup power, and that is a concern if that power prevents socially inefficient asset transfers.

In the latter case, the inefficiencies primarily arise from the debtor externalizing the cost of its environmental contamination. The beneficiary of this is primarily the senior lenders, who receive the sale proceeds.

This suggests that Canada might be on the right track when it provides environmental claims with a superpriority. But maybe it does not go far enough. In particular maybe the superpriority claim needs to be against the debtor's enterprise, rather than the particular piece of contaminated property. And note that such a superpriority works even in cases where the lender is oversecured and would otherwise be inclined to underinvest in monitoring the debtor, since the superpriority puts the lenders' equity cushion at risk.

But broad notions of enterprise liability are probably more apt to be academic than real, especially given the threat any such argument would pose to asset-backed securitization.[93] The United States might consider adopting at least the Canadian version of the superpriority rule.

And there might be some room to construct a middle-ground mechanism to address the issue of unpaid environmental liabilities in the corporate group. For example, under US banking law, regulators have the power to require financial distressed banks to obtain contractual capital commitments from their parent companies.[94]These agreements, which imposed fixed potential liabilities on the parent company are then subject to special priority status in the parent's subsequent bankruptcy case.[95]A similar model might work with regard to environmental claims.

[92] 11 U.S.C. §363(k).

[93] An insurance or bonding scheme might also seem like an obvious solution, but we worry that such a system is subject to the same information constraints that prevent an involuntary creditor from pricing the risk of non-payment in the first instance. Only an over-inclusive insurance or bonding requirement would seem able to overcome this problem.

[94] 12 U.S.C. §1831o(e)(2).

[95] 11 U.S.C. §507(a)(9).

Adopting an expanded version of the Canadian superpriority or contracting for parent-company liability takes care of the problem of debtors that transfer value from environmental claimants to senior lenders, but there remains the problem of debtors who sell their assets too cheaply. This latter effect amounts to a transfer from junior creditors, including any involuntary creditors who do not benefit from a superpriority.

It can be expected that banks and other financial institutions will argue that a broadening of the superpriority —or the creation of it, in the case of the United States— will discourage lending to companies that have any connection with environmental pollution. But in part that is exactly the point: make companies internalize the cost of they impose on involuntary creditors, like environmental claimants. This issue was front and centre with respect to a different type of involuntary creditor —pension claimants— in a recent Ontario Court of Appeal decision.

Re Indalex Limited[96] concerned a cross-border proceeding where Indalex filed for CCAA protection in Canada and Indalex's parent companies and US based affiliates sought Chapter 11 protection in the US. The Canadian company was sold through a quick sale in the CCAA proceedings but the sale proceeds were insufficient to repay the DIP lenders. The US parent company covered the shortfall, in accordance with its obligations under a guarantee. At issue in the Court of Appeal decision was who as between the US parent company and the pension plan beneficiaries could claim the money from the sale proceeds held by the monitor in a reserve fund. The US parent claimed the funds based on its payment under the guarantee and the pension plan beneficiaries claimed the money based on deemed trust provisions in the provincial pension legislation.

Justice Gillese concluded that the deemed trust continued to operate under provincial law and stood ahead of the DIP lenders super-priority. In addition, she held that the employer had breached its fiduciary duties by wearing two hats as administrator of the pension plans with fiduciary duties to the pension plan beneficiaries and also as a corporation with a duty to act in the best interests of the corporation. The remedy for this breach was a constructive trust in favour of the pension plan beneficiaries.

In rendering her decision in *Indalex*, Justice Gillese was not prepared to address the issue of adapting to the new corporate reorganization model of quick sales and the impact of expanding priority for involuntary creditors in this context. She observed that the case concerned a liquidating CCAA and that there was no restructuring of the company. However, she was not

[96] 2011 ONCA 265 ("Indalex").

prepared to consider how such a reality should be taken into account in dealing with unpaid pension obligations.

Leave to appeal to the Supreme Court of Canada is currently being sought from *Indalex*. Already comments from number of the top Canadian law firms suggests that lending has been impacted by the decision and deals have been put on hold.

While Justice Gillese is convinced that Canadian corporate law duties force directors of a corporation on the cusp of a CCAA filing to consider the broader societal like concerns, she does not propose solution for how the uncertainty around super-priority created by her decision can be dealt with. That is, even CCAAs that result in quick sales require a DIP lender to fund the process.

A better point in time to consider whether and how a quick sale will impact involuntary creditors, like the pension claimants in *Indalex*, is the new section 36 process for approval by the court of a quick sale. Priorities need to be clear and not altered on a case-by-case basis.

More generally, to the extent there exists a gap between the private, internal efficiency of reorganization case and questions of social efficiency, which are of sufficient nuance that they can not be addressed by statute ex ante, there needs to be a mechanism to place such questions before court. This is one area where the Canadian monitor, who is no beholden to any particular stakeholder in the case, might provide a better tool than its American counterpart. Specifically, it cannot be expected that a creditors committee will consider issues beyond the class it represents.

On the other hand, consideration has to be given to the structure of the sale process itself. In particular, safeguards have to be in place to protect against collusion between the debtor's management and senior lenders. In this regard, the tendency to subject deals to "higher and better" offers, much more common in the United States than Canada, is a step in the right direction. But there is still a need for vigilance against sale structures that are auctions in name only.

IV. Conclusion

We have identified three key issues that must be dealt with in the context of the treatment of involuntary creditors and the new reality of quick sales in reorganizations under the CCAA and Chapter 11:

a) Involuntary creditors loose the ability to object;

b) Quick sales may result in lost value that could have gone to involuntary creditors; and

c) Broader issues of efficiency and externalities.

As we have already suggested, the appropriate response to these concerns must be clear and consistent and not result in uncertainty around priorities of voluntary creditors. The following responses may be considered:

a) The monitor or the US creditor committees may be a proxy for the lost voice of involuntary creditors. In addition, representative counsel, appointed by the court and paid for by the estate of the debtor may fulfill this role.

b) The requirement of an auction in "non-emergency" situations to ensure that value is not lost that could potentially have gone to the involuntary creditors.

c) The requirements that the public interest is considered in the section 36 sale process test may serve as an example of how externalities and broader efficiency related issues may be considered at an early stage in the process.

THE BANK'S FIDUCIARY DUTY: THE EVOLUTION OF THE DOCTRINE OVER THE LAST 30 YEARS

Ruth PLATO-SHINAR*

SUMMARY: I. *The Bank's Fiduciary Duty: Historial View*. II. *The Evolution of the Bank's Fiduciary Duty – The English Model*. III. *The Evolution of the Bank's Fiduciary Duty – The Israeli Model*. IV. *The Need For Harmonization*.

I. THE BANK'S FIDUCIARY DUTY: HISTORIAL VIEW

The concept of imposing a fiduciary duty in commercial contexts is an ancient idea rooted in Roman law and even in the legal systems that preceded it.[1] However, the main development of the idea is connected to the changes that the modern post-industrial society underwent, and to the development of the free professions. These processes led to a fundamental change in the structure of businesses and in the manner of their activities; and as a result thereof — to a change in the nature of the relationship between service providers and their customers.[2]

In the past, service providers were individuals, familiar to their customers. The business domain of the service providers was limited and understood by the customer. The connection between the service provider and the customer was personal, based on their familiarity. But, in the twentieth century, a new phenomenon began to develop: the creation of business corporations for the purpose of providing services, including multi-functional companies

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1 Tamar Frankel, *Fiduciary Law*, Fathom, 2008, chapter 1.

2 Tamar Frankel, "Fiduciary Law", 71 *Cal. L. Rev.*, 1983, 803-804.

that supplied services in many different fields. These business corporations, in order to perform their functions and as a result of their size, incorporated sophisticated technological means. This technological development increased the ability of these corporations to acquire, store and reproduce information, including information regarding their customers. All of this led to a growing volume of customers, who, mostly, were not personally known to the corporation's employees, and did not receive personal service. As a result, not only the structure of these businesses and their nature of operation changed, but also the nature of their relationship with their customers.[3]

The processes described above are important to society, because they both promoted individual welfare and increased the efficiency of resource allocation. On the other hand, these processes have led to some basic problems: the creation of new forms of power and the gradual strengthening of this power in the hands of the service providers; the increase of conflicts between the service providers and their clients, or between different clients; the placement of trust and reliance by customers in the service provider, who is perceived by them as an expert, acting professionally in their best interests; the dependency of the individual on the service provider and, as a result, his vulnerability that could possibly be exploited by the service provider.[4]

The appropriate way to deal with all these problems is to impose a legal obligation on the service provider, to act in favor of the client and to protect his interests, especially in situations where the service provider has an incentive to exploit its power to the detriment of the client. This legal duty is the fiduciary duty.

This article will deal with the fiduciary duty imposed on a particular service provider — the commercial bank, when providing core banking services to its clients.

The bank's fiduciary duty, whenever it is applied, sets a very high standard of conduct for the bank. The bank is obliged to act with integrity and fairness. It must also act with professionalism and skill. However, beyond that, the fiduciary duty is underpinned by the duty to exercise its power and authority without abusing them. The key words are loyalty and fidelity. The bank 'as a fiduciary' is required to perform its duties solely for the purpose for which the power was vested in it, without ulterior motives and while protecting the interest of the beneficiary — the customer. The bank must act for

[3] Paul D. Finn, "Fiduciary Law and the Modern Commercial World, in E. McKendrick (ed.), *Commercial Aspects of Trusts and Fiduciary Obligations*,1992, 19 and 20.

[4] Frankel, supra note 2, *ibidem*.

the best interest of the customer. Moreover, the bank must prefer the interest of its customer to the interests of others, including its own self-interest. Obviously, this is an onerous duty which is difficult to put into practice.[5]

These characteristics of the bank's fiduciary duty are common to the various legal systems that impose such a duty on the banks. But there are remarkable differences between different legal systems, as to the implementation of this duty. Over the past decades, and especially during the last 30 years, various models of the bank's fiduciary duty have been developed in the different jurisdictions.[6]

The article will deal with two models that reflect opposite trends: The English model, under which the concept of the bank's fiduciary duty became very narrow over the years; and the Israeli model, under which the duty is applied extremely broadly.

II. The evolution of the bank's fiduciary duty – The english model

Under the English model, which applies in England, Canada, and other states that adhere to the common law system, the banker-customer relationship is not considered to be a fiduciary relationship.[7] Nevertheless, the English courts are willing to impose a fiduciary duty on the bank under certain factual situations and circumstances, as discussed below.

1. *Investment Advice*

The main category in which the fiduciary relationship has been recognized is where the bank assumes the role of the customer's advisor, for

[5] Plato-Shinar, Ruth, "The Bank's Fiduciary Duty under Israeli Law: Is there a need to transform it from an Equitable Principle into a Statutory Duty?", 39 *CLWR*, 2012, 219, 220-221. Plato-Shinar, Ruth, "An Angel named 'The Bank': The Bank's Fiduciary Duty as the basic Theory in Israeli Banking Law", 36 *CLWR*, 2007, 27, 29-30. Plato-Shinar, Ruth, *The Bank's Fiduciary Duty – the Duty of Loyalty*, Israel, Bar Publishing House, 2010, 71-77.

[6] Plato-Shinar, Ruth, "The Bank's Fiduciary Duty: An Israeli-Canadian Comparison", 22 *BFLR* 1, 2006. Plato-Shinar, Ruth and Weber, Rolf H., "Three Models of the Bank's Fiduciary Duty", 2 *Law and Financial Markets Rev*., 2009, 422.

[7] Ellinger, E. P. *et al*., *Ellinger's Modern Banking Law*, 5th ed., Oxford, Oxford University Press, 2011, 126, 129, 134. J. Wadsley, J. and Penn, G., *The Law Relating to Domestic Banking 107*, 2nd ed., London, Sweet and Maxwell, 2000. Chuah, J., "General Aspects of Lender Liability Under English Law", *Banks, Liability and Risk*, London, Informa Law, W. Blair ed., 2001, 40. In Canada: Ogilvie, Margaret H., *Bank and Customer Law in Canada*, Toronto, Irwin Law, 2007, 196. Crawford, Bradley, *The Law of Banking and Payment in Canada*, vol. 2, Thomson Reuters, Ontario, 2010, §§ 9-49.9, 9-99.

example when the bank provides investment advice.[8] The leading case in this category is Woods v Martins Bank, from 1958.[9] This case dealt with a simple and unsophisticated man who was persuaded by a bank to purchase shares in a company which had an overdraft at the bank, without disclosing this fact to the purchaser. The purchaser lost his investment, having relied entirely on the bank's advice, in the absence of any business knowledge, experience or common sense of his own. The court found that there was a relationship of trust between the parties, which resulted in the imposition of a fiduciary duty on the bank. By virtue of this duty, the bank was obliged to disclose its conflict of interest to the customer and, by failing to do so, it breached the fiduciary duty.

However, over the years and especially over the past 30 years, the English courts have adopted a much more reluctant approach. The courts have stressed that a fiduciary duty will be recognized only under special circumstances, such as where the customer actually reposed trust and confidence in the bank and relied on its advice; or where the bank actually knew that the customer was relying on its professional judgment; or where the bank was purporting to act in the best interests of the customer. A fiduciary duty may also exist where the customer is in fact accustomed to being guided by the advice of the bank. Another instance is the bank's undertaking to act on behalf of the customer and the customer's reliance upon this undertaking. The recurring motives in the case law are the relationship of special proximity between the parties; relationship of dependency; the customer's inferior-

[8] Ellinger *et al*., *ibidem*, at pp. 134-136. In Canada: Ogilvie, Margaret H., *Canadian Banking Law*, 2nd ed**.,** Toronto, Carswell, 1998, at p. 459-466; Ogilvie, *ibidem*, at p. 210-212; See mainly the judgments of Standard Investments Ltd. *v* C.I.B.C., 1984, 5 D.L.R., 4th, 452, Ont. H.C., revd., 1986, 22 D.L.R., 4th, 410, Ont. C. A.; Hodgkinson *v* Simms, 1994, S.C.J. No. 84, 117 D.L.R., 4th, 161, S.C.C.,; Scaravelli *v* Bank of Montreal, 2004,, 46 B.L.R., 3rd, 322, 69 O.R., 3rd, 295, Ont. S.C.J., In relation to the Standard Investment case, see Ogilvie, Margaret H., "Banks, Advice-Giving and Fiduciary Obligation", 7 *Ottawa L. Rev.*, 1985, 263; Bradely Crawford, "Bankers' Fiduciary Duties and Negligence", 12 *Can. Bus. L. J.*, 1986, 145; R. P. Austin, "The Corporate Fiduciary", 12 *Can. Bus. L. J.*, 1986, 96; Ziegel, Jacob S. "Bankers' Fiduciary Obligation and Chinese Walls: A Further Comment on Standard *v* C.I.B.C.", 12 *Can. Bus. L. J.*, 1986, 21; Marshall, John C., "The Relationship between Bank and Customer: Fiduciary Duties and Confidentiality", 1 *B.F.L.R.* 33, 1986. In relation to Hodgkinson *v* Simms, see Margaret H. Ogilvie, "Fiduciary Obligations in Canada: From Concept to Principle", *J. Bus. L.*, 1995, 638. McCamus, John D., "Prometheus unbound: Fiduciary Obligation in the Supreme Court of Canada", 28 *Can. Bus. L. J.*, 1997, 107. Smith, Lionel D., "Fiduciary Relationship Arising in Commercial Contexts – Investment Advice: Hodgkinson *v* Simms", *Can. Bar Rev*., 1995, 714. In relation to Scaravelli *v* Bank of Montreal, see Ogilvie, Margaret H., "Judicial Intuition and Bank Fiduciary Obligation: Scaravelli *v* Bank of Montreal", 21 *B.F.L.R.*, 2005, 89.

[9] Woods *v* Martins Bank, 1 Q. B. 1959, 55; 3 All E.R., 1958, 166; 1 W.L.R., 1958, 1018.

ity and vulnerability, and the bank's hegemony over the customer's affairs; etc. Whatever the special circumstances may be, the general impression is that they are essential for the recognition of a fiduciary duty.[10]

Another example for this restrictive approach is the Canadian case of *Hodgkinson v Simms*,[11] where it was ruled that the essential requirement for the imposition of a fiduciary duty with regard to investment advice is a voluntary undertaking by the advisor to act on behalf and in favor of the customer. Once it has been ruled that a fiduciary relationship arises only upon a voluntary undertaking of the bank, it is equally clear that the bank can expressly exclude or restrict its liability by contract, in such a way that its relationship with the customer would not include fiduciary duties.[12]

Lately, even circumstances such as those mentioned above have not always been enough to recognize a fiduciary relationship between the bank and the customer. In *JP Morgan Chase Bank* v *Springwell Navigation Corporation*,[13] it was ruled that "*the mere fact that one party to a commercial relationship "trusts" the other does not predicate a fiduciary relationship. The word "trust" …has a variety of meanings. In a broad sense, trust is an important element in many commercial dealings…*"[14] In the absence of a legitimate expectation that the bank would subordinate its interests to those of the customer, no fiduciary duty will be imposed.[15]

2. *Taking Collaterals*

Another category where a fiduciary duty has been recognized under English law is the taking of collaterals.[16] The leading case in this category used to be *Lloyds Bank Ltd. v Bundy*.[17] This case dealt with an old and simple man who pledged his house and farm to secure his son's business debts. The bank failed to disclose to the father the true state of his son's financial affairs, or to recommend that the father seek independent advice. A few months later, due to a deterioration in the son's financial situation, the bank enforced the security and sold the property.

10 Supra, notes 7 and 8.

11 Supra, note 8.

12 Ogilvie, supra note 7, at p. 197.

13 2008, EWHC 1186 (Comm.).

14 *Ibidem*, at paragraph 574.

15 *Ibid*em, at paragraphs 572-578.

16 Ellinger, Lomnicka, Hare, supra note 7, at pp. 131-134. In Canada: Ogilvie, supra note 7, at pp. 212-214. Ogilvie, supra note 8, at pp. 472-483.

17 Lloyds Bank Ltd. *v* Bundy, 1974; Q. B., 1975, 326; 3 All E. R., 1974, 757; 3 W. L. R., 1974, 501 (C.A.).

The court held that the bank owed a fiduciary duty to the father, who had placed his trust and confidence in the bank. The bank was aware of the father's reliance, but it, nevertheless, failed to make a full disclosure. The court found that such behavior was tantamount to a breach of the fiduciary duty, and declared the charge null and void.

However, this approach was discredited in the case of *Nat. Westminster Bank plc. v Morgan*,[18] whose basic model was similar to that of the Bundy case (this time, a wife guaranteed a mortgage on the family home to secure business debts of her husband). The House of Lords refused to find that the relationship between the bank and the security provider was a fiduciary relationship. Instead, it applied the doctrine of undue influence, finding it more suitable for the issue of security taking.[19] The House of Lords further cautioned against attempts to precisely define the situations in which a fiduciary duty arises, showing reluctance to acknowledge the doctrine.

During the last 30 years, the Morgan case has become the prevailing precedent, and similar cases of taking collateral from a wife or an aged parent were addressed by applying the doctrine of undue influence rather than the fiduciary duty.[20] In 1993 the House of Lords authoritatively ruled that undue influence is the appropriate doctrine for cases of banks taking security inappropriately from weak parties, [21]and the doctrine of fiduciary duty was abandoned.

In summary, even if, in the past, English courts were willing to recognize the relationship between the bank and the customer as a fiduciary relationship in certain cases, this approach has changed substantially over the last few decades and especially over the last 30 years. Today, under English law, the bank would only be subject to a fiduciary duty in very rare cases.

III. The evolution of the bank's fiduciary duty – the Israeli model

Another model of the bank's fiduciary duty is the Israeli model. The Israeli courts adopted the concept of the bank's fiduciary duty from the English law. However, from the moment that it was introduced in Israel, the courts

[18] National Westminster Bank plc. *v* Morgan, 3 All E. R., 1983, 85, revd; 1 A. C., 1985, 686, 1 All E. R., 1985, 821; 2 W. L. R. 588 (H.L.).

[19] Although in the end it was ruled that the bank did not exercise undue influence on the wife.

[20] Supra, note 16.

[21] Barclays Bank Plc. *v* O'Brien, 1994, 1 A. C. (H.L.). C. I. B. C., Mortgages plc *v* Pitt, 1994, 1 A.C. 299 (H. L.). Ogilvie, supra note 8, at p. 477.

expanded it far beyond its original English counterpart. Over the last 30 years, the Israeli courts have created a unique model of the bank's fiduciary duty, which is enormously wide.[22]

The idea of the bank's fiduciary duty was introduced in Israel at the first time in the case of Israel Mortgage Bank v Hershko,[23] in 1975. This case dealt with a loan provided to a customer. As a result of various limitations, the loan was established through a complex arrangement. The customer was not given a satisfactory explanation as to the essence of the transaction and therefore he did not understand that the way the loan had been established would cause him huge losses. The Israeli Supreme Court adopted the English judgent of Bundy mentioned above,[24] and ruled that the bank owed a fiduciary duty to the customer. Further it was ruled that the bank had breached its fiduciary duty by failing to provide the customer with full explanation, even though the customer had received independent advice from his attorney.

For many years the Hershko case was an isolated case regarding the recognition of the bank's fiduciary duty. However, during the late 80' and especially in the 90', the Israeli courts began to use this concept more often. The Israeli courts have determined, in various contexts, that "*the list of situations in which there is a fiduciary relationship is not closed and it exists in a diverse range of legal relations*".[25] Thus it was determined that fiduciary duty has broad application and applies "*in every case where a person has power and control over another*".[26]

Indeed, the bank has power and control over the customer's interests and his financial property. The relations between the bank and the customer are relations of dependence by the customer on the bank. The customer depends on the bank in terms of the consulting services provided by it, in the provision of the service itself and in the determination of the legal arrangement applicable thereto. In the provision of the service, the customer expects the bank to act with a high level of professionalism and responsibility and an exemplary level of good faith. Customers tend to have special confidence in the bank, and in many cases feel no need to seek a second opinion before acting in accordance with the bank's advice. The banks' involvement in the financial life of every individual in the State is so deep and comprehensive that today it would not be possible to imagine the possibility of an individual manag-

22 See the materials in footnotes 5 and 6.

23 Civil Appeal 1/75 Israel Mortgage Bank Ltd *v* Hershko, 29(2) PD 208, 1975.

24 Supra note 17.

25 Kosoi *v* Bank Y.L. Feuchtwanger Ltd., 1984, 38(3) PD 253, 278.

26 *Ibidem*.

ing his financial affairs without the banks. The bank possesses information that is not available to the general public, and also possesses special skills and technical means which individuals do not possess. All of the above enable the bank to help prevent its customers from sustaining losses, whereas the customer possesses no similar capability. The banks, for their part, are careful to cultivate public confidence in them, and it is even reasonable for duties to be imposed on them which are designed to fulfil the reasonable expectations which they themselves are instrumental in creating.[27]

The Israeli courts developed an additional justification for the bank's fiduciary duty, one which is based on the quasi-public status of the banks.[28] It was explained that their activities have the characteristics of a vital service to the public. The banks perform many public duties, serve as agents for the implementation of government policy and a pipeline for the transfer of government loans to the public, and enjoy the backing of the Bank of Israel to secure the deposits of their customers.[29] The individual, for his part, views the bank as a quasi-public body and places a great deal of trust in it.[30] The perception of the banks as quasi-public bodies led to the conclusion that the banks should be subject to special duties, including the fiduciary duty.[31]

During the last two decades, the bank's fiduciary duty has been broadly interpreted by the Israeli courts. The courts have applied it in a very wide manner, in four different aspects as follows:

In the personal aspect — The type of customers to whom it applies: The fiduciary duty applies to each and every customer: whether he is an individual or a corporation; whether he is a business customer or a private customer; whether he is an ordinary customer without financial experience, or a sophisticated customer who is familiar with the banking and financial world.[32] The fiduciary duty will apply even to customers who have financial power that can

[27] For the descriptive theories that lie behind this rhetoric, see Plato-Shinar, An Angel Named "The Bank", supra note 5, at p. 33-36. Plato-Shinar, the Bank's Fiduciary Duty, supra note 5, at p. 51-67.

[28] Sahar *v* Discount Bank, 51(4) P. D., 1997, 476-477.

[29] Civil Appeal 8068/01 Ayalon Insurance Company Ltd. *v* The Executor of the Oppalgar's Estate, 59(2) P. D., 2004, 349, 369.

[30] Civil Appeal 1570/92 United Mizrahi Bank *v* Zigler, 49(1) P. D., 1995, 369, 384. Civil Appeal 5893/91 Tefachot Israel Mortgage Bank Ltd. *v* Tzabach, 48(2) P. D., 1994, 573, 585.

[31] Rubinstein, Michal and Okon, Boaz, "The Bank as a Social Agency", *Shamgar's Book - Articles*, Part C, Jerusalem, Nevo, 2003, 819, 831. Weinrot, Abraham and Medina, Barak, *Lending Laws – The Borrower's Protection in Israeli Law*, Tel Aviv, Bursi, 1990, 98-102.

[32] Ben-Oliel, Ricardo, *Banking Law - General Part*, Jerusalem, Sacher Institute, 1996, 58.

be likened to the strength of the bank.[33] Every customer, by virtue of his very status as a customer, is entitled to a fiduciary duty.

In this regard it should be noted that according to Israeli law, a customer does not need to be an account holder, nor must have a long and regular relationship with the bank. Even someone who conducts a one-time transaction will be deemed to be a customer for the purpose of that particular service which he received from the bank,[34] and is entitled to fiduciary protection.

In the topical aspect — The type of the activities to which it applies: The banker's fiduciary duty applies to all the types of banking services, activities and transactions that the bank performs on behalf of the customer.[35] We have seen that the fiduciary duty arises from the existence of a bank-customer relationship. The relationship between the parties, by its very definition, is what imposes the fiduciary duty, and not a specific action that the bank wishes to perform.

In the circumstantial aspect: The imposition of the fiduciary duty is not dependent upon the existence of specific circumstances, such as special reliance of the customer on the bank.[36] The duty is deemed to be an integral component of the bank-customer relationship. In effect, the fiduciary duty serves as an undeniable presumption that exempts the customer from the burden of proving its applicability in a particular case: The duty always exists.

In the chronological aspect: The fiduciary duty is broadly applied also with respect to the period of time in which it exists. It originates at the pre-contractual stage and it is already binding upon the bank when negotiating with a potential customer.[37] Naturally, the duty applies as long as the bank-customer relationship exists. Furthermore, from the moment the fiduciary duty has arisen, it continues to exist, also after the closing of the account and the termination of the contractual relationship between the parties.[38]

33 Civil Appeal 7424/96 Mizrahi United Bank Ltd. *v* Eliahu Garziani, 1988, Co. Ltd, 54(2) P. D., 2000, 145, 161-162.

34 This arises from the definition of the terms "customer" and "service" in The Banking (Service to Customers) Law, 1981.

35 Tefachot Israel Mortgage Bank Ltd. *v* Tzabach, supra note 30, at 594 and 595. Ben-Oliel, supra note 32, at pp. 102-105.

36 Tefachot, *Ibidem*, at 595.

37 *Ibidem*, at 585, 594. See also: FitzGibbon, Scott "Fiduciary Relationships are not Contracts", 82 *Marq. L. Rev.*, 1999, 303, 309. Compare to the Canadian case Standard Investments Ltd. *v* Canadian Imperial Bank of Commerce, supra note 8. In this case the bank provided financial advice to a customer regarding the purchase of the controlling shares in a company. It was ruled that the fiduciary duty already existed when the bank offered to provide the service.

38 Civil File (Dimona) 1099/99 Turgeman *v* Bank Leumi LeIsrael Ltd., 2000(4) Takdin Magistrate, 2000, 1140 at paragraph 6.

Certain aspects of the fiduciary duty, such as the bank's duty of confidentiality, continue even after the death of the customer.[39]

In recent years, Israeli courts have ruled that the bank owes a fiduciary duty not only to its customers, but to third parties as well. Thus, a fiduciary duty was recognized vis-à-vis guarantors;[40] purchasers of apartments that were built by a constructor who received finance from the bank;[41] other creditors of the customer;[42] a third party who has a right to draw money from the customer's account;[43] and "*any person when the bank is aware, or should be aware, that such a person might be influenced by the bank's behavior*".[44]

Lately, a new approach is being developed by the Israeli courts, according to which the bank has a fiduciary duty vis-à-vis the general public.[45] It was explained that "*The existence of a general contract with the public expands the circle of those eligible to trust the bank, to the entire general public. The existence of such a contract imposes fiduciary duties on the banks to the public, without a direct connection to the particular service that is being provided or to the concrete circumstances surrounding the customer in his activity at the bank. It may be said that the general contract creates a starting threshold of fiduciary duties to the general public as a whole, which will be further intensified if the special circumstances so require*".[46]

According to this approach, the imposition of the fiduciary duty to the general public as a whole could lead to the imposition of general obligations which are not expressed only at the level of relations with a particular person. A fiduciary duty to the general public may be binding on the bank

[39] Civil Appael 1917/92 Skoler *v* Jerby, 47(5) P. D., 1993, 764, 772.

[40] Miscellaneous Civil Application (Tel Aviv) 3706/03 Bank Hapoalim Ltd. *v* Rimon, Nevo Database, 2003, at paragraph 5. Opening Motion (Tel Aviv) 672/96 Prioff *v* Bank Hapoalim Ltd., Takdin District Database, 2000. Civil File (Jerusalem) 1790/88 United Mizrahi Bank Ltd. *v* Ziegler, District Judgments, 1992 (1) 172, p. 175. See Plato-Shinar, Ruth, "The Bank's Duty of Disclosure towards a Mortgagor of Assets Securing Debts of a Third Party", 49 *Hapraklit L. Rev.*, 2007, 385.

[41] Plato-Shinar, Ruth, "Construction Loans in Israel: Bank's Liability Towards Third Parties", 23 *International Construction Law Review*, 2006, 187, at p. 194-198. Plato-Shinar, Ruth, "Construction Loans – Does the Bank Owe a Fiduciary Duty Towards Buyers of Appartments?", 4 *Land Law J.* 38, 2005, issue no. 6.

[42] C. F., Tel Aviv, 113219/97 Iris Constructors *v* Hamizrahi Bank Ltd., 16 Dinim Shalom 250, 1999.

[43] C. A. 717/89 Bank Igud Le-Israel Ltd *v* Eran Tours Ltd., 49(1) P. D. 114, 1995.

[44] Civil File (Tel Aviv District Court) 2069 Farhi Food Services *v* Bank Hapoalim, not published, 1997.

[45] Application for Civil Appeak 9374/04 E. & G. Advanced Systems for Driving Teachers Ltd. *v* Bank Leumi Le-Israel Ltd., 69 Dinim Supreme 809, 2004, at paragraph 6(b).

[46] Rubinstein and Okon, supra note 31, at p. 826, 828. Civil File (Jerusalem) 5272/03, Iluz e. Discount Bank Ltd., Takdin District Database, 2004, at paragraphs 9, 13.

at the time of determining general policy, such as the bank's financial reporting policy or its investment policy, and may even impose on the bank responsibility for the financing of transactions that are detrimental to the public, for example, in the field of environmental quality.[47]

In summary, the discussion above shows that the fiduciary duty imposed on banks under Israeli law is enormously wide.

Is there any explanation for such an approach? It seems that the reason for the wide approach of the Israeli courts is the unique position of the Israeli banking sector, and the enormous economic powers of the Israeli banks. The Israeli banking market is characterized by centralization and a lack of competition.[48] In the Israeli banking system, five banking groups are prominent, when two of them (Bank Leumi and Bank Hapoalim) control over sixty percent of the banking operations.[49] The possibility of additional banks entering into the system is regulated pursuant to the Banking (Licensing) Law 1981, and requires approval from the Bank of Israel. However, it would appear that the Bank of Israel has not only made no attempts to halt the trend of centralization, but it has even tried to encourage this trend, out of the belief that centralization and power would be conducive to the stability of the banks.[50] The huge market power possessed by the banks, and —in particular— the two major banks, in conjunction with the significant gaps in information, and the lack of a developed system of credit rating, aggregate to high entry thresholds for new players in the sector.[51] This centralized structure constitutes an oligopoly (or to be more precise, a duopoly), that strengthens the power of the existing banks.[52]

[47] Rubinstein, Okon, supra note 31, at p. 832. For criticism on this approach, see Ruth Plato-Shinar, "To Whom Does The Bank Owe a Fiduciary Duty?", 29 *Quarterly Banking Review*, 2004, 67 Issue no. 154. Plato-Shinar, The Bank's Fiduciary Duty, supra note 5, at p. 146-148.

[48] The Report of the Parliamentary Interrogatory Committee regarding the Banking Fees (2007) at 14-16. Available at: *http://www.knesset.gov.il.committees/heb/docs/bank_inq.pdf* (the "Banking Fees Report"). With regard to the centralization of the banks in the capital market, see The Report of the Inter-Ministerial Team regarding Reform in the Capital Market (2004) at p. 14. Available at: *http://ozar.mof.gov.il/hon/2001/hon_dep/bachar.asp*, the "Bachar Report". Meir Chet, *Banking in Israel: Structure, Activities and Crisis*, The Jerusalem Institute for Israel Studies, 1994, at p. 14-21, 31.

[49] The Bachar Report, supra note 48, at p. 15.

[50] The Banking Fees Report, supra note 48, at p. 22.

[51] The Bachar Report, supra note 48, at p. 15.

[52] Ben-Horin, Moshe, *The Securities and Capital Market*, 1996, 161. For another approach, see Shifron, Gad, "The Centralization of the Banks in Israel and in Other Countries", 31 *Quarterly Banking Review*, 1993, Issue no. 124, 28–33. Akiva Sternberg, "Competition in the

Against this background, the Israeli courts' approach is understandable, in that it attempts to restrict the banks from abusing their power. The suitable tool for this purpose is the fiduciary duty.

IV. The need for harmonization

Whereas, according to English law, the bank is not usually deemed to be a fiduciary, the situation in the Israeli law is totally different, as was shown above. The difference between the two legal systems —the English and Israeli— is not merely theoretical, but it is reflected in practice in a wide spectrum of cases. One can point to numerous Israeli judgments in which the customer's claim against the bank was accepted on the basis of the determination that the bank had breached the fiduciary duty that is imposed on it. Had these claims been heard under English law, they would have been dismissed due to non-recognition of the existence of a bank's fiduciary duty. I will demonstrate this in a number of contexts.

One example relates to the duty to provide information.[53] As a rule, the English courts loath to broaden the duty of disclosure that is imposed on the bank. An example of this is the matter of *Suriya and Douglas* v. *Midland Bank plc*,[54] in which a customer required an interest bearing current account on which checks could be drawn. As this type of account was not customary at the bank, the customer was forced to run two separate accounts concurrently: one of which was an interest bearing account and another account on which checks could be drawn. At a later stage, the bank introduced a new type of current account which suited the customer's precise needs. However, the bank failed to disclose this to the customer and caused him to continue holding the non-interest bearing account for another four years. The customer sued the bank for loss of interest, claiming that there had been a contractual obligation on the bank to inform him about the aforesaid innovation. The court rejected the claim and held that a bank-customer relationship does not impose a duty of disclosure towards the customer. Even if the bank has a policy of informing customers of new types of accounts, this does not provide the customer with a cause of action should the bank fail to do so. An Israeli court would have ruled otherwise

Israel Banking System --- A Further Examination", 33 *Quarterly Banking Review*, 1995, issue 130, 62.

53 In this matter see: Plato-Shinar, Ruth, "The Banks' Duty of Disclosure - towards a New Model", 27 *B. F. L. R.*, 2012, 427.

54 1999, 1 All E.R. (Comm.) 612.

on the basis of the fiduciary duty, which obliges the bank to protect and to further the interest of the customer.

Another example deals with the obligation to provide explanations.[55] In the Israeli case of Hershko mentioned above,[56] it was ruled that the bank breached its fiduciary duty to a customer that received a complicated loan, by failing to provide the customer with the full explanation that was required, even though the customer had received independent advice from his attorney. Under English law, it is doubtful that the customer would have succeeded in his claim because, under normal circumstances, a customer that relies on private professional advice is not deemed to be one who has relied on the bank's advice, and, without such reliance, a fiduciary relationship is not usually recognized.[57]

In the Israeli case of Turgeman,[58] the issue at hand concerned a tax credit that was received in respect of the Turgeman couple at a branch of the bank. The couple had previously run a joint account at the branch; however, when they got divorced the account was closed. An account existed at the branch in the name of the husband alone which was in overdraft. The bank deposited the tax credit in the husband's account. The woman sued the bank, *inter alia*, in respect of a breach of the fiduciary duty towards her. The court accepted the claim and held that the fiduciary duty to the customer continues even after closure of the account. Hence, the bank owed a duty of trust to the woman even after closure of the joint account and it was prohibited from depositing the tax credit in a separate account belonging to the husband, without her consent. However, under English law, a claim based on the fiduciary duty would have been dismissed. We have seen that the bank —customer relationship, *per se*, does not create a fiduciary duty; and, according to English law, even if a fiduciary duty exists at the time of closure of the account, the bank— customer relationship comes to an end, and the bank owes no duty to the customer, except for the duty of confidentiality.

These and other examples illustrate the huge difference between Israeli law and English law regarding the implementation of the concept of the

55 Plato-Shinar, supra note 53, at p. 437-439.

56 Israel Mortgage Bank Ltd *v* Hershko, supra note 23.

57 This is aside from the doctrine of undue influence, according to which, also, the bank would bear no responsibility if the obligor (mostly surety) received independent legal advice. See: Ellinger Lomnicka hare, supra note 5, at p. 139–53; Mark Hapgood, general ed., Paget's Law of Banking, 13th ed., London, LexisNexis Butterworths, 2007, 689–700.

58 Turgeman *v* Bank Leumi Le-Israel Ltd, supra note 38.

bank's fiduciary duty. Naturally, differences exist in relation to other legal systems that impose other models of the fiduciary duty on the banks.

These differences are, apparently, a source of problem. The banking business has become truly global. Yet, legal rules and doctrines are still very much based on national frameworks. The result is that obligations of banks depend on the place of the executed business transactions, and for global banks it makes the compliance with applicable rules difficult. Since many banks are prominently represented in different jurisdictions, the impression exists that not enough consideration is given to the different concepts of the fiduciary duty of banks vis-à-vis their customers in the real world. Obviously, the described legal differences are obstacles to the global banking business. The harmonization of some basic rules would improve the legal certainty without jeopardizing the flexibility of the banks to a substantial extent. It would seem to be worthwhile to give greater attention to the possibilities of a certain harmonization of rules that implement the doctrine of the bank's fiduciary duty.[59]

Alongside the call for harmonization in the implementation of the case law doctrine of the bank's fiduciary duty, an interesting trend of recent years should be noted, which may reduce the gaps between the different legal systems. Under banking regulation that is on the rise in many countries, various behavioral rules are imposed on the banks by legislation or by the regulator. These rules are, in effect, expressions of the fiduciary duty.

This is, for example, the situation in England, where the courts are reluctant to impose a fiduciary duty on the banks.[60] However, the duty has gained significant strength through the entrenchment of its various components in the binding principles of the Financial Services Authority (FSA).[61] These principles bind the bank to conduct its business with integrity;[62] to pay due regard to the interests of its customers and treat them fairly;[63] to manage conflicts of interest fairly, both between itself and its customers and between a customer and another customer;[64] and to take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment.[65]In the investment field, English

[59] Plato-Shinar and Weber, supra note 6, at p. 433.

[60] See chapter B, above.

[61] FSA Handbook: High Levels Standards, Principles for Businesses, PRIN 2.1 -The Principles, Available at *http://fsahandbook.info/FSA/html/handbook/PRIN/2/1*.

[62] PRIN 2.1.1(1).

[63] PRIN 2.1.1(6).

[64] PRIN 2.1.1(8).

[65] PRIN 2.1.1(9).

banks are subject to the "client's best interests rule". This rule determines that "*a firm must act honestly, fairly and professionally in accordance with the best interests of its client*".[66] As discussed above, this is precisely the core meaning of the fiduciary duty.[67]

These and other similar provisions actually reduce the existing gap between the different legal systems regarding the method of implementation of the bank's fiduciary duty. If this trend continues, then despite the different approaches of the courts in the different jurisdictions, harmonization could be achieved in practice after all.

[66] FSA Handbook: Business Standards, Conduct of Business Sourcebook, Conduct of Business Obligations, COBS 2.1.1, available at *http://fsahandbook.info/FSA/html/handbook/COBS/2/1*. The rule is an implementation of section 19(1) of the European Council Directive 2004/39 Markets in Financial Instruments (MiFID), 2004 O.J. (L 145), available at *http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CONSLEG:2004L0039:20070921*, en PDF.

[67] In Chapter A, supra.

CHAPTER III

THE EVOLUTION OF THE LEGAL FRAMEWORK AROUND THE WORLD OVER THE LAST THIRTY YEARS

ONLINE DISPUTE RESOLUTION –ODR— BUILDING E-CONFIDENCE IN EUROPE

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SUMMARY: I. *E-Confidence*. II. *Developing online dispute resolition —ODR—in consumer redress*. III. *ODR in spanish consumer law*.

I. E-CONFIDENCE

Over 493 million people are in the European internal market, even though many of the consumers are reluctant to use the web, especially if that involves a cross border transaction: An important part of the e-commerce depends on the confidence in the cross-border transaction, as of the 33% of Europeans who shopped online in 2008, out of whom only 7% did cross-border.[1] Confidence in the network is measured in terms of security: consumers will only be able to evaluate the advantages that e-commerce offers over traditional methods if they know the medium and understand how it works. But besides an appropriate regulatory framework, the e-confidence is also based on a responsive system of conflict resolution, perhaps more intensely than in offline relationships. In other words, the harmonisation of consumer law has tried to give same —or at least equivalent— contracting conditions all over Europe. But only when individual redress is able to be fast and cheap, consumers will feel comfortable with this type of transactions. For this reason, one of the lines started by the Commission is the development of tools to simplify the claim process.

For this reason, consumers need simple, fast and an inexpensive system to seek for redress; only in that case, consumers will take the risk of a default or defective performance by the enterprise. The current strategy for consumer protection 2009-2014, is again insisting on increasing consumer con fidence

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[1] Special Eurobarometer 298: October 2008.

to new technological challenges as a way to increase the efficiency of their protection.[2] For this reason, it is soon understood that cross-border by its nature means an area created without borders, such as the internet, and therefore the greatest concern is to provide the new practices of e-commerce with alternative methods of dealing with disputes. It is this fact that is bringing about the change from ADRs to ODRs.

II. Developing online dispute resolition —ODR— in consumer redress

In the EU point of view, any alternative dispute resolution (ADR) that is used to deal with consumer complaints is considered to be a basic instrument for generating the so called consumer access to justice. ADRs have played a key role in enforcement for consumers across the EU. This situation stems from the actions initiated by the green paper on "*consumer access to justice in the internal market*" in 1993, which sought to design a regulatory framework in which mechanisms to ensure the effectiveness of consumer protection could be generated. This green paper on the state of the question observed the proliferation of various kinds of ADR for consumer complaints in EU member countries, to meet the demand for faster and cheaper processes than the court system.

In that sense, the consumer ADR system was laid down in two sets of regulations at the Community level: the Commission Recommendation of 30 March 1998 on the principles applicable to the bodies responsible for out-of-court settlement of consumer disputes and the Commission Recommendation 2001/310/CE of 4 April on the principles for out-of-court bodies involved in the consensual resolution of consumer disputes. The EU has been developing a high level task in this direction, especially from 2009 on, but in November 2011 an important step was done because the EU approved a Proposal of Directive on consumer ADR[3] that tries to offer a standard level of consumers' protection all over Europe. If that piece of regulation is definitive-

[2] This question has been referred to repeatedly in documents on e-commerce since the first e-Europe plan in 2002. The most recent document is the "Report on cross-border e-commerce in the EU", SEC(2009) 283 final, of March 2009, compiled by the Commission Working Group. This reports that 21 per cent of individuals do not use the internet for shopping because they are worried about problems in the way complaints may be handled or failures on the part of businesses. See *ec.europa.eu/consumers/strategy/docs/com_staff_wp2009_en.pdf*, last accesed January 25th 2012.

[3] Proposal for a Directive of the European Parliament and of the Council on alternative dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and

ly approved, a first and crucial step to harmonization of enforcement system will be done. So, the choice for individual redress in consumers' complaints through ADR is definitively done.

The intersection between the development of ADR in consumer law and electronic commerce, as well as a great opportunity to use ICT in consumer ADR, is very clear in the Communication 161/2001 and is seen as the best instrument for developing what we have called e-confidence.[4] At present, the development of ODR is no longer only a question of consumer access to justice, but the generation of confidence in the new medium.[5] In fact, the e-confidence has become the basis of ODR development in the EU and so, the consumer ODR value lies in the effectiveness of the system. Thus the search for efficiency along with cost reduction has made the classic ADR adapt to the online environment where experiences are numerous.

Online Dispute Resolution is an expression which emphasizes the fact that the conflict resolution processes are online, as opposed to ADRs which are not. But from this almost tautological statement, there is a wide range of experiences. For that reason, we will use "ODR system" to refer, as Poblet states, to any process, methods or techniques that use information and communication technologies (ICT) to facilitate the resolution of disputes.[6] Given that broad definition, some precisions have to be done. Firstly, ODR cannot be merely considered as an online adaptation of ADR. In fact, ODR can be larger than ADR as the online context also allows the cybercourts,

Directive 2009/22/EC (Directive on consumer ADR), COM, 2011, 793 final, 2011/0373 (COD).

[4] Commission Recommendation of 4 April 2001 on the principles for out-of-court bodies involved in the consensual resolution of consumer disputes, *OJ L 109*, April 19th, 2001, pp. 56–61.

[5] See Communication of July 2nd, 2009 from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on the enforcement of the consumer acquis: Nevertheless, these key factor is far from being achieved: as C stays European consumers remain reluctant to reap the benefits that market integration provides. One reason for this is that consumers do not feel confident that their rights will be equally protected when buying abroad 1 . In a single market, consumers should not be concerned with where a trader is established since it should not influence the level of protection against unfair commercial practices. A particular challenge for the EU therefore is to secure a consistently high level of enforcement across its territory. It is the purpose of this Communication to take stock of ongoing Commission work and to explore the potential for future initiatives in the context of a comprehensive analysis of enforcement related activities.

[6] Poblet, M., "Introduction: Bringing a new vision on online dispute resolution", in Poblet (ed.), *Expanding horizons of ODR, Proceedings of the 5th International Workshop on online dispute resolution*, Firenze, 2008, p. 1.

that would not be an "alternative" way of resolving disputes.[7] Secondly, ODR can be used in e-disputes or in conflicts arisen in traditional transactions, that is to say, offline. Nevertheless, as a way of building e-confidence, the natural field of analysis is online transactions conflicts.[8] Thirdly, the use of ICT in a dispute resolution system offers a great variety of levels that can be outlined going from the use of ICT in the environment of conflict resolution to the generation of new ODR platforms mediated by the technical advances of the Internet, especially the www2, which promotes interoperability.

In that sense, not every use of ICT in a dispute resolution system would be considered as an ODR. The use of electronic mail in an ADR process can be considered as ODR only in a very large sense. And we can add the use of videoconferencing in some ADR steps —such as the hearing in an arbitration process—.[9] These practices can be described as a very initial step in ODR, but they are the first level in the adaptation of traditional ADRs to the new environment and these experiences support the ability to resolve conflicts between consumers and providers by "electronic means".

The ODR system becomes more complex in case of greater interface between the technical instruments and the way of dispute resolution. So, the ODRs are to be analyzed bearing in mind that they have a large amount of conceptual independency as ICT allows a technical approach that in the offline world can simply not be possible.[10] As Benyekhlef[11] states, technology already provides "*mechanisms that use a sound technological infrastructure to automate certain functions, model the relevant process and provide an interface through which all steps of the procedure can be accomplished, documented and archived*". It is that automation, modelling and interfacing which can be developed in different levels, depending on the type of ODR. In this sense, the ODRs are a system to resolve or facilitate the resolution of disputes that only in a part can be considered as the online develop of ADRs for two reasons: ODRs include non alternative systems of dispute resolution, and ODRs also refer to brand

[7] See, Kaufmann-Kohler, G. and Schultz, T., *Online dispute resolution. Challenges for Contemporary Justice*, The Hague, Kluwer Law International, 2004, pp. 5 to 10.

[8] See Suquet, J., "Online dispute resolution (ODR): una visión jurídica del estado del arte tecnológico", *Revista Vasca de Derecho Porcesal y Arbitraje*, 2010, t. XXII, pp. 62 y 63.

[9] For different opinions about the kind of electronic means that would be essential for a sytem to be considered ODR, see Suquet, *op. cit.*, p. 63.

[10] Poblet, M. *et al.*, "ODR y mediación en línea: estado del arte i escenarios de uso", Poblet, M. *et al.* (eds.), *Materiales para el Libro Blanco de Mediación en Catalunya*, Barcelona, Centre d'Estudis Jurídics i Formació Continuada, Departament de Justícia de la Generalitat de Catalunya, Colección Justicia y Sociedad, pp. 159-169.

[11] Benyekhelf,K. and Gélinas, F. "Online Dispute Resolution", *Lex Electronica*, vol.10, num. 2, Été-Summer 2005, p. 95, *http://www.lex-electronica.org/articles/v10-2/Benyekhlef_Gelinas.pdf*.

new technical means of solving disputes that are away from the definition of the ADR types. And that means a different juridical approach because of the versatility of new technology.

Nevertheless, as it has been stressed by Hörnle, ODR in consumer issues are of added value because they can be easily adapted to every type of claim depending on the economic value of the complaint and the use of some standards that are able to guarantee the main principles of dispute resolution systems.[12] Regarding consumer disputes in e-commerce, the role of alternative dispute resolution is stressed on two important pieces of regulation: the art 17 D 2001/31/EC[13] —the e-commerce Directive—; and the Joint declaration by the Council and the Commission made when the "Brussels I" Regulation on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters was adopted.[14] For that reason, in November 2011, the EU has approved a *proposal of Regulation on consumer ODR*.[15] This piece of regulation will develop an online platform for the resolution of consumer complaints in electronic commerce when they would be cross-border. The proposal for a regulation is targeting a very specific area: cross-border complaints in the field of electronic commerce, but with enough depth and breadth. It deals, therefore, clearly the requirements of the resolution of consumer disputes and their adaptation to the online environment.

III. Odr in spanish consumer law

1. *"Electronic arbitration" in the spanish system od consumer arbitration*

Since 2008, Spain has opted to regulate a specific type of ODR: that is, consumer arbitration understood as a system that combines procedures of

[12] Hornle, J, "Online Dispute Resolution in Business to Consumer E-commerce Transactions", The Journal of Information Law and Technology (JILT), 2002 (2). *http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2002_2/hornle*. Last accessed October 5th, 2010.

[13] Directive 2000/31/EC of 8 June 2000 concerning certain judicial aspects of the services of the information society, and in particular electronic commerce, within the internal market, OJ L 178.

[14] Joint declaration of the Council and the Commission concerning Articles 15 and 73 of the Regulation in the minutes of the Council meeting of December 22nd, 2000 which adopted this Regulation. See Council Regulation (EC) num. 44/2001, of December 22nd, 2000 on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (the Brussels Regulation).

[15] Proposal for a Regulation of the European Parliament and of the Council on online dispute resolution for consumer disputes (Regulation on consumer ODR)COM(2011) 794 final, 2011/0374 (COD) .

mediation and arbitration in keeping with the description provided above. In fact, the regulation of electronic consumer arbitration is presented in the Preamble to Regulation 231/2008 as its principal novelty.[16] This innovation represents the development of a system that combines the use of ICTs for consumer arbitration and mediation and the building of on-line platforms for ODR in such matters, the main aim of which is to make the procedure swifter and to eliminate costs.[17]

The regulation lays down, in a number of precepts, the procedures for electronic consumer arbitration. Here, a clear distinction is drawn between electronic arbitration and "procedural steps taken on-line" as part of a conventional arbitration process (article 3.3). Following this distinction, in both instances it deems applicable Act 11/22 June 2007 (insofar as this is not provided for in Regulation 231/2008), governing a citizen's electronic access to public services. This reference can be attributed to the fact that consumer arbitration is of an institutional nature which means it is subject to the authority of administrative law as regards the use of electronic media for giving legal notice and for other effects.

All in all, Regulation 231/2008 has a somewhat restrictive view of electronic arbitration since it only considers procedures that are conducted "wholly" by electronic media, although it then recognizes that some steps might be completed face to face. Such an approach gives rise to problems of definition: how many face-to-face operations are necessary before the arbitration will no longer be considered electronic? Art. 45, in discussing the instruction and administration of evidence in an electronic arbitration, states that "In an electronic arbitration when the instruction and administration of evidence is agreed to be conducted face-to-face, the procedure shall be undertaken by videoconference or by any other technical means that allows identification and direct communication between parties". We can conclude from the forgoing that the use of videoconferencing constitutes a face-to-face procedural step, even though it is conducted by electronic means and, strictly speaking, it is not conducted face-to-face. As such article 45 provides a good example of what was discussed earlier: the use of videoconferencing represents an ICT application to mediation and arbitration procedures that achieves an equivalent effect to that of a face-to-face hearing based on techniques of distance communication that allow the emission of images.

[16] The importance of this approach had previously been identified in the *Libro Blanco sobre Mecanismos Extrajudiciales de Solución de Conflictos en España*, *op. cit.*, p. 97.

[17] For a further discussion, see Montesinos Garcia, A., "*El arbitraje de consumo virtual*" in Cotino Hueso, L. (coord.), *Consumidores y usuarios ante las nuevas tecnologías*, Valencia, 2008, p. 264.

However, what Regulation 231/2008 actually foresees as constituting electronic arbitration is a centralized computer application that the Ministry of Health and Consumer Affairs received the mandate to create (article 51.2) as an equivalent system to that of conventional consumer arbitration only conducted by electronic means. In other words, it is a procedure, adapted to the provisions laid down in the Regulation, that is carried out virtually and in which the problems that have to be overcome involve determining which board of arbitration has jurisdiction (article 52); how legal notices can be served (article 54); where the arbitration should take place (article 55) and how the electronic signature mechanism can be implemented so as to guarantee the identity of the parties and the integrity of the communication (article 53).

2. *Mandatory electronic mediation in small claims*

There is ab intense relation between ODR and small claims, i.e. the claim does not have a great economic value. So, an important practical point to bear in mind is the fact that most consumer disputes fall into that category of small claims. Two consequences arise from this: on the one hand, if there is no swift, cheap mechanism of resolution, these claims are unlikely to reach the courts;[18] and, on the other hand, although the redress sought by each separate consumer may be of little value, there might be a very large sum involved if all the consumers are considered together. Take, for example —at the EU level — the SANCO (Directorate-General for Health and Consumers) study into commercial practices relating to the sale of flight tickets via the Internet, which led to the drawing up of a list of good and bad practices.[19] This sector is, therefore, one in which disputes will only be settled if this mechanism of resolution is chosen.

For that reason, the Spanish Royal-Decree 5/2012 on civil and commercial mediation provides online mediation for claims of less than 600 euros (article 24). This provision will be mandatory, provided that parties have possible access to the system. It supported the same idea as DF4a, which envisages the creation of an application for simplified electronic mediation

[18] Point 2 of preamble to R 98: most consumer disputes, by their nature, are characterized by a disproportion between the economic value at stake and the cost of its judicial settlement; the difficulties that court procedures may involve may discourage consumers from exercising their rights in practice, especially in the case of cross-border conflicts.

[19] See the website of the Directorate-General for Health and Consumers: *http://ec.europa.eu/consumers/enforcement/sweep/index_en.htm*.

for quantity claims with no dispute on law grounds. This can be the start point for a real development of consumers ODR in Spain.

In short, the commitment to ODRs for consumer complaints has enormous potential and this will undoubtedly be expanded in the near future.

THE PROPOSED HAGUE PRINCIPLES ON CHOICE OF LAW IN INTERNATIONAL COMMERCIAL CONTRACTS

Neil B. COHEN*

SUMMARY: I. *Introduction*. II. *Major Issues*. III. *Other features of the draft principles*. IV. *Areas of potencial difficulty*.

I. INTRODUCTION

The Hague Conference on Private International Law recently embarked on a project of major importance to international commercial law – the preparation of an instrument setting out rules for determining the law that governs international commercial contracts. Determination of the law applicable to international commercial contracts is an area in which certainty would be desirable. That certainty is present under the law of many States, but is absent in others. Accordingly, the guidance provided by the Hague Conference project will be valuable in establishing an international norm.

The project has proceeded with great efficiency. In 2009, the Hague Conference on Private International Law established a Working Group on Choice of Law in International Commercial Contracts to prepare a set of principles to govern the topic. The Working Group met three times in 2010 and 2011, culminating with the preparation of draft Hague Principles on Choice of Law in International Commercial Contracts (hereinafter the "draft Principles," or "draft Hague Principles") as well as a policy document highlighting the policy choices made in that draft.

The report of the Working Group was then submitted to the Council on General Affairs and Policy of the Hague Conference on Private Interna-

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tional Law for its consideration. At the April 2012 meeting of the Council on General Affairs, the Council accepted the report of the Working Group and decided to establish a Special Commission "*to discuss the proposals of the Working Group and make recommendations as to future steps to be undertaken, including the decision to be taken on the form of the non-binding instrument and the process through which the commentary shall be completed.*" The Special Commission will meet for the first time in November 2012.

This project is quite important because uncertainty as to the legal rules that will govern disputes arising under an international contract is a deterrent to entering into such contracts. While such uncertainty does not typically prevent formation of such contracts, like all uncertainty it is taken into account in pricing a transaction and determining whether it is beneficial to a party.

In the distant past, the idea that parties to a contract had a say in determining which law would govern it was controversial,[1] but, in contemporary legal regimes, most states give parties to a commercial contract some degree of autonomy in determining the applicable law.[2] Yet, while such party autonomy is a widely accepted concept, it is not accepted everywhere and, even where accepted, it is not always applied with equal vigor. The result is that, for many transactions, substantial uncertainty remains as to the law governing a contract.

As noted above, the Hague Conference has concluded that an instrument designed to further party autonomy to select the applicable law, and set uniform principles governing it, would be of significant usefulness. The Hague Conference, however, has decided that, rather than preparing a binding instrument such as a convention, it will initially formulate its principles as a set of advisory principles.

This paper summarizes the draft Principles prepared by the Working Group and highlights issues raised by those draft principles.

[1] See, Beale, Joseph H., "What Law Governs the Validity of a Contract?", 23 *Harvard L. Rev.*, 1910, 260, 261 ("So in the case of the adoption of a law to govern the nature and obligation of a contract, it is entirely possible from the point of view of any one state that the law of that state or of some other state should be applied to the determination of the question; but if the law of that state is not applied, it is a result of the sovereign will of the state which controls the contract. Now, if it is said that this is to be left to the will of the parties to determine, that gives to the parties what is in truth the power of legislation so far as their agreement is concerned. The meaning of the suggestion, in short, is that since the parties can adopt any foreign law at their pleasure to govern their act, that at their will they can free themselves from the power of the law which would otherwise apply to their acts. So extraordinary a power in the hands of any two individuals is absolutely anomalous; so much so that even the courts which adopt a rule of this sort have been occupied in defining limitations to the exercise of the parties' will").

[2] See, e.g., Uniform Commercial Code § 1-301.

II. Major issues

1. *What contracts will be covered by the Hague Principles?*

The draft Principles address "*choice of law in international contracts entered into by two or more persons acting in the exercise of their trade or profession*." Thus, the draft Principles cover business-to-business transactions but not consumer transactions.

What is an international contract? article 1(2) of the Draft Principles states that

> For the purposes of these Principles, (i) a contract is international unless the parties have their places of business in the same State and the relationship of the parties and all other relevant elements, regardless of the chosen law, are connected only with that State; (ii) if a party has more than one place of business, the place of business is that which has the closest relationship to the contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of the contract.

Thus, the draft Principles opt for a broad definition of internationality, under which all contracts are presumed to be international and covered by the principles unless not only do all the parties have their places of business in the same State but also all other relevant elements of the transaction are connected only with the State in which those parties are located. It is important to note that a place of business of a multi-location party is not determined by tests used in other contexts, such as its place of central administration[3] (or chief executive office),[4] habitual residence[5] or center of main interests, under which each entity has only one location. Rather, the draft Principles utilize a transaction-specific test (the place of business is that which has the closest relationship to the contract and its performance) under which a party can be located in one State for one transaction and another State for a different transaction. So, for example, the place of business of a multinational law firm with offices in many States may be the United States when the firm enters into contracts to provide legal services in the United

[3] See United Nations Convention on the Assignment of Receivables in International Trade, article 5(h).

[4] See, *e. g.*, Uniform Commercial Code § 9-307(b).

[5] See *e. g.,* Regulation (EC) num. 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations ("Rome I"), article 4(1), pars. (a), (b), (d), (f), and article 4(2).

States from its New York office but in Mexico when it enters into contracts to provide legal services in Mexico from its Mexico City office. This rule has some advantages. For example, a contract entered into in Ireland between the Irish office of an international architectural firm headquartered in Iceland and the Irish office of an international law firm headquartered in London, is, in many ways, a domestic contract (notwithstanding the home offices of the parties); all relevant personnel are located in Ireland, both parties have offices in Ireland, and the contract will be performed in Ireland. On the other hand, this rule has some disadvantages as well, inasmuch as it requires a determination of the office of a party that has the "*closest relationship to the contract and its performance.*" This will be obvious in some cases, but not in others, especially in a world in which many offices of a party to a contract are involved in its performance.

Note as well that, although the title of the draft Principles indicates that they cover "international commercial contracts," the scope provisions of the draft Principles do not use the phrase "commercial contracts." Rather, article 1(1) indicates that the draft Principles govern international contracts "*entered into by two or more persons acting in the exercise of their trade or profession.*" The intent, obviously, is to exclude consumer contracts and include "business-to-business" contracts. Indeed, the "*Policy Document Regarding Hague Principles on Choice of Law in International Commercial Contracts*" accompanying the presentation of the draft Principles to the Council on General Affairs and Policy of the Hague Conference (hereinafter the "Policy Document") says as much: "*The draft Hague Principles will apply only to commercial contracts involving business-to-business transactions. As a result, employment and consumer contracts will be excluded*".[6] It is not so obvious, however, that the phrase "*acting in the exercise of their trade or profession*" excludes employment contracts. After all, many professional, be they lawyers or carpenters, are employed by others. While the intent of the drafters is clear, it is possible to read the language of the draft Principles in isolation and reach a different conclusion.

2. *How broad is the autonomy provided for by the Hague Principles?*

While there may be some fuzziness in determining whether a contract is within the scope of the draft Hague Principles, there is no similar fuzziness

[6] Policy Document Regarding Hague Principles on Choice of Law in International Commercial Contracts, Annex III to Choice of Law in International Contracts: Development Process of the Draft Instrument and Future Planning, January 2012 (the "Policy Document") at par. 10.

with respect to the rule of autonomy that the draft Principles propose. It is simple and straightforward: Under the draft Principles, "*a contract is governed by the law chosen by the parties*".[7] Moreover, just to make sure that no reader misses the point, the draft Principles explicitly provide that "*no connection is required between the law chosen and the parties or their transaction*".[8]

This rule, quite obviously would ratify the choice of any body of law in an international commercial transaction without regard to whether the parties or the transaction bear any relation to the law chosen by the parties.[9] This is certainly the predominant view in international instruments such as those promulgated by the Hague Conference,[10] regional instruments such the Mexico City Convention[11] and the Rome I regulations,[12] and much domestic legislation.[13]

Yet, this degree of party autonomy is not accepted world-wide. Indeed, it is not accepted in at least one jurisdiction that firmly supports party autonomy as a general matter - the United States of America. For example, in contracts within the scope of the Uniform Commercial Code, the range of choices for the law governing the contract is limited to States to which the transaction bears a "reasonable relation".[14] In cases governed by the com-

[7] Proposed Hague Principles on Choice of Law in International Commercial Contracts, Annex II to Choice of Law in International Contracts: Development Process of the Draft Instrument and Future Planning, January 2012 (the "Draft Principles"), article 2(1).

[8] Draft Principles, article 2(4).

[9] But see text at notes 22-25, *infra*, for important limits on the applicability of the law chosen by the parties.

[10] Hague Convention of December 22nd, 1986 on the Law Applicable to Contracts for the International Sale of Goods, article 7; Hague Convention of 14 March 1978 on the Law Applicable to Agency, article 5; Hague Convention of June 15th, 1955 on the law applicable to international sales of goods, article 2(1).

[11] Inter-American Convention on the Law Applicable to International Contracts, article 2.

[12] Rome I, article 3(3).

[13] According to the [policy paper], such jurisdictions include article 3 and article 41, 1st sentence Choice-of-Law Act of China's Mainland (2010); article 20 Act on the Application of Laws in Civil Matters Involving Foreign Elements of Taiwan (2010); article 7 Act on the General Rules of Application of Laws of Japan (2006); article 25(1) Conflict of Laws Act of Korea (2001); article 3540 Civil Code of Louisiana (1991); article 434(1) Civil Code of Mongolia (1994); article 3111(1) Civil Code of Quebec (1991); article 1210(1) Civil Code of the Russian Federation; article 116(1) Federal Act of 18 December 1987 on International Private Law of Switzerland.

[14] See Uniform Commercial Code § 1-301(a). It should be noted that, in 2001, the American Law Institute and the Uniform Law Commission, the joint sponsors of the Uniform Commercial Code, promulgated a new Official Text of the Uniform Commercial Code under which parties in international transactions could choose the law of any State without regard to whether the transaction bore any relation to that State. After seven years of enact-

mon law of contracts, the predominant approach in the United States is that of the Restatement (Second) of Conflict of Laws, under which a choice of law will not be enforced if *"the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice*".[15]

The difference between the prevailing view in the United States and that proposed by the draft Principles may be less than it seems. In particular, for common law contracts governed by choice of law rules such as those in the Restatement, it would be difficult for a party attacking a choice of law clause to expect success in arguing against its enforcement. If the clause selects a state that has a substantial relationship to the parties or the transaction, it will be upheld under the first prong of the test. If the state selected is one that does not have a substantial relationship to either the parties or the transaction, it is likely that the proponent of the choice of law will be able to argue that there is a reasonable basis for the choice of that state. After all, why have the parties agreed to have their contract be governed by the law of that state if there is no reasonable basis for it? As a result, the Restatement rule likely filters out very few exercises of party autonomy.

3. *What types of law may be designated by the parties?*

In light of the fact that the full title of the draft Hague Principles is "*The Hague Principles on Choice of Law in International Commercial Contracts,"* one would expect that the draft Principles would concern themselves with choices made by contracting parties as to which *law* —that is, which rules made by sovereign States— will govern their contract. The draft principles do, of course, provide rules for the choice of *law*, but they also provide for the selection by the parties of bodies of rules that do not emanate from a sovereign. Immediately after stating the rule of autonomy that the parties may choose the law that will govern their contract, the draft Principles tell us that "*In these Principles a reference to law includes rules of law*".

What are "rules of law?" The draft Principles are somewhat vague here, but the intent is clearly that the parties may not only designate law of a State but also "rules of law," such as the UNIDROIT Principles of International Commercial Contracts, that exist without being the law of any particular State.

ment efforts in which only the United States Virgin Islands enacted the new choice of law rule, however, the sponsors retrenched and the Official Text reverted to the earlier version requiring the transaction to bear a reasonable relation to the State specified by the parties.

[15] Restatement (Second) of Conflict of Laws § 187(2)(a).

Yet the text of the draft Principles contains no definition of the phrase "rules of law." Other documents prepared by the Working Group that prepared the draft Principles provide guidance, however. For example, in "*Choice of Law in International Contracts: Development Process of the Draft Instrument and Future Planning,"* the document by which the draft Principles were transmitted to the Council, the Working Group states the following:

The Working Group tentatively agreed that the chosen rules of law must be:

1. Distinguished from individual rules made by the parties; and
2. A body of rules.

The Working Group agreed to examine further characteristics of and limitations to the parties' choice of non-State law in the Commentary.

The Policy Document [included in the package presented to the Council] will report the agreement in the Working Group that the draft Hague Principles not include any express definition or limitation of the term "rules of law", as this provides the maximum support for party autonomy. The Policy Document will reflect the diversity of opinion in the literature on the definition of "rules of law" for choice of law purposes.[16]

The Policy Document addresses the matter as well. It states:

> The draft Hague Principles do not limit the parties to designating the law of a State; rather they allow for parties to select not only State laws but also "rules of law". The Working Group also agreed that the Principles would not include any express definitio or limitation of the term "rules of law", as this provides the maximum support for party autonomy, regardless of the method of dispute resolution (i.e., court or arbitration). However, the Working Group acknowledged that there are limits to the rules of law chosen by the parties. In particular, the chosen rules of law must be distinguished from individual rules made by the parties and must be a body of rules. These issues will be further examined in the Commentary on the basis of a very extensive literature and practice on this matter.[17]

The idea that parties should be able to designate "rules of law" in addition to law of sovereign States did not originate with the Working Group. Rather, such designations are common in the law of commercial arbitration, as exemplified by the UNCITRAL Model Law on International Com-

[16] Report of the Working Group, Annex I to Choice of Law in International Contracts: Development Process of the Draft Instrument and Future Planning, January 2012, p. 3.

[17] Policy Document, par. 16.

mercial Arbitration.[18] Yet, the matter is hardly without controversy. A similar principle was proposed for the Rome I Regulation,[19] but rejected.[20]

At least three issues are raised by the proposed power to designate non-State rules of law. The first issue, of course, is whether parties should be able to bypass sovereigns entirely and choose a body of law not emanating from a State. Second, if the parties are to be granted such a power, what qualifies as a "rule of law" other than law emanating from a State? The contrasting approaches of the European Commission and the Hague Conference Working Group are instructive in this regard. While the European Commission proposal for Rome I limited the choice to rules "recognized internationally or in the [European] Community,[21] the draft Hague Principles contain no "express definition or limitation," merely guiding the tribunal, in an unspecified way, to distinguish rules of law from "individual rules made by the parties" and requiring that the rules of law be a "body" of rules.

Third, bodies of non-State law are, by their nature, incomplete. Even a broadly comprehensive body of such rules, such as the UNIDROIT Principles of International Commercial Contracts, is not nearly as comprehensive as the full body of contract law of a moderately advanced legal system. Thus, if the parties designate a non-State body of rules, what is a tribunal to do if there is a dispute about an issue not addressed by those rules? Should the tribunal defer to the law of the State whose law would govern in the

[18] See UNCITRAL Model Law on Arbitration (1985, with amendments 2006), article 28(1). As pointed out in the Explanatory Note to article 28, "[b]y referring to the choice of 'rules of law' instead of 'law', the Model Law broadens the range of options available to the parties as regards the designation of the law applicable to the substance of the dispute. For example, parties may agree on rules of law that have been elaborated by an international forum but have not yet been incorporated into any national legal system. Parties could also choose directly an instrument such as the United Nations Convention on Contracts for the International Sale of Goods as the body of substantive law governing the arbitration, without having to refer to the national law of any State party to that Convention".

[19] The original proposal for Rome I submitted by the European Commission contained an article (3)(2), which read: "The parties may also choose as the applicable law the principles and rules of the substantive law of contract recognized internationally or in the Community." As noted by Professor Helmut Heiss, "This provision was intended to permit a choice of law in favor of non-State law, such as the UNIDROIT Principles of International Commercial Contracts (UNIDROIT Principles), the Principles of European Contract Law (PECL, or *Lando* Principles), or the Draft Common Frame of Reference insofar as it contains rules of contract law, including insurance contract law; not, however, the *lex mercatoria* in general." Helmut Heiss, *Party Autonomy*, in Franco Ferrari and Stefan Leible eds., Rome I Regulation: The Law Applicable to Contract Obligations in Europe, at 9-10.

[20] article 3(1) of the Rome I Regulation states simply that "A contract shall be governed by the law chosen by the Parties."

[21] See note text at notes 19-20, *supra.*

absence of the designation of non-State law by the parties? Should it try to imagine how the body that promulgated the non-State law would have resolved the matter?

4. *What limits are placed on the exercise of party autonomy by the parties?*

While the draft Principles might appear, at first glance, the give absolute dominion to the law (or rules of law) chosen by the parties, this is not the case. Rather, the draft Principles include limits on the exercise of that autonomy that are typical in this field. First, the Principles "*shall not prevent a court from applying overriding mandatory provisions of the law of the forum which apply irrespective of the law chosen by the parties*".[22] Second, a court may exclude application of a provision of the law chosen by the parties if "such application would be manifestly incompatible with fundamental notions of public policy (*ordre public*) of the forum.[23] Which state's fundamental policy?

It should be noted that the concept that a provision of the law chosen by the parties may be excluded if it is manifestly incompatible with fundamental notions of public policy has some difficulties associated with it. First, it is not so obvious which State's public policy is the basis of the comparison. The draft Principles refer to the law of the forum, but that is not the only possibility. In the United States, for example, the Restatement (Second) of Conflict of Laws provides that a choice of law is not effective "*application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which… would be the state of the applicable law in the absence of an effective choice of law by the parties*".[24]

Second, the notion of "*manifestly incompatible with fundamental notions of public policy*" is not very precise, leading the possibility of excessively broad readings. Is every provision of foreign law that reaches a result that could not have been reached by the parties in the reference State (whether that State is the forum State or the State whose law would govern in the absence of choice by the parties) one that is, by virtue of that violation of legal principles of the reference State, incompatible with fundamental notions of public policy? If so,

[22] Draft Principles, article 11(1).

[23] *Ibidem*, article 11(3).

[24] Restatement (Second) of Conflict of Laws § 187(2)(b). Similarly, the proposed revision to the Uniform Commercial Code provided that a choice of law "is not effective to the extent that application of the law of the State or country designated would be contrary to a fundamental policy *of the State or country whose law would govern in the absence of agreement*". Proposed Uniform Commercial Code § 1-301(f) (2001).

the party autonomy provided by the draft Principles would be limited in effect to rules of construction rather than rules of validity. It is the clear that the Working Group did not intend such a broad reading of the public policy limitation, inasmuch as the Policy Document provides that:

> There was unanimity within the Working Group that the primary goal of promoting party autonomy supports a generally restrictive approach to overriding mandatory rules and public policy. It was affirmed that any restriction on the application of the law chosen by the parties must be clearly justifiable and no wider than necessary to serve the objective pursued. Therefore, the draft Hague Principles emphasise the exceptional character of public policy and overriding mandatory rules…The Working Group agreed that such exceptional character should be dealt with in greater detail in the Commentary, rather than in the article of the draft Hague Principles.[25]

III. Other features of the draft principles

The draft Hague Principles address several other issues that are needed for a complete instrument, but which are less likely to require investment of significant time or effort by the Special Commission.

1. *Express or tacit choice*

The draft rules provide that "*A choice of law…must be made expressly or appear clearly from the provisions of the contract or the circumstances*".[26] Quite obviously this means that arguments that a contract contains a tacit, or implicit, choice of law will not prevail under the Principles. Moreover, the draft Principles quite properly distinguish between choice of law provisions and choice of forum provisions, and indicate that the latter is not, in itself, a choice of the law of the forum.[27]

2. *Formal validity of choice of law*

The draft Principles provide that "*A choice of law is not subject to any requirement as to form unless otherwise agreed by the parties*".[28] The main rule here is clear, but it is not clear, though, where an agreement to the contrary between the

[25] See Policy Document at paragraph 45.
[26] Draft Principles, article 3.
[27] *Idem.*
[28] Draft Principles, article 4.

parties would be found. After all, an agreement to the contrary found in the same document that contains the choice of law would be largely robbed of meaning since it is unlikely that that very document would not satisfy the form requirements mentioned in it. Perhaps, in some cases, the parties may have a master agreement of sorts that governs future contracts that may contain choice of law clauses.

3. *Law governing whether parties have consented to the choice of law*

The draft Principles provide that "*The consent of the parties as to a choice of law is determined by the law that would apply if such consent existed*".[29] Thus, in determining whether each party consented to the choice of law, the draft Principles direct a tribunal to apply the law that would apply if that consent existed (i.e., the putatively chosen law). This rule eliminates the possibility of secondary debates about which law governs the determination of whether the parties agreed to the choice of a particular law, but creates a theoretical risk of the stronger party forcing a choice of law of a State that has minimal requirements to demonstrate consent. It is for this reason, perhaps, that the rule is qualified by article 5(2). Paragraph (2) provides: "*Nevertheless, to establish that a party did not consent to the choice of law, it may rely on the law of the State where it has its place of business, if under the circumstances it is not reasonable to determine that issue according to the law specified in the preceding paragraph*". Paragraph (2) serves as a safety valve, of sorts, protecting parties from being found to have agreed to a choice of law that might be valid only under the law of the State chosen.[30] Nonetheless, this safety valve is quite subjective. While it provides needed flexibility to courts and other tribunals, it similarly undermines predictability and certainty.

4. *Autonomous nature of the choice of law*

What if the contract containing the choice of law is itself invalid (under the chosen law or some other law)? Does the invalidity of the contract, as a whole, invalidate the choice of law, perhaps requiring determination under a different law as to whether the contract is valid? article 6 of the draft Principles provides that *"A choice of law cannot be contested solely on the ground that the contract is not valid."* As explained in the policy paper:

[29] Hague Principles, article 5, par. 1.

[30] See discussion in Policy Document, par. 28.

> article 6 requires that the parties' choice of law should be subject to an independent assessment that is not automatically tied to the validity of the main contract. Thus, the parties' choice of applicable law would not be affected solely by a claim that the main contract is invalid. Instead, that claim of invalidity of the main contract would be assessed according to the applicable law chosen by the parties, provided that the parties' choice is effective. Further, arguments which seek to impugn the consent of the parties to the contract would not necessarily undermine the consent of the parties to the choice of law.[31]

Thus, in a sense, the choice of law clause is treated as a "contract within a contract," the validity of which is determined without reference to the validity of the vessel in which it is contained. This rules has analytical benefits, but may seem contrary to the general assumption that parties wish their contracts to be valid and, thus, do not intentionally choose governing law that would make their contract invalid. Contrary to that assumption, under article 6 a choice of law that renders the parties' contract invalid would be respected.

5. *No Renvoi*

As in most private international law instruments, the draft Principles contain a presumption against renvoi: "*A choice of law does not refer to rules of private international law of the law chosen by the parties unless the parties expressly provide otherwise*".[32] While anti-renvoi rules eliminate the possibility of a tribunal being "bounced" from one jurisdiction to another, they can also result in the application of the law of a State even in circumstances in which the courts of that State would not apply its law.

6. *Formal validity*

Unlike the provision concerning the autonomous nature of the choice of law, the provision in the draft Principles that addresses the formal validity of the choice of law does appear to have a bias in favor of enforcing the parties' choice. The provision states that "The contract is formally valid if it is formally valid under the law chosen by the parties, *but this shall not exclude the application of any other law which is to be applied by a court or arbitral tribunal to support formal validity*".[33] As explained the policy paper:

[31] Policy Document, par. 32.
[32] Hague Principles, article 7.
[33] Hague Principles, article 9(1) (emphasis added).

> In formulating the proposed liberal regime, the Working Group followed the well-established principle of favor negotii which seeks to avoid formal invalidity as far as possible. This implies that, in relation to formal validity only, the parties' contractual relationship may be determined by reference to connecting factors other than the law chosen by the parties. Those may include, for example depending on the venue, the law of either of the States where any of the parties or their respective agent is present when the contract is concluded, the law of the State where either of the parties has its habitual residence at the time of conclusion or the law of the State where the contract was concluded.[34]

7. *Application of draft Principles to assignments*

When one party assigns its rights under a contract to a third party, the presence of the third party creates multiple relationships. For example, if the obligee of a contractual obligation assigns its rights to an assignee, the obligor retains a contractual relationship with the assignor, the assignor and assignee have a contractual relationship pursuant to the contract of assignment, and the assignee that seeks to enforce the rights under the contract (acquired from the assignor) against the assignee is asserting rights under a contract to which it was not a party. Thus, while there are two contracts (the contract between the obligor and the assignor and the contract between the assignor and the assignee), there are three relationships as to which the applicable law must be determined. Not surprisingly, many find this to be a confusing area.

The draft Principles provide guidance in this area by delineating which issues are governed by the law chosen by the parties in the contract creating the obligation and which issues are governed by the law chosen by the parties in the contract of assignment. The former governs "*(i) whether the assignment can be invoked against the debtor, (ii) the rights of the assignee against the debtor, and (iii) whether the obligations of the debtor have been discharged*".[35] The latter governs only the "*mutual rights and obligations of the creditor and the assignee arising from their contract*".[36]

While there was some sentiment in the Working Group that these provisions should not be included in the draft Principles as they do not govern which law applies to a particular contract and, instead, merely clarify which

[34] Policy Document, par. 40.

[35] Draft Principles, article 10(b).

[36] *Ibidem*, article 10(a).

contract's governing law governs which issues in the context of the three-party relationship resulting from assignments, the prevailing view was to include them as a matter of guidance.[37] The Working Group considered, but rejected, providing similar guidance in the context of other multi-party situations such as such as subrogation, delegation, and set-off. Instead, it is anticipated that these issues will be addressed in commentary.[38]

IV. Areas of potencial difficulty

What issues will be most challenging for the Special Commission as it considers the recommendations of the Working Group? The issue most fraught with difficulty is likely to be the ability of the parties to designate non-State "rules of law" to govern their contract. While there is precedent for this in the world of commercial arbitration, the experience in the European Union in being unable to reach agreement on a similar provision is instructive. Moreover, even if the Special Commission decides to follow the recommendations of the Working Group and provide for designation of non-State law, decisions as to whether and how to define and limit the concept may be difficult. While there was general consensus in the Working Group that non-State rules of law such as the UNIDROIT Principles of International Commercial Contracts are included in the concept of "rules of law," there was little agreement as to how to generalize the definition, leading to the decision to leave the term undefined. Of course, the risk of too narrow a definition is that useful sources of non-State law will be excluded. On the other hand, too broad a definition could result in the inclusion of bodies of rules that do not have the same indicia of legitimacy as rules emanating from an international organization such as UNIDROIT.

In addition, two other issues that may prove challenging. First, while the limitations relating to mandatory provisions of law and incompatibility with public policy are generally accepted in most legal systems, the narrowness or breadth of their application differs among States; the application of the draft Hague Principles in this context will necessarily involve formulations of these limitations that emphasize the narrowness of application of the limitations, which may engender debate as to the appropriate role of these limitations. Second, the wide grant of party autonomy, allowing the parties to select the law of a State to which their transaction bears no relation, is broader than that currently in place in some States. While the Working

[37] Policy Document, par. 41.

[38] *Ibidem*, par. 43.

Group did not have difficulty reaching consensus on this point, the Special Commission, as a diplomatic entity rather than a collection of experts like the Working Group, may not have as an easy a time resolving the matter.

V. Future expansion of the hague principles?

In their current formulation, the draft Hague Principles address only situations in which the parties have designated the law governing their contract. They do not address what law is applicable to the contract in the absence of such a designation. Should the Hague Principles also cover situations in which the parties have not designated applicable law? Some members of the Working Group preferred a "complete instrument" such as the Rome I Regulation that would provide guidance in this context as well. Other members felt that the primary agenda of the project was the promotion and explication of party autonomy and that it might prove difficult to reach consensus on the principles determining the applicable law in the absence of a designation by the parties. At its April 2010 meeting, the Council on General Affairs and Policy of the Hague Conference decided that priority should be given to the development of rules for cases where a choice of law has been made.[39] Thus, while the current draft of the Hague Principles does not address determination of the applicable law in the absence of party choice, it is possible that, after completing its work in the context of party autonomy, the Working Group will return to this question.

[39] Hague Conference on Private International Law, Council on General Affairs and Policy, Conclusions and Recommendations Adopted by the Council (April 7th -9th, 2010) at p. 2.

FACILITATING EXPANSION OF CROSS-BORDER E-COMMERCE-DEVELOPING A GLOBAL ONLINE DISPUTE RESOLUTION SYSTEM (LESSONS DERIVED FROM EXISTING ODR SYSTEMS –WORK OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW)

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SUMMARY: I. *The Growing Need for Online Dispute Resolution (ODR).* II. *Existing and Proposed ODR Systems – Substantive Principles for Low Value High Volume Fast Track Claims.* III. *Anatomy of a Global ODR System.* IV. *Work of the United Nations Commission on International Trade Law.* V. *Multi-Stakeholder Model – UNCITRAL Consensus Building.*

I. THE GROWING NEED FOR ONLINE DISPUTE RESOLUTION (ODR)

1. *Birth of the Internet – Origin and Evolution of ODR Systems*

The advent of the Internet and subsequent development of the World Wide Web (or "the Web") ushered in a new era of understanding about the world in which we live and forever changed peoples' conceptions of human inter-

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action.[1] Today, individuals can communicate their ideas across continents, retrieve their news from multiple sources simultaneously, and conduct their business in a global marketplace. However, just as disputes can arise in the context of real-world interactions, so too can they arise in the context of online-world interactions.

Before the expansion of the internet, online conflicts were generally considered social issues, not requiring any particular process or technological platform. Users would sometimes get caught in "flame wars," where tempers would flare and insults were exchanged. Forum moderators might intervene to calm down emotions, but that was usually the extent of the response. With the rise of the commercial internet in the mid-1990s online conflicts took on a greater importance. Users were quite skeptical of these new online environments, and it became clear that widespread adoption would be difficult if users weren't assured that any problems they encountered would be quickly resolved. As a result, by the turn of the century ODR had become a priority for both business and government, and ODR providers emerged to handle the cases.

One early example was domain names. In the mid-1990s, the vast majority of the world's population had no idea what a domain name was, but by the end of the decade domain names were highly valued properties, with some selling for millions of dollars. The creation of enormous value from nothing over a very short period of time generated quite a few disputes.

In the real world, one business can often use the same or similar name as another business with little or no conflict, particularly in circumstances where the businesses are small, their goods or services are different, and the areas within which they do business are separate.[2]In the online world, how-

[1] From humble beginnings as a network project (which allowed no commercial use) for an agency within the Department of Defense known as the Advanced Research Projects Agency Network, ARPA, the internet expanded throughout the 1980's to include academic institutions such as the National Science Foundation (NSF), which established the National Science Foundation Network (NSFNET). Commercialization of the network and its transformation into the World Wide Web of today began in 1992 with the Congressional passage of the Scientific and Advanced-Technology Act which granted permission to the National Science Foundation to provide access to members of the education community with both academic and commercial ties. Thus, NSF's system could and did connect to commercial networks. *See* 42 U.S.C. §1862(g) (2002). For more information, *see* Leiner, Barry M. et al, *A Brief History of the Internet*, Internet Society, *available at http://www.isoc.org/internet/history/brief.shtml* (last accessed September 26th, 2011) *and* Gregg, Judd, Rogers, Harold, et al, *Relationship with the Internet Corporation for Assigned Names and Numbers*, Government Accountability Office (2000) (noting footnote 6) *available at http://www.gao.gov/new.items/og00033r.pdf* (last accessed Sept. 29, 2011).

[2] *See* Miller & Jentz, *Human Resource Management and E-Commerce: The Online Legal Environment*, 61-62 (West 2002).

ever, there is only one area of business – cyberspace.[3]Thus, conflicts between parties over the right to use a particular domain name were inevitable, and because of cyberspace's international scope, litigating such disputes was exceedingly burdensome and prohibitively expensive. As a result, devising alternative methods for resolving domain name disputes became necessary.

2. *Developments in e-Commerce and ODR*

The real driver for the expansion of ODR was and is commerce. Business-to-business ("B2B") and business-to-consumer ("B2C") e-commerce have grown exponentially in the past decade, due in large part to the rising number of individuals connected to the Internet.[4] In the late 1990s roughly between two and five percent of the world's population used the Internet.[5] By 2010, however, that percentage had increased to nearly thirty percent,[6] with users dispersed over every geographic region around the globe.[7] The acceptance of the Internet as a commercial trading platform also increased and continues to increase as the number of commercial transactions that consumers complete online continues its meteoric rise, so too does the amount these consumers are spending.[8]

From 1999 to 2009, for example, the value of e-commerce in the United States alone expanded nearly 400% from $33 billion in 1999, at best, to $182 billion in 2009.[9] At the same time, internet usage in the United States

[3] *Ibidem*, at 62.

[4] *Possible Future Work on Online Dispute Resolution in Cross-Border Electronic Commerce Transactions, Note by the Secretariat,* 43rd Sess., 21 June- 9 July, 2010, U.N. Doc. A/CN.9/706.

[5] *See Id*. (citing OECD, "Empowering e-consumers, strengthening consumer protect ion in the internet economy", 8-12 December 2009, DSTI/CP (2009)20/FINAL, para. 13).

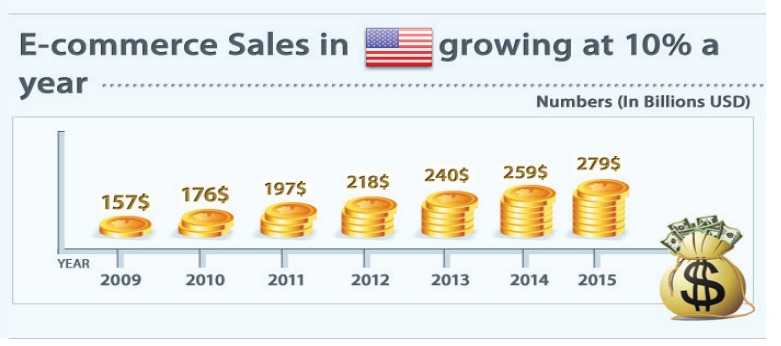
[6] *See Internet World Stats: Usage and Population Statistics* (updated as of April 5, 2011), available at *http://internetworldstats.com/stats.htm*.

[7] There were an estimated 1.4 billion internet users around the world at the end of 2008 and of the 1.6 billion people estimated in 2009, China hosted the largest number of users with 298 million, followed by the United States with 191 million, Japan with 88 million, and Africa with 53 million. While more than half of the population in developed countries has access to the internet, the corresponding share is on average 15-17 percent in developing countries. *Possible Future Work on Online Dispute Resolution in Cross-Border Electronic Commerce Transactions, Note by the Secretariat,* Official Records of the General Assembly, Forty-third Session, United Nations, New York 5 (2010) (A/CN.9/706).

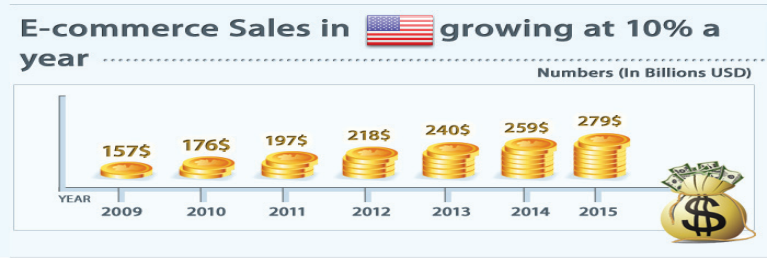
[8] See "E-Commerce and Internet Industry Over-view", *Plunkett Research, Ltd*., available at *http://plunketresearch.com/Industries/EcommerceInternet/EcommerceInternetStatistitcs/tabid/167/Default.aspx* (illustrating that consumers in the U. S. spent $131.8 billion on online commercial transactions in 2009, with a projected increase to $182.6 billion by 2012).

[9] *Idem*.

expanded from 36.6% of the population to an enormous 78.1%.[10] For the period 2009-2015, as indicated in the graph which follows, e-commerce sales in the United States are projected to rise 10% a year to a total of $279 billion by 2015.[11]



For the period of 2010-2015 worldwide, e-commerce sales are projected to rise at the rate of 19% per year from a total $572.5 billion to $1.4 trillion in 2015, as indicated in the graph which follows.[12]



This significant growth of e-commerce in the last decade and the projected continuing growth has spurred the development of various public and

[10] "World Bank Development Indicators", *World Bank*, last updated Jul. 28th, 2011 (made available by Google, Inc.) available at *http://www.google.com/publicdata/explore?ds=d5bncppjof8f9_&met_y=it_net_user_p2&idim=country:USA&dl=en&hl=en&q=internet+usage+statistics#ctype=l&strail=false&nselm=h&met_y=it_net_user_p2&scale_y=lin&ind_y=false&rdim=country&idim=country:USA&ifdim=country&hl=en&dl=en.*

[11] Khalid, "How Big is E-Commerce Industry", *The Invesp Blog*, available at *http://www.invesp.com/blog/* last visited Oct. 11th, 2011.

[12] *Idem.*

private initiatives aimed at providing redress to both businesses and consumers involved in domestic disputes arising out of online transactions.

Disputes arising in the online context can vary considerably and are often extremely difficult for courts to handle for a number of reasons, including: the high volume of claims; the contrast between the low value of the transaction and the high cost of litigation; the question of applicable law (in both e-commerce and consumer protection contexts); and the difficulty of enforcement of foreign judgments.[13] For years, courts all over the world have been promoting the use of Alternative Dispute Resolution ("ADR") as an effective, and even preferred, substitute for litigation.[14] ADR has been praised for its speed, flexibility, informality, and its solution-oriented (as opposed to blame-oriented) approach to conflict resolution.[15] However, traditional ADR methods, such as arbitration, have proven to be less than helpful tools for addressing the complications inherent in judicial resolution of web-based transactional disputes.

Unlike other dispute resolution processes, ODR is a fast, efficient, flexible, and inexpensive mechanism for handling e-commerce disputes, both at the domestic level and across borders. ODR processes provide businesses and consumers with a simple and reliable process through which to resolve conflicts arising out of their online interactions. ODR works the way the internet works, with resolutions built directly into websites and transaction flows, as opposed to being imposed by a central judicial authority that is completely separate from the online environment where the issue arose. ODR is also cross-jurisdictional and independent of any single set of laws or regulations, which is a better fit with the global nature of the internet. ODR offers clear benefits to both buyers and sellers: consumers appreciate the ability to get their issues resolved quickly and painlessly, and merchants like how consumers are more willing to make purchases (and pay higher prices) when they know a fair and painless resolution process is available to them. ODR also unlocks new demand from cross-border buyers who might have been averse to making purchases outside of their home geography without a clear resolution process. In essence, ODR is the best approach to providing redress and justice on the internet.

[13] Rule, Colin *et al*., "Designing a Global Consumer Online Dispute Resolution (ODR) System for Cross-Border Small Value-High Volume Claims—OAS Developments", 42 *U. C. C. L. J*., 2010, 221, 223-224.

[14] See Arno R. Lodder and John Zeleznikow, "Enhanced Dispute Resolution Through the Use of Information Technology", 8 *Cambridge University Press*, 2010.

[15] *Idem*.

II. Existing and Proposed ODR Systems – Substantive Principles for Low Value High Volume Fast Track Claims

1. *eBay*

eBay, an American Internet company with experience in business-to-business, business-to-consumer, and consumer-to-consumer transactions, launched in 1995 and has made numerous acquisitions over the years, including the PayPal payment service in 2002.[16] In 2009, eBay added to the dispute resolution services available through PayPal and initiated an on-eBay ODR platform for resolving "item not received" and "item not as described" claims.[17] Today, the eBay platform handles over 60 million e-commerce disputes annually. These disputes have an average value of$70-100 and they are processed through a Resolution Center that enables parties to resolve their problems amicably through direct communication. The number of disputes being resolved through eBay's online platform is expanding steadily as the transaction volume on the site increases, about 13% per year.[18] More than forty-five billion dollars in merchandise is sold on eBay each year and eBay has more than ninety-million active buyers and sellers, in 16 languages and 36 countries around the globe as well as Hong Kong.[19]

eBay also provides information to facilitate identification of reliable sellers. It makes extensive use of a Feedback system, which keeps market participants honest and avoids possible disputes. Currently eBay houses more than four billion feedback ratings left by transaction participants for each other.[20] The system allows participants to make informed choices about who they will trade with based on reports of positive or negative experience?[21]

[16] *Possible Future Work on Online Dispute Resolution in Cross-Border Electronic Commerce Transactions*, Note by the Secretariat, 43rd Sess., 21 June- 9 July, 2010, U.N. Doc. A/CN.9/706.

[17] *Idem.*

[18] *Corporate Fact Sheet: Q4 2010,2010,* eBay Inc., available at *http://ebayinc.com/content/fact_sheet/ebay_inc_corporate_fact_sheet_q4_2010_* (last visited Oct. 11th, 2011).

[19] eBay.com. identifies the following countries and Hong Kong as countries for which it has a website: Argentina, Austria, Australia, Belgium, Brazil, Canada, China, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, India, Ireland, Italy, Korea, Malaysia, Mexico, Netherlands, New Zealand, Norway, Philippines, Poland, Portugal, Russia, Singapore, Spain, Sweden, Switzerland, Taiwan, Thailand, Turkey, United Kingdom, Vietnam.; See *Idem*, for statistics on number of sales and users (last visited Oct. 11th, 2011).

[20] See Corporate Fact Sheet: Q4 2010, eBay Inc., available at *http://ebayinc.com/content/fact_sheet/ebay_inc_corporate_fact_sheet_q4_2010_* (last visited Oct. 11th, 2011).

[21] *How do I leave Feedback*?, eBay, Inc. (June 20th, 2011) available at at *http://pages.ebay.com/help.feedback/questions/leave.html* (last visited Sept. 26, 2011).

eBay assigns parties a "star" based on how many positive reviews they have received. For example, if the seller has 10 to 49 positive ratings, they get a yellow star and if the seller has 50 to 99 positive ratings they get a blue star.[22] A seller with a million or more positive ratings is entitled to a "shooting silver star".[23]This system allows buyers to see at a glance, how trusted the seller is by other market participants. Merchants have a strong incentive to take good care of their buyers so as to avoid receiving negative feedback, which can harm their future commercial prospects.

In the feedback system, like the dispute resolution system, buyers and sellers are treated differently. Buyers can leave positive, neutral, or negative ratings while sellers can only leave short comments and positive ratings.[24] Although this is a system which exacts honesty from sellers by the threat of a negative rating, eBay is very clear that feedback extortion and manipulation is not allowed.[25] For example, buyers cannot use threats of poor feedback to demand a refund or some additional good or service which was not included in the purchase price.[26] Similarly, sellers aren't allowed to demand positive Feedback from buyers in return for expedited shipping or other services.[27] While eBay does not issue trustmarks to vendors, prospective buyers nevertheless are able to identify reliable vendors in any one of the 36 countries plus Hong Kong in which eBay operates based on the billions of feedback ratings left by previous transaction participants. This achieves two of the main goals of any trustmark system: empowering buyers with information, and facilitating compliance of vendors with awards so that they will receive positive ratings in the feedback system.

Under the eBay Buyer Protection Policy, buyers can file a report when they have not received an item they purchased or if the item was received but did not match the seller's description. Only consumers who buy items from the U. S. eBay site and use an eligible payment method may file a claim and that claim must be based on a "good faith dispute" between the buyer and seller of "goods".[28] Sellers can also file through eBay when they

[22] *Idem.*

[23] *Idem.*

[24] *Idem.*

[25] *Idem.*

[26] All About Feedback Policies, eBay, Inc. (June 20th, 2011) available at *http://pages.ebay.com/help/policies/feedback-ov.html* (last visited Sept. 26, 2011).

[27] *Idem.*

[28] Unpaid Item Policy, eBay, Inc. available at *http://pages.ebay.com/help/policies/unpaid-item.html* (last visited Sept. 22nd, 2011).

have not received a payment or when they need to cancel a transaction.[29] The types of claims for buyers offered for resolution under the policy include:

1. The buyer did not receive the items within the estimated delivery date, or

2. The item received was wrong, damaged, or different from the seller's description. For example:

i. Buyer received a completely different item.

ii. The condition of the item is not as described.

iii. The item is missing parts or components.

iv. The item is defective during the first use.

v. The item is a different version or edition displayed in the listing.

vi. The item was described as authentic but is not.

vii. The item is missing major parts or features, and this was not described in the listing.

viii. The item was damaged during shipment.

ix. The buyer received the incorrect amount of items.[30]

The eBay Buyer Protection Policy is not a product warranty of any kind and applies only to the transaction. It covers only the original purchase price and the shipping cost. It does not cover "damages".[31] The buyer therefore retains rights to bring suit in an appropriate forum to recover "damages". eBay also has a more limited dispute resolution system for sellers which permits them to file claims against buyers, but only for nonpayment of an item.[32]

[29] What to do When a Buyer Doesn't Pay (Unpaid Item Process), eBay, Inc. available at *http://pages.ebay.com/help/sell/unpaid-items.html* (last visited Sept. 22nd, 2011).

[30] Unpaid Item Policy, eBay, Inc., available at *http://pages.ebay.com/help/policies/unpaid-item.html* (last visited Sept. 22nd, 2011).

[31] *Idem*.

[32] eBay sellers are able to initiate claim against non-paying buyers, strictly for the recovery of payment. After an auction closes a buyer has four days to initiate payment. If payment is not received in that period, the seller can open an unpaid item case in the Resolution Center. If the case is closed without the buyer paying, there are very few remedies or alternatives for the seller. eBay may credit the seller for the final value fee and may choose to not charge the seller the listing fee if they choose to relist the item. Additionally, eBay may take action against the buyer including indicating a lack of payment on the buyer's account. The time restrictions on the filing of claims are expressed in terms of when payment was made, such as "within 45 days of payment."; See *What to do When a Buyer Doesn't Pay (Unpaid Item Process)*, eBay, Inc. available at *http://pages.ebay.com/help/sell/unpaid-items.html*, last visited Sept. 22nd, 2011 (for general details); See also *Unpaid Item Policy*, eBay, Inc. available at *http://pages.ebay.com/help/sell/unpaid-items.html*, last visited Sept. 22nd, 2011 (for general details); See also Unpaid Item Policy, eBay, Inc. available at *http://pages.ebay.com/help/policies/unpaid-item.html*, last

2. *Concilianet*

In Mexico, Concilianet, an online dispute resolution system run by the Consumer Protection Federal Agency (Office of the Federal Prosecutor for the Consumer, Profeco), has been established to strengthen the protection and defense of consumers' rights. Concilianet provides consumers who have purchased goods or services, either electronically or by traditional means with a cost-effective way to initiate and resolve complaints or claims against participating suppliers via a virtual Internet platform.[33]

Concilianet began as a pilot program in 2008 with two participating providers and moved to small deployment with five providers in 2009.[34] Today, Concilianet has expanded to full national implementation with 26 participating suppliers.[35] According to Profeco, the use of ODR in the initial stages reduced the time for resolving disputes by nearly 50 percent and increased the number of settlements to about 96 percent. Furthermore, 97 percent of the consumers polled reported that they would utilize the Concilianet procedure again.[36]

Under the Concilianet system, a consumer is provided with a username (i.e., his or her email address) and a valid password. This data forms the electronic signature, which will identify the consumer every time he or she uses the online resolution mechanism. The consumer may then file a claim based on any disagreement with a statement of use, e.g., non-compliance with terms previously agreed to in the sale or supply of the product or service, such as:

1. Breach of warranty,

visited Sept. 22nd, 2011, and How Sellers May Be Protected From Losing a Case, eBay, Inc., June 20th, 2011, available at *http://pages.ebay.com/help/policies/buyer-protection.html#policy1*, last visited Sept. 26, 2011 and Conditions Under Which a Case Can Be Filed, eBay, Inc., June 20th, 2011 available at *http://pages.ebay.com/help/policies/buyer-protection.html#policy1*, last visited Sept. 26th, 2011 (for more specific details).

[33] Rogers, Rule and Del Duca, Designing a Global Consumer Online Dispute Resolution (ODR) System for Cross-Border Small Value-High Volume Claims – OAS Developments, 42 *U. C. C. L. J.*, 2010, 221, 224 and 225.

[34] *Idem.* The Pilot program started with Aero Mexico and Hewlett Packard. The small deployment included Aero Mexico, Hewlett Packard, Volaris, Office Depot, and Gas Natural.

[35] *Idem*. Aero Mexico, Federal Electricity Commission, Deremate.com, Dorians, Factories in France, Mexico's Natural Gas, Geo Group, Metropolitan Group, HP, Hypercable, LAN, Liverpool, LG Mexico, Mabe, Natural Maxigas, Free market, Mixup, Office Depot, Redpack, Sadasi, Saks, Sanborn's, Sears, Telcel, Telecable, Volaris. The Federal Electricity Commission is the only publicly run company.

[36] *See Welcome to Concilianet*, PROFECO, 2007, available at *http://concilianet.profeco.gob.mx/concilianet/faces/inicio.jsp,* translated using Google Translate on Sept. 19th, 2011.

2. Breach of contract, or
3. Refusal to surrender.[37]

Concilianet does not cover claims for damages; however, consumers are not barred from bringing actions for damages in court. In fact, Concilianet specifically advises consumers to bring actions for damages in court. Once the consumer has submitted a complaint, Profeco sends a response via e-mail within 5 days. The consumer is responsible for periodically reviewing Concilianet's website in order be aware of the status of his or her complaint. Once Profeco has determined that it is competent to hear the complaint it will schedule the date and time for the settlement hearing, in which the consumer must appear through Concilianet. The settlement hearing takes place in Concilianet' s virtual courtroom, where the consumer, the supplier, and the mediator are all present in order to find the best and most expeditious solution to the complaint.[38]

3. *Internet Corporation for Assigned Names and Numbers (ICANN)*

Since 2000, the Internet Corporation for Assigned Names and Numbers (ICANN) has been operating an online arbitration system to resolve domain name disputes across borders. Instead of forcing a party engaged in trademark infringement to file suit in court, a party can simply submit a complaint to an ICANN-approved dispute resolution provider and resolve the entire matter online.[39] ICANN's domain name dispute resolution system has been highly successful and it resolves thousands of disputes across borders annually.[40]

ICANN lists the types of claims offered for resolution through its online dispute resolution as follows:

1. A Domain Name Transfer
2. An Unsolicited Renewal or Transfer Solicitation
3. Accreditation
4. An Unauthorized Transfer of Your Domain Name
5. A Trademark Infringement
6. A Uniform Domain Name Dispute Resolution (UDRP) Decision

[37] See *Use Provisions*, PROFECO, 2007, available at http://*concilianet.profeco.gob.mx/concilianet/faces/que_es.jsp*, translated using Google Translate on Sept. 19th, 2011.

[38] *Idem*.

[39] See *ICANN Domain Name Dispute Resolution Policies*, ICANN available at *http://www.icann.org/en/udrp/* last visited Sept. 05th, 2011.

[40] *Idem*.

7. A Registrar Service
8. Inaccurate Who is Data
9. Spam or Viruses
10. Content on a Website[41]

Although ICANN offers an array of online dispute proceedings, the remedies are very limited. The remedies are primarily limited to the cancellation or change of a registered name. ICANN has an approval process for selecting providers and requires that a provider have a track record, list of potential panelists, and requested limitation on the number of proceedings.[42]

To initiate a dispute, the Complainant must give the Respondent actual notice about the complaint. Once the Respondent has received actual notice, they have 20 days to respond, The Complainant is responsible to pay all fees.[43] The selected panel will initiate and conduct the proceedings. Panelists are required to be impartial and independent. The panel can determine what remedies to grant. All decisions by the panel are published over the internet. The panel must forward its decision to the provider within 14 days and the provider must relay the decision to the opposing parties within three days.[44]

4. *Better Business Bureau (BBB)*

"The Council of Better Business Bureaus (CBBB) is a not-for-profit organization representing its 122 member Better Business Bureaus throughout the United States and Canada".[45] A local Better Business Bureau (BBB) office is a nonprofit organization supported by local businesses. BBBs assist in the resolution of disputes between a business and its customers. When a marketplace dispute arises, BBBs work with the business and the customer to reach a resolution using various dispute resolution (DR) processes, each of which provides an alternative to going to court. Through the use of an online complaint system, BBBs help to resolve thousands of complaints each year.[46]

[41] See *Have a Problem? Dispute Resolution Options*, ICANN, available at *http://www.icann.org/en/dispute-resolution/* last visited Aug. 30th, 2011.

[42] *Idem*.

[43] *Idem*.

[44] *Idem*.

[45] Cole, Steven J. and Underhill, Charles I., "Fifteen Years of ODR Experience: The BBB Online Reliability Trust Mark Program", 42 *U. C. C. L. J.*, 2010, 443, 443- 444.

[46] See, "Dispute Resolution Processes and Guides", *Council of Better Business Bureaus*, 2011, available at *http://www.bbb.org/us/Dispute-Resolution-Services/Process/*, last visited Oct. 11th, 2011.

Most BBBs offer several dispute resolution methods to help resolve disputes, such as conciliation, mediation, informal dispute resolution, conditionally-binding arbitration, and binding arbitration.[47] The BBB Online Complaint System handles disagreements between business and their customers; it will not resolve workplace disputes, discrimination claims, matters that are or have been litigated, or claims about the quality of health or legal services.[48]

A customer's submitted claim is forwarded to the business within two business days. The business is then asked to respond within 14 days, and if a response is not received, a second request is made.[49] The customer is notified of the business's response once the BBB receives it, or is notified that no response was sent. Complaints are usually closed within 30 business days.[50]

The BBB also uses a trustmark system to help consumers in identifying reliable vendors.[51] BBB allows vendors who meet the BBB's standards to be "accredited".[52] These standards include being "trustful", "honest in advertising", and "transparent".[53] Additionally, vendors agree to "fulfill contracts

[47] In conciliation a BBB staff will collect factual information from both parties to a dispute and work to encourage open communication between them. In mediation, a BBB will provide a professionally-trained mediator to talk with the parties and guide them in working out their own mutually-agreeable solutions. In IDS, a BBB will provide a professionally-trained hearing officer who will listen to both sides and make a non-binding decision on how to resolve the dispute. In conditionally-binding arbitration, a BBB will provide a professionally-trained arbitrator who will listen to both sides and make a decision on how to resolve the dispute that is binding on the parties only if the customer accepts the decision. In binding arbitration, a BBB will provide a professionally-trained arbitrator who will listen to both sides, weigh the evidence presented and make a decision on how to resolve the dispute that is binding on all parties. When participating in conciliation, mediation, or informal dispute settlement (IDS) with a BBB, the complaining party is free to take his or her dispute to court if unable to resolve the issue. When participating in conditionally-binding arbitration, the customer is free to go to court if he or she does not like the decision, but the business must abide by the decision so long as the customer accepts it. When participating in binding arbitration, the arbitrator's decision cannot be reviewed by a court except under very limited circumstances. The BBB will contact the complaining party to let him or her know what type of dispute resolution process is applicable to the particular issue at hand.

[48] See, "The Better Business Bureau Online Complaint System", *Council of Better Business Bureaus*, 2011, available at *https://www.bbb.org/file-a-complaint/*, last visited Oct. 11th, 2011.

[49] *Idem*.

[50] *Idem*.

[51] Cole, Steven J. and Underhill, Charles I., "Fifteen Years of ODR Experience: The BBB Online Reliability Trust Mark Program", 42 *U. C. C. L. J.*, 2010, 443, 456 and 457.

[52] See, "The Better Business Bureau Online Accreditation Standards", *Council of Better Business Bureaus*, 2011, available at *http://www.bbb.org/us/bbb-accreditation-standards/*, last visited Oct. 11th, 2011.

[53] *Idem* (noting that in a global online system the compliance with these standards of conduct could be ascertained through an eBay feedback type system); *see supra* note 26).

signed and agreements reached as well as honor representations by correcting mistakes as quickly as possible".[54]Accredited businesses are allowed to display BBB Accredited Business marks (i.e. trustmarks) in their stores, online or in other advertising.[55] This trustmark signals to the consumer that the business meets BBB standards and that BBB dispute resolution will be available to them if they transact with that business.[56]

5. *Organization of American States (OAS)*

In February, 2010, the U.S. Department of State submitted to the OAS a proposal focused on building a practical framework for consumer protection through *inter alia* an OAS-ODR Initiative for electronic resolution of cross-border e-commerce consumer disputes: a system "designed to promote consumer confidence by providing quick resolution and enforcement of disputes across borders, languages, and different legal jurisdictions".[57] The OAS-ODR Initiative utilizes a central clearinghouse, which, in conjunction with national consumer authorities and national administrators, maintains a single database of certified ODR providers, manages the dispute resolution process, and acts as the central focal point for electronic communication among the parties.[58] The initiative also attempts to simplify enforcement issues by providing for ODR in the vendor's locale. The vendor opts-in to the system with national administrators in the area where the vendor does business and the seat of arbitration for the process is the vendor's State.[59] In the event of non-compliance, the award may be enforced by the national consumer authority or national administrator in the vendor's home country by taking direct enforcement action, requesting assistance from payment networks, or referring the case to collection agencies.[60]

Under the OAS-ODR Initiative, a consumer would be able to file a cross-border complaint online against a registered vendor in another par-

[54] *Idem*.

[55] Cole, Steven J. and Underhill, Charles I., "Fifteen Years of ODR Experience: The BBB Online Reliability Trust Mark Program", 42 *U. C. C. L. J.*, 2010, 443, 456 and 457.

[56] *Idem.*

[57] See Rogers, Rule *et al.*, "Designing a Global Consumer Online Dispute Resolution (ODR) System for Cross-Border Small Value-High Volume Claims – OAS Developments", 42 *U. C. C. L. J.*, 2010, 221, 234.

[58] *Possible Future Work on Online Dispute Resolution in Cross-Border Electronic Commerce Transactions, Note by the Secretariat,* 43rd Sess., 21 June- 9 July, 2010, U.N. Doc. A/CN.9/706.

[59] *Idem*.

[60] *Idem*.

ticipating State. This initial complaint process would involve the buyer completing an online form that includes a checklist of the types of claims available for resolution, including:

1. Non-delivery of goods or non-provision of services;
2. Late delivery of goods or late provision of services;
3. Vendor sent wrong quantity;
4. Delivered goods were damaged;
5. Delivered goods or provided services were improper;
6. Vendor made misrepresentations about goods;
7. Vendor did not honor express warranty; or
8. Vendor improperly charged or debited buyer's account.[61]

Once filed, the complaint would then proceed in the following successive phases: the initiation/negotiation phase, the online arbitration phase, and the award phase.[62] During the initiation/negotiation phase, the buyer and vendor would be provided the opportunity to exchange information and proposals, and negotiate —through electronic means— a binding settlement.[63] If an amicable settlement could not be reached during this initial phase, the case would then be brought to the arbitration phase, at which time an online arbitrator would be appointed by a qualified ODR provider where the vendor is located to evaluate the case and either conduct a facilitated settlement (i.e. mediation) or, if necessary, issue a final and binding arbitral award.[64]

6. *Chargeback Procedures*

Chargebacks are ODR procedures which can be used by buyers if a credit card is used for payment of any type of purchase whether in a store or online. Chargebacks can also be used for purchases made in the service industry, such as at a hotel or restaurant. While each credit card company uses a slightly different process, the general process used by all companies is very similar. Consumers initiate a chargeback after an issue arises following a purchase. Examples of transaction issues that might lead to chargebacks are non-delivery of goods or delivery of substantially different goods. After the consumer contacts their credit card issuer and files a chargeback, the funds are immediately reversed from the seller's merchant account back to

[61] *See* Rogers, Rule *et al.*, "Designing a Global Consumer Online Dispute Resolution (ODR) System for Cross-Border Small Value-High Volume Claims – OAS Developments", 42 *U. C. C. L. J.*, 2010, 221, 261.

[62] *Ibidem*, at 236.

[63] *Idem*.

[64] *Idem*.

the buyer. The merchant has the ability to "re-present" the charge, disputing the buyer's assertions, which results in another immediate reversal of the funds back to the seller. The process can continue in this manner for several iterations, with fees charged for each additional reversal. Cases that continue back and forth may eventually be arbitrated by the card network (e.g. Visa or MasterCard), but that arbitration can be quite expensive, so there is a strong incentive to either resolve or give up the case prior to reaching that point.[65]

In the United States, federal law requires credit card companies to allow chargebacks.[66] To take advantage of this system, a buyer must notify the credit card company of the disputed charge within sixty days of receiving notice of the charge from the credit card company.[67] If the buyer alleges that the charge is incorrect because the goods were not delivered "in accordance with the agreement made at the time of the transaction," the credit card company must undertake an investigation to determine whether or not that is true.[68] Under these regulations chargebacks extend only to consumer and not to business transactions.[69] In Europe, credit card companies are not required to provide chargeback services.[70] Although chargebacks are not as prevalent in Europe as in the United States, they are still used fairly frequently.[71] The availability of chargebacks in countries where such a mechanism is not mandated indicates their popularity and usefulness to both credit card issuers and credit card users.[72]

Each credit card company currently has a slightly different chargeback system. For example, the types of claims which they process vary. Visa, MasterCard, and Discover for example, have claims for "Illegible transaction receipt," while American Express does not.[73] However, generally the companies have claims for the same types of transactions. Examples of these in-

[65] *See Chargebacks and Dispute_Resolution*, Visa, Inc., 2011, available at *http://usa.visa.com/merchants/operations/chargebacks_dispute_resolution/#anchor_2*, last visited Oct. 11th, 2011.

[66] 15 U. S. C. A. §1666 (2010); *See* 12 C. F. R. pt. 205.14 (1999); *See also* Perritt, Henry H., *Dispute Resolution in Cyberspace: Demand for New Forms of ADR*, 15 Ohio St. J. on Disp. Resol., 2000, 675, 692.

[67] 15 U. S. C. A. §1666(a), 2010.

[68] 15 U. S. C. A. §1666(a)(3)(B)(ii), 2010.

[69] *See* 12 C. F. R. §226.3, 2011; *see also* Perritt, Henry H., *Dispute Resolution in Cyberspace: Demand for New Forms of ADR*, 15 Ohio St. J. on Disp. Resol., 2000, 675, 690.

[70] Perritt, Henry H., *Dispute Resolution in Cyberspace: Demand for New Forms of ADR*, 15 Ohio St. J. on Disp. Resol., 2000, 675, 693.

[71] *Idem.*

[72] *Idem.*

[73] See Chargebacks and Dispute Resolution, VISA INC., 2011, available at *http://usa.visa.com/merchants/operations/chargebacks_dispute_resolution/#anchor_2*.

clude fraudulent and counterfeit transactions, declined authorizations and failure to receive merchandise.[74]

While many of the reasons for a chargeback do not include any buyer-seller interaction, there are a number of situations in which the buyer-seller interaction may lead to a chargeback.[75] The four most common reasons for a chargeback which involves interaction of buyers and sellers are a) non-delivery, b) delivery of non-conforming goods or services, c) charges after cancellation of a recurring transaction, and d) duplicate processing of a single transaction.[76]

Consumers cannot receive damages in a chargeback process. They will either be re-billed, with the new bill showing an absence of the disputed charge, or their account will be credited with the disputed amount.[77]

Quite often a payment facilitator is also involved in the chargeback process. For example, PayPal, a company which helps consumers pay electronically online, does not begin or administer chargebacks, but does facilitate the process from the seller's side.[78] After a buyer has independently initiated a chargeback with their credit card issuer, the card network contacts PayPal and PayPal places a hold on the seller's PayPal funds related to the chargeback.[79] PayPal then requests information from the seller that could help to determine whether the charge should be "re-presented" to the buyer, effectively disputing the buyer's account of the issue.[80] PayPal uses the chargeback system as a separate process, distinct from another dispute resolution process handled entirely by PayPal. Buyers must choose which system to use, the PayPal claims process or the credit card chargeback process.[81] They may not pursue claims using both systems,[82] so if the buyer initiates a PayPal claim process and subsequently files a chargeback through their card issuer, the PayPal claim is immediately shut down and the chargeback process takes precedent. In dealing with Chargebacks, PayPal works only with the seller, be-

[74] *Idem.*

[75] *Idem.*

[76] *Idem.*

[77] See Chargeback Cycle, VISA INC., 2011, available at *http://usa.visa.com/merchants/operations/chargebacks_dispute_resolution/chargeback_cycle.html.*

[78] See Your Guide to Chargebacks, PAYPAL (2011), *available at https://cms.paypal.com/us/cgi-bin/?cmd=_render-content&content_ID=security/chargeback_guide.*

[79] *Idem.*

[80] *Idem.*

[81] *See PayPal User Agreement*, PAYPAL (2011), *available at https://cms.paypal.com/cgi-bin/marketingweb?cmd=_render-content&content_ID=ua/BuyerProtection_full&locale.x=en_US#13. Protection for Buyers.*

[82] *Idem.*

cause the buyer is working through their card issuer.[83] PayPal specialists help sellers by disputing the chargebacks on their behalf, because PayPal is actually the merchant of record in the transaction.[84] Some credit card companies also have detailed instructions on their websites dedicated to helping sellers avoid and dispute chargebacks.[85]

7. *E-Commerce Redress Interchange (ECRI) and NGO Fast Track Substantive Principles - Common ODR Data Standards*

The E-Commerce Redress Interchange (ECRI) Working Group, has proposed a standardized communication system in order to facilitate the growth of global ODR systems.[86] This proposal would include textual information localized by language, but would also include "graphic and audio communications as appropriate".[87] The group notes that the "ECRI standard *can be incorporated with automatic translation tools* to offer maximum flexibility to parties in choosing their preferred method of communication", (emphasis original) which suggests a potential synergy with online translation services like those offered by eBay, which provides instantaneous online translation into 16 languages, and Google, which provides instantaneous online translation into 58 languages.[88]

A second group consisting of 20 non-governmental organizations (NGO's) and a member of the European Parliament[89] has submitted a pro-

[83] *See Your Guide to Chargebacks*, PAYPAL (2011), *available at https://cms.paypal.com/us/cgi-bin/?cmd=_render-content&content_ID=security/chargeback_guide.*

[84] *Idem.*

[85] *See Preventing Chargebacks*, PAYPAL *(2011)*, *available at http://usa.visa.com/merchants/operations/chargebacks_dispute_resolution/preventing_chargebacks.html, https://cms.paypal.com/us/cgi-bin/?cmd=_render-content&content_ID=security/chargeback_guide.*

[86] Loebl, Zbynek *et al.*, *The E-Commerce Claims Redress Interchange (ECRI) Working Group Standards Proposal*, ECRI WORKING GROUP (2010) available at *http://www.odr2012.org/files/ECRIstandard.doc*.

[87] *Ibidem* at 1.

[88] *See Ibidem* at 1. See also What is Google Translate?, *Google, Inc.*, available at *http://translate.google.com/about/index.html*, last visited Sept. 19th, 2011, and eBay's Homepage available at *http://www.ebay.com/*, last visited Oct. 14th, 2011.

[89] The participating NGO's and member of the European Parliament are: The American National Standards Institute; Arbeitsgruppe Rechtsinformatik, Institut für Europarecht, Internationales Recht und Rechtsvergleichung, Universität Wien; Center of Negotiation and Mediation of Law Faculty at UNAM (Mexico); Centre for Socio-Legal Studies, University of Oxford; ADR.eu, Czech Arbitration Court; Chartered Institute of Arbitrators (Singapore) Limited; Dispute Resolution Division, Council of Better Business Bureaus, Inc.; Faculty of Law, Potchefstroom Campus, Northwest University, Potchefstroom, South Africa; Gould Ne-

posal to the United Nations Commission on International Trade Law's Working Group III.[90] This proposal recommends creation of "a comprehensive set of standardized codes for dispute cases".[91] These codes would be numeric and would "[provide] redress in low value, high volume e-commerce transaction disputes".[92] These codes would facilitate communication between parties that do not share a common language by providing a common reference for them to state their grievances and desires.[93]

The proposal states that the initial deployment must be limited in scope, focusing upon four primary fact-cases: 1. Goods/services not delivered. 2. Goods/services not ordered. 3. Goods/services not as described. 4. Settlement not complied with.[94] These four fact-cases could then be "enhanced step by step as the system develops".[95]

III. Anatomy of a Global ODR System

These examples of current ODR systems and coordination efforts give an indication of the current global landscape and what types of solutions have been most successful in scaling to higher volumes and lasting for multiple years. However, it is clear that these systems are still quite disconnected and uncoordinated. To most effectively respond to the challenge of global redress and consumer protection a broader, coordinated ODR system is clearly need, with efficient mechanisms for communicating standardized procedures and case details across borders and enforcing outcomes.

gotiation & Mediation Program, Stanford Law School; Hong Kong Internet Forum; Hong Kong Institute of Arbitrators (HKIArb); Institute of Commercial Law, Penn State Dickinson School of Law; Institute of Law and Technology, Faculty of Law, Masaryk University; International Association for Commercial and Contract Management (IACCM); International Law Department of China Foreign Affairs University; ODR LatinoAmerica; The School of Law at the University of Leicester; and Universitat Oberta de Catalunya (Spain); Zuzana Roithova (Member of the European Parliament), the National Center for Technology and Dispute Resolution and the Pace Law School; *See also* Institute of International Commercial Law, et al, *Creating a Cross-Border Online Dispute Resolution Data Exchange System*, U.N. Comm. on Int'l. Trade Law, Working Group III (2011) (note submitted to, but not adopted by, Working Group III) available at *http://www.odr2012.org/files/system.docx*.

90 *Idem*.

91 Institute of International Commercial Law, et al, *Creating a Cross-Border Online Dispute Resolution Data Exchange System*, U.N. COMM. On Int'l. Trade Law, Working Group III, 2011 (note submitted to, but not adopted by, Working Group III) at 2.

92 *Ibidem,* at 1.

93 *Idem*.

94 *Ibidem,* at 2.

95 *Idem*.

The design we propose for this system draws from the lessons learned in all the ODR implementations just described. From eBay we observed how to automate a resolution system so that it can handle millions or tens of millions of cases by leveraging software. From Concilianet we noted how conciliation and mediation approaches can be combined with synchronous interactions to generate very high satisfaction. From ICANN we learned some of the risks of selection bias, and the benefits of a truly global roster of ODR providers so as to work multiple cultural contexts. The BBB demonstrates the power of having offices in each geography and the marketing effectiveness of a strong brand. The OAS design, as well as the ECRI standard, highlights the need for clear protocols to facilitate cross-border coordination. In this section we attempt to knit together these lessons and lay out a blueprint for how such a global system could be designed and implemented.

1. *What is a Global ODR System?*

In describing the anatomy of a global ODR system, we mean a global system for disputes related to cross-border e-commerce transactions. Functioning cross-border ODR means that ODR programs participating in the system will:

- Meet consistent criteria and operate under similar rules;
- Either be accredited or reviewed by national regulator(s) prior to their participation;
- Be assisted by interlinked consumer centers providing guidelines to consumers and outreach to domestic online sellers;
- Incorporate common ODR procedural language/communication standards understandable to all ODR providers and consumer centers, in order to facilitate resolution by the parties as well as resolution by third-party mediation/arbitration; and
- Operate as an online platform, implementing common ODR language.

2. *Components of a Global ODR System*

Any future cross-border ODR system must provide:

- Minimum common ODR rules and standards for ODR providers and neutrals, i.e. results of the work of UNCITRAL Working Group III (hereinafter "Working Group III");[96]
- Cross-border ODR infrastructure interconnecting all ODR stakehold-

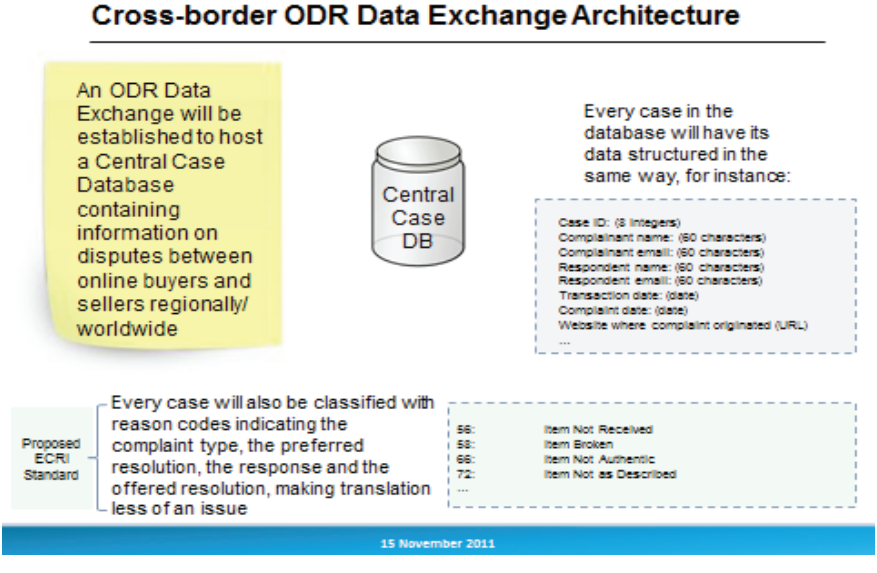
[96] *See* part IV, *infra*, for further discussion of the work of UNCITRAL.

ers and

- Available way to set up and incorporate the Minimum Common ODR Rules and the Cross-Border ODR Interconnecting Infrastructure Rules while at the same time supporting the establishment of various ODR programs on a global or regional basis competing and complementing one another.

3. *Cross-Border ODR Infrastructure*[97]

It is becoming increasingly clear that such a cross-border resolution system will only be possible if there is a complementary system enabling the various resolution end-points (e. g. government agencies, buyers and sellers, online dispute resolution service providers, entities involved in enforcing judgments etc.) to exchange information in real time in multiple languages. This information may include new dispute filings, messages between disputants, and proposed solutions, resolution status, and agreement adherence. This information exchange system will not provide case adjudication or enforcement of outcomes; it will only enable data about disputes to be shared around the globe in multiple languages in an efficient and seamless manner. Structurally, the cross-border ODR data exchange architecture is illustrated as follows:



[97] This part of the article is based on a paper authored and delivered at the May 2011 Working Group III meeting by Colin Rule, Zbynek Loebl, Vikki Rogers, LeahWing and Ethan Katsh. *See also* footnote 89*supra*.

The data exchange architecture may operate in the following way:

Immediate Roles of the Database

- Common Data Structure. A common data structure will be created and used, vetted, and agreed upon by all the participants in the system. This structure will describe each individual piece of data that will be included in a single case, along with specified data types, lengths, and dependencies.
- Comprehensive Set of Standardized Codes. As a necessary component of this data structure, the participants will agree on a comprehensive set of standardized codes for dispute cases. These standardize codes will also encompass reason and resolution codes and also codes used by the parties in the negotiation and self-directed dispute resolution stages of their dispute. These numeric codes will correlate to every common dispute, response, and resolution type, so that when a case is shared between nodes the reason code will describe the exact nature of the dispute and the resolutions. These codes will also greatly facilitate communication between parties who do not share a common language, because simply knowing the codes and their meanings will be adequate to understand the most important aspects of the case.
- *E-Commerce Claims Redress Interchange Standard (ECRI*). The common data structure described above has been proposed as an international multi-lingual communication standard for ODR under the name E-Commerce Claims Redress Interchange Standard (hereinafter "ECRI").[98] The idea of ECRI is that the ODR standard codes can be represented not only in textual and numeric form, but also as symbols/images or even sounds. This will enable using a very wide range of existing devices to access ODR systems, including mobile phones etc. It will also enable full unlimited participation into redress systems for persons who may have difficulty communicating effectively with textual communication. The use of ECRI will greatly facilitate participation through the reduction of barriers for certain populations.
- *Data Structures for Simple Fact-Based Cases.* Initially, the data structures will be developed for simple fact-based cases like the following: (i) goods/services ordered but not delivered; (ii) goods/services not ordered; (iii) goods/services not as described; and (iv) settlement not complied with.[99]

[98] *See E-Commerce Redress Interchange (ECRI) and NGO Proposals, supra* notes 86 and 89.

[99] *See supra* note 94.

These initial data structures will then be enhanced step by step as the system develops. An associated system/application will enable rapid, seamless, and continuous updating of the data structures.

- *Essential Architecture for Resolution of Disputes and Efficient Enforcement.* The common data structures will provide the essential architecture not only for the resolution of cross-border e-commerce disputes but also for eventual efficient cross-border enforcement. It will enable the interconnection of public and private redress systems. This interconnection will be an essential component of cross-border enforcement across all payment channels and internet intermediaries.[100]
- *Global/Regional Case Database.* A global and/or regional case database will be created and made available to all system participants through web services, so that cases can be voluntarily shared between nodes around the globe. Information sharing is happening on an ad hoc basis between groups now, but these systems are incompatible overlapping systems usually worked out between individual nodes. This new architecture will enable instant exchange between all system participants, as well as a universal view of cases around the globe, enabling better holistic monitoring and response.

4. *Additional Roles of the Database*

In addition to the above described principal functions, the ODR Data Exchange may gradually assume additional roles/responsibilities, such as any of the following:

- *Information System for Buyers.* It can help to organize information awareness campaigns and become the principal information system for cross-border buyers where they will learn about their rights, opportunities for ODR, and all available information and enforcement channels.
- *Automated Negotiation Data Exchange Platform.* It can operate an automatized negotiation data exchange application/platform, which the disputing parties use to try to resolve their issues amicably before contacting an ODR provider for facilitated settlement or arbitration. Such assisted self-directed dispute resolution should significantly reduce the number of cases going to third parties for dispute intervention as is evidenced by statistics of the private global ODR players like eBay.
- *Point of Entry for Cross-Border Environment – Global Logo.* In case there is a

[100] *See* Cross-Border Data Exchange Diagram *supra* at page 17.

strong international coordination on a global or regional basis it can even become a single point of entry into the cross-border ODR environment for buyers and sellers, offering a universal service represented by a global logo. Dissatisfied buyers can then simply click on the logo displayed on the seller's website to get easy, instant access to consumer redress.

- *Facilitating Central Clearinghouse Management – Facilitating Participation of Online Sellers.* If coordinated efforts of the key ODR stakeholders mentioned above occur (perhaps only on a regional basis) the stakeholders can input the information to enable the central clearinghouse to manage the finances required to make the redress system self-sustaining. Proceeds collected from online traders for the usage of the ODR logo can be aggregated by the central clearinghouse and distributed appropriately to all the participants in the system, enabling the central clearinghouse to monitor the system. This global logo would also facilitate participation of online sellers in the system and cover the system's administrative costs. Even small regular contributions from online sellers on a global scale will result in adequate resources.
- *Assist Providers in Administrating the ODR Process.* The ODR Data Exchange could: (i) help ODR providers administer the ODR process; and (ii) develop financial records and also allow for resolution of disputes while maintaining confidentiality, data protection and privacy interests of its users as information flows across borders.

Setup and Implementation of the Global ODR System[101]

In addition to a Data Exchange infrastructure, any global ODR system requires a network of service providers to actually facilitate and decide cases. A design for a pilot private initiative has been proposed based on the ODR Rules and other documents under preparation by Working Group III.[102]

The basic concept of the proposed pilot is the following:

- *Participation in the Pilot.* Participation in the pilot will be open to any reg-

[101] Charles Underhill from the Better Business Bureau also contributed substantially to this part in addition to the authors of this article.

[102] *See infra* note 119; *See also Possible Future Work on Online Dispute Resolution in Cross-Border Electronic Commerce Transactions, Note by the Secretariat,* 24th Sess., 14-18 Nov., 2011, U.N. Doc. A/CN.9/WG.III/WP.109, para. 7 *and Possible Future Work on Online Dispute Resolution in Cross-Border Electronic Commerce Transactions, Note by the Secretariat,* 23rd Sess., 23-27 May, 2010, U.N. Doc. A/CN.9/WG.III/WP.721, para. 140 (noting minimum criteria for the accreditation of ODR providers and neutrals, substantive legal principles and enforcement appendix).

ulator and consumer organization and/or ADR/ODR provider(s) following input and/or endorsement by respective national regulator(s). In the future system, ADR/ODR providers will administer cases and consumer organizations will provide guidance to consumers and liaise with involved domestic online sellers to ensure their wide participation in the cross-border ODR.

- *ODR Infrastructure Platform*. The cross-border ODR infrastructure platform will be piloted as a set of services to participating ADR/ODR providers and possibly consumer centers; the platform itself will not be an ODR provider but will provide its services to the participating ODR providers and possibly consumer centers. The service will be developed by an international team of technical experts (service team) with input from national regulators, consumer centers and ODR providers.
- *Publication of an Open Communication Standard and Minimum Technical Requirements – Communication of Modifications.* Consistent with the above, at the conclusion of the pilot, the technical experts will finalize and publish an open communication standard and minimum technical requirements so that future ODR providers are able to implement their own unique ODR solutions in compliance (or consistent) with the published specifications. There should also be a duty of every user to communicate all additions or modifications of the communication standard to the service team and the right of the service team to publish selected additions and/or modifications as updates of the published communication standard.
- *Provider Supplemental Rules.* Participating ODR providers will be able to issue supplemental rules. Such supplemental rules cannot be in conflict with the ODR Rules but can complement them.
- *Tracking and Confirming Costs – Preventing Forum Shopping*. The pilot will track and confirm the costs of maintaining the cross-border ODR infrastructure platform and specifications as well as the best ways to prevent forum shopping and cherry picking among participating ODR providers.
- *Localizing Communication Standards*. Participants in the platform will agree to localize the communication standard(s) into their language(s) and to encourage the use of the UNCITRAL ODR Rules in their respective countries.
- *Encouraging Participation in Cross-Border ODR – Opting in on a Case-By-Case or Formal Public Participation*. One role of the participating ODR providers (including public and/or private consumer centers and trustmark programs) will be to encourage appropriate online sellers to develop and

participate in cross-border ODR as a standard business practice and provide a valuable service to customers. Businesses may opt into cross-border ODR either on a case-by-case basis or through formal, public participation in various ODR and/or trust mark programs.

The pilot was announced on 15November 2011 at the meeting of the UNCITRAL Working Group III in Vienna. The pilot will begin with an initial stage, during which the following principle tasks are to be provided:

- Verification and testing of the proposed functions of the cross-border ODR infrastructure platform and information about the services to be provided by the service team;
- Clarification of costs involved for ODR providers with administering cross-border ODR disputes;
- Necessity/desirability of some type of coordination structure of the participating ODR stakeholders;
- Contacts and discussions with payment channels;
- Contacts and discussions with large online sellers and associations of online sellers

The future cross-border ODR system will probably emerge step by step by connecting the most active current players and expanding further to include new ODR providers, consumer centers as well as new types of disputes. There might be differing ODR programs in different countries or regions with different types of disputes and funding models or a strong internationally coordinated central system. All this will depend on activities and projects of key ODR stakeholders. Nevertheless, the underlying foundation of the global ODR system might be developed in the near future, during the next one or two years.

IV. Work of the United Nations Commission on International Trade Law

The United Nations Commission on International Trade Law ("UNCITRAL") established by the United Nations General Assembly in 1966, promotes the progressive harmonization and unification of international trade law for the purpose of achieving efficiency and predictability and reducing

transaction costs in transnational ventures.[103] UNCITRAL has prepared a wide range of conventions, model laws, legislative guides and other instruments dealing with the substantive and procedural law governing transnational trade.[104]

The 60 members of UNCITRAL (hereinafter "the Commission"), in plenary session, determine its projects, programs and agenda and create working groups, which are assigned to specific areas of research and development.[105] The Commission's Secretariat provides logistical assistance for these working groups and in particular facilitates their meetings by preparing drafts of proposed instruments.[106]

Members of the Commission are all voting members of every working group. In addition although not entitled to voting privileges, states that are not members of the Commission, as well as international governmental organizations, may attend sessions as observers and participate in deliberations.[107] Invited international NGOs may also attend sessions as observers and represent their organizations' views on matters where the organization concerned has expertise or international experience.[108]

In its June 2000 New York meeting, the Commission held a preliminary exchange of views and proposals on the subject of including ODR in its future work program.[109] During this exchange, the Commission determined that special attention should be given to the ways in which alternative dispute procedures might be made available to businesses and consumers.[110] States noted that traditional dispute mechanisms, including litigation through the

[103] *See The UNCITRAL Guide: Basic Facts about the United Nations Commission on International Trade Law*, U.N. (2007), *available at http://www.uncitral.org/pdf/english/texts/general/06-50941_Ebook.pdf.*

[104] *Idem*.

[105] *Idem*; The current 60 members of UNCITRAL are: Algeria, Argentina, Armenia, Australia, Bahrain, Benin, Bolivia, Botswana, Brazil, Bulgaria, Cameroon, Canada, Chile, China, Colombia, Czech Republic, Egypt, El Salvador, Fiji, France, Gabon, Georgia, Germany, Greece, Honduras, India, Iran, Israel, Italy, Japan, Jordan, Kenya, Latvia, Malaysia, Malta, Mauritius, Mexico, Morocco, Namibia, Nigeria, Norway, Pakistan, Paraguay, Philippines, Poland, Republic of Korea, Russia, Senegal, Singapore, South Africa, Spain, Sri Lanka, Thailand, Turkey, Uganda, Ukraine, the United Kingdom, the United States of America and Venezuela, an official list is *available at http://www.uncitral.org/uncitral/en/about/origin.html*, last visited Oct. 14th, 2011.

[106] *Idem*.

[107] *See Annotated Provisional Agenda*, 22nd Sess., 13-17 Dec., 2010, U.N. Doc. A/CN.9/WG.III/WP.104.

[108] *Idem*.

[109] *Idem*.

[110] *Idem*.

courts, were inadequate for addressing low-value/high-volume, cross-border e-commerce disputes because they were too costly and time-consuming in relation to the value of the transaction in controversy. They also noted that difficult issues often arise in the cross-border context regarding jurisdiction and applicable law.[111] Since the parties voluntarily agree to use the ODR procedure and the procedure incorporates substantive principles to be applied in the resolution of the disputes, use of this procedure bypasses and avoids the highly controversial jurisdiction and applicable law issues which otherwise would arise.[112]

At its July 2010 New York session, the Commission discussed the scope of work to be undertaken. It was initially observed that the scope should be limited only to B2B transactions, as issues related to consumer protection were difficult to harmonize because consumer protection laws and policies varied significantly from State to State.[113] It was further stated that work in that area should be conducted with extreme caution in order to avoid undue interference with consumer protection legislation.[114] UNCITRAL ultimately gave the task of researching ODR solutions to Working Group III (Online Dispute Resolution) (hereinafter 'Working Group III').[115] Working Group III was given the mission to work specifically on issues pertaining "to cross-border electronic commerce transactions, including business-to-business and business-to-consumer transactions".[116] The new working group was composed of all the member states of UNCITRAL and was to hold take up the issue in Vienna from December 13-17, 2010 at its twenty-second session.[117]

In response to these observations, the view was expressed that, in the present electronic environment, consumer transactions constitute a significant portion of cross-border electronic and mobile commercial transactions.[118] The Commission concluded that, although the scope of work undertaken must be carefully designed not to affect the rights of consumers, it would be feasible to develop a generic set of rules applicable to both kinds

[111] *See generally* Rogers, Rule *et al.*, "Designing a Global Consumer Online Dispute Resolution (ODR) System for Cross-Border Small Value-High Volume Claims – OAS Developments", 42 *U. C. C. L. J.* 3, 2010.

[112] *Idem*.

[113] *Ibidem,* at 4.

[114] *Idem*.

[115] *Idem*.

[116] *Ibidem*, at para. 4.

[117] *Ibidem,* at para. 6.

[118] *Idem*.

of transactions. Working Group III is now in the process of developing a system of legal standards that will facilitate the increased use of ODR mechanisms necessary to provide for the quick resolution and enforcement of both low value-high volume B2B and B2C disputes across borders.

At its December 2010 meeting in Vienna, Working Group III requested that the Secretariat prepare draft generic procedural rules for ODR, taking into account that the types of claims with which ODR would deal should be B2B and B2C cross-border, low value-high-volume transactions.[119]

On March 17, 2011, the Secretariat distributed a note containing an updated annotated draft of fast-track procedural rules ("the Rules") incorporating suggestions made at the December 2010 meeting.[120] This draft was the basis of discussion at the May 2011 meeting of the Working Group in New York. According to the Secretariat, these "*simple, user-friendly generic rules…reflect the low-value of claims involved, the need for a speedy procedure, and… emphasize conciliation, since the majority of cases are resolved at that stage*".[121]

Working Group III decided to follow a four-phases development plan to produce instruments for ODR.[122] First, it should create procedural rules to facilitate ODR.[123] Second, an appendix to the preliminary rule should provide "*substantive legal principles for deciding cases*".[124] Third, an appendix should consider minimum requirements for ODR providers to aid consumers and, fourth, the Working Group should consider "a cross-border enforcement mechanism".[125]

On September 17, 2011, the Secretariat distributed its updated annotated draft of fast-track procedural rules to be used as the basis for the Working Group discussion for its November 14-18 meeting in Vienna. Section 1 (1)provides that the UNCITRAL online dispute resolution rules ("the Rules") are intended for use in the context of cross-border low-value, high-volume transactions conducted in whole or in part by the use of electronic means of communication. Section 1 (2)provides that:

[119] *Online Dispute Resolution for Cross-Border Electronic Commerce Transactions: Draft Procedural Rules*, Note by the Secretariat, 23rd Sess., 23-27 May, 2011, U.N. Doc. A/CN.9/WG.III/WP. 107.

[120] *Online Dispute Resolution for Cross-Border Electronic Commerce Transactions: Draft Procedural Rules*, Note by the Secretariat, 23rd Sess., 23-27 May, 2011, U.N. Doc. A/CN.9/WG.III/WP. 107.

[121] *Ibidem*, at para. 7.

[122] See *Report of Working Group III (Online Dispute Resolution) on the Work of its Twenty-Third Session*, 23rd Sess., 23-27 May, 2011, U. N. Doc. A/CN.9/WP.721, at para. 52 *and* para. 54.

[123] *Idem*.

[124] *Idem*.

[125] *Idem*.

> The Rules are intended for use in conjunction with an online dispute resolution framework that consists of the following documents [which are attached to the Rules as Annexes and form part of the Rules]:
>
> (a) Guidelines for online dispute resolution providers;
>
> (b) Online dispute resolution provider supplemental rules;
>
> (c) Guidelines and minimum requirements for neutrals;
>
> (d) Substantive legal principles for resolving disputes;
>
> (e) Cross-border enforcement mechanism;
>
> …

During the May 23-27, 2011 meeting in New York, Working Group III reaffirmed that there was a need to address "*disputes arising from the many low-value transactions, both B2B and B2C, which were occurring in very high-volumes worldwide and required a dispute resolution response which was rapid, effective and inexpensive*".[126]At its previous meeting in December 2010 Vienna had also Working Group III noted that the language barrier was a significant challenge to addressing this issue that would prevent businesses and consumer from effectively communicating with each other although progress has been made in this area.[127] Although this problem remains an issue, considerable progress has been made by eBay, Inc. and Google, Inc., which both offer extensive online translation services.[128]

At its May 23-27, 2011 New York meeting, Working Group III reviewed its first draft of procedural rules governing cross-border electronic commerce transactions.[129] It noted that this first draft was for *"fast-track procedural rules that could be used as a model by ODR providers*".[130] It was also noted that the draft procedural rules were generic and that they could apply equally to B2B as well as B2C transactions provided "that those transactions have the common feature of being *low-value*" (emphasis added).[131] This was in keeping with the mandate from UNCTRIAL, which was that "*work on [ODR]*

[126] *Online Dispute Resolution for Cross-Border Electronic Commerce Transactions: Draft Procedural Rules, Note by the Secretariat,* 23rd Sess., 23-27 May, 2011, U.N. Doc. A/CN.9/WG.III/WP.107, at para. 5 (citing Official Records of the General Assembly, 65th Sess., Supplement num. 17, U. N. Doc. A/CN.9/716 at para. 16 (21 June – 9 July, 2010)).

[127] *Report of Working Group III (Online Dispute Resolution) on the Work of its Twenty-Second Session,* 22nd Sess., 13-17 Dec., 2010, U. N. Doc. A/CN.9/716 at para. 22.

[128] *See supra* note 88.

[129] *Online Dispute Resolution for Cross-Border Electronic Commerce Transactions: Draft Procedural Rules, Note by the Secretariat,* 23rd Sess., 23-27 May, 2011, U. N. Doc. A/CN.9/WG.III/WP.107.

[130] *Ibidem*, at para. 6.

[131] *Idem*.

topic should focus on ODR relating to cross-border e-commerce transactions, including B2B and B2C transactions".[132]

At its meeting in New York, May 23-27, 2011, Working Group III reaffirmed use of a three phase: i.e. "negotiation", "conciliation" and an "arbitration phase" *process*.[133] The Draft Procedural Rules proposed by the Working Group reflect this structure by incorporating a "negotiation", "conciliation", and "arbitration" three stage approach as follows:

- In the first phase, the parties would negotiate with each other;
- In the second phase a neutral would be appointed for the purpose of facilitating a solution; and
- In the third phase to resolve the very few cases not resolved by use of the first two phases, a neutral (possibly the same neutral used in the second phase) would arbitrate the dispute.

It has been suggested that by limiting the conciliation efforts of a competent and independent neutral independent in this second phase so as to prohibit ex parte discussions, the impartiality of the neutral and the integrity of the process would be preserved, thereby facilitating use of the same neutral in the second and third phases of the process.

Discussion has occurred suggesting that a substantially identical result could be achieved by utilizing a two phase process in which the second phase would combine phases 2 and 3 and be designated as the "Conciliation-Arbitration" phase. Under this process, a neutral who meets the standards of competence, independence and impartiality, and who would be prohibited to have ex parte discussions would initially attempt conciliation and proceed to arbitration if the conciliation was unsuccessful.[134]

Working Group III is scheduled to further refine its draft procedural rules at its November 14-18, 2011 meeting in Vienna.

[132] *Idem*.

[133] *See Report of Working group III (Online Dispute Resolution) on the Work of its Twenty-Third Session*, 23rd Sess., 23-27 May, 2011, U. N. Doc. A/CN.9/721; *See also Report of Working Group III (Online Dispute Resolution) on the Work of its Twenty-Second Session*, 22nd Sess., 13-17 Dec., 2010, U.N. Doc. A/CN.9/716.

[134] These so-called "web-arb" procedures are flexible and can be adjusted to meet varying needs. *See* Fullerton, Richard, "Med-Arb and Its Variants: Ethical Issues for Parties and Neutrals", *Dispute Resolution Journal*, May-October 2010; Blankley, Kristen M., "Keeping A Secret From Yourself? Confidentiality When The Same Neutral Serves as Mediator and Arbitrator", *Baylor Law Review*, Spring 2011; Bartel, Barry C., "Med-Arb as A Distinct Method of Dispute Resolution: History, Analysis, and Potential", *Willamette Law Review*, Summer 1991.

V. Multi-Stakeholder Model – UNCITRAL Consensus Building

In developing a fast track system for ODR it is important to maintain balanced consideration of the concerns of all stakeholders. Therefore, developing a Multi-Stakeholder Model is not only desirable, but necessary in order to successfully create the system.[135] Interested stakeholders include:

- Public agencies (as policy makers, legislators and regulators);
- Consumers;
- Online businesses;
- Payment channels; and
- ODR providers.

Differences may also exist in the needs and interests of sub-groups within these individual stakeholder classifications. For example, when high value/low volume claims are involved, stakeholders (irrespective of whether they are business or consumer stakeholders) need and in most cases will utilize sophisticated dispute resolution procedures. Conversely, when low value/high volume claims are involved, stakeholders (irrespective of whether they are business or consumer stakeholders) will need in most cases and utilize fast track low cost less sophisticated dispute resolution procedures.[136]

The challenge is to incorporate within the ODR system options which give stakeholders the choice of using a fast track, simplified, inexpensive process for low value/high volume claims or a slower, sophisticated, costly but more detailed process for high value/low volume claims.[137]

[135] Del Duca, Louis F., *Options for Low Value/High Volume and High Value/Low Volume Claims*, Proposals for the 11th International Online Dispute Resolution Forum (Sept. 9, 2011), comment in response to Loebl, Zbynek, *Discussion on pre-dispute binding arbitration agreement*, Proposals for the 11th International Online Dispute Resolution Forum (Aug. 7th, 2011) both available at *http://www.odr2012.org/node/14*, last accessed Sept. 27th, 2011.

[136] *Idem*.

[137] *Idem*.

DEVELOPMENTS IN COMMERCIAL LAW. PARADOXES AND CHALLENGES. A NEW ERA.

Raúl Aníbal ETCHEVERRY*

SUMMARY: I. *First stage*. II. *The paradoxes or contradictions. Apparent or real ones*. III. *The world of information and law*. IV. *The globalization*. V. *The commercial law in the present and future.*

I. FIRST STAGE

An analysis of Commercial law compared to other branches of legislation can be viewed as a constant interpenetration of civil and commercial law, and thence to other branches of public law such as administrative law, constitutional and criminal law.

This phenomenon is not only the root for more consistency but the basis, together with the said branches of law, to a new space where the connection with computer law and, electronic commerce is made.

From the collision of particles between the various branches of law, apparent contradictions and paradoxes arise, which can be found in the new law of this last century.

The law, jurisprudence, doctrine develop as living structures, which can better be understood from a fractal[1] concept point of view, rather than a Euclidean geometric one.

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[1] View Fractals, written in 1977 by Benoit B. Mandelbrot and his predecessors Thom (1972) and Sir Darcy Thompson (1917): the reference is taken from the Effective Date, Buenos Aires, April 1981 num. 47 p. 39 et seq.

The legal system is not a system with replacements in which new rules take the place of old ones in a harmonic and organized way. The overlap of legal rules between today's new world and yesterday´s old one is the standard. This is why we say that a legal system of a certain country cannot be characterized from a Euclidean geometry point of view but from a fractal geometrical or scaling order typical of the living organisms.

After the deep crisis that stroke legislations in the twentieth century due to revolutionary wars being them implicit or explicit, violent or silent, the planet all experienced essential changes, full of contradictions and paradoxes.

II. The paradoxes or contradictions. Aparent or real ones

A paradox is a strange fact that is opposed to general opinion and feelings.

The Paradox from Epimenides, historical author of this concept, is as follows: Epimenides was a Cretan. He said that Cretans are always liars, so if what he said was true, he, for being a Cretan, had to lie and therefore what he claimed should be false.

Together with large doses of social reforms that sought to improve the lives of the people, we find extreme forms of capitalism side by side to fundamentalist narrow-mindedness.

On one hand, we see an increase in the accumulation of goods and wealth, more poverty, a struggle for peace and the unleash of violent actions, and at the same time we also see exemplar actions and sublime work done by different sectors and groups which are all contrasted with despotism, war and terror.

The bipolar world should be finished, regional unions are in crisis, despotic governments are overwhelmed by social unrest and some democracies dwindle into dictatorships.

In various parts of the world's we see the worst corruption mingled with honest people working and struggling to live with dignity.

To this world in convulsion that calls for a substitute, belongs a defined "rule of law" that is not liquid, whose reason for being there is not a nonsense, nor has lack of values but unfolds in paradoxes, contradictions and surprises.

This also happens, regarding business law. Between hundreds of possible examples, we will only mention just a few.

At various times, Government is concerned on policies to protect citizens from fundraisers.

In Argentina, as in many other countries, the government focused to protect the common citizen from the apparent "attractive" offers made by fundraisers for business purposes.

The said tender offers were subject to detailed regulation.

Law 17,811 gave place to the National Securities Commission and enacted strict rules regarding securities, Article 16 strictly defines the public offering of securities as

> "*the call made in a general way to persons or to particular sectors or groups to perform legal acts related with securities, being these securities held by the issuers or by organizations or corporations engaged exclusively or partially in the trade of such securities. through personal offers, newspaper publications, radio broadcasts or television, movies, posters, signs, programs, circulars and printed communications or any other media activity*".

Today, virtual reality supports a new form of business on the web, known as "crow funding, which can be described as an informal call asking to contribute money for any business, usually operated by young people that manage sites or platforms on the web, thus creating a very real home market outside the traditional "public calls" to invest. Who invest their money do not have any protection, except the general rules on civil liability and criminal law.

Should it be accepted a so different way of fundraising? Are there any different dangers for the average citizen compared to normal fundraising?

The goal would be to analyze whether it would be desirable to enact laws for these practices to protect consumers (in this case, small investors), knowing that an excess in regulation can terminate this type of business.

There are other paradoxes of interest.

Legal positions today argue that the law should be flexible, legislation should follow open standards and notions (better known as soft law), compared to the old and rigid standards of law.

Another issue is the tendency to delete from the law certain definitions and concepts, such as "company", "merchant", "merchant statue". (In Argentina, the proposed new unified code submitted to the National Congress on June 8, 2012, follows this trend).

While some legal systems carefully regulate the notion of legal entity — such as it is in the current Argentine law and the proposed new unified code of civil and commercial— in other jurisdictions, (e.g. the German Commer-

cial Code) the law only names the notion of "legal status" describing few consequences and refraining from defining the term.

The notion of "merchant" was a nineteenth-century law archetype of the law fully defined and described in detail in the codes of the nineteenth century, indicating the pros of becoming a merchant and the cons of breaching the so-called "merchant Statute".

The same occurred with the notion of "commercial transactions" which evolved in two different ways, one into its deletion; the other, followed by Mexicans and French, into the increase of the number of acts to be considered "act of trade".

There is a dual existing law generating discussions and clashes because of the existence of local laws coexisting with regional integration law.

Something similar happens in between market protectionism and market freedom. These virtual or real paradoxes in law, confirm that this science is not exact but social and the rules that regulate human beings in their behaviors are built in protein and non-geometric frames.

To end these examples, there is one referred to a triple legal solution.

This triple legal solution can be seen in the formalities required to consider an existing agreement or contract between the parties.

The offer and acceptance in writing is the traditional rule of law since writing is known by men. This rule was later ratified without amendments with the invention of printing.

Written consent provides certainty and is proof of the existence of agreement or acceptance.

This is the interpretation in the old codes. In Argentina, both the Civil Code from Velez Sarsfield in 1871, and the Commercial Code, written also by him together with the Uruguayan jurist Acevedo, establish only for very small amounts the validity of a witness proof trying to demonstrate that a contract has been accepted.

Therefore, our country made the reservations permitted by the 1980 Vienna Convention on the law of International Trade, that is, requiring writing as an essential proof of offer and acceptance of a contract.

But the world has gone other ways. And the few countries that took the reservation have been seeing a change in their business reality to which they need to adapt.

Also the New York Convention on arbitration related to the implementation and enforcement of awards, refer to documents in "writing". The same happened with the model law of arbitration UNCITRAL, which was taken by many countries as part of their domestic law.

The issue was that Guttenberg's invention was very important to mankind. But this lighting event is fading .as time goes by.

Today things are different. Together with the informality of contracts and agreements, which derive from the need of speed in business, we can find Internet which helps to communicate in real time with anyone anywhere on the planet. If it wouldn´t be for informality and internet, the exponential increase in international business would not have existed.

And so we have a triple order, which is not necessarily contradictory, but indicates an evolution:

a. Contracts in which the acceptance is made in writing.

b. Written agreements, required as a general principle, but being followed, and therefore diluted, by new complementary rules which accept non-written forms. An excellent example is the Peruvian law of arbitration, taken from UNCITRAL model.

c. Electronic contracting, in which there is a "document" in a technical sense, but not in "writing".

In issuing electronically a binding will, it is considered that an "available document" exists when the following conditions are met:

1. The Message is perceptible by the senses.
2. It is possible to storage it in records.
3. It can be reproduced.
4. Information can be taken out of it.

Are all these requirements, necessary to consider that there is an "available document"? Or just one or some of them are sufficient?

Every one of these requirements are indivisibly linked, as they are the characteristics of the same phenomenon.

Together they describe something real, that American law, Chile and other countries including not few judgments and arbitration awards consider as an available document, ie, valid to be presented as evidence in court or arbitration, as proof of an existing will.

Argentina, with the enactment of law 25506 regarding digital signatures, has accepted a concept of much more flexibility. What has yet to be done is the withdrawal of the reservation made in the Vienna Convention regarding International Trade.[2]

[2] As an example in this topic, there is a court decision in the city of Budapest, in which, despite the fact that Hungary had made the same reservation as Argentina and other countries, the ruling admitted the validity of an international sales contract concluded by telephone. Quoted in the new book-Zuppi Garro, on the International Sale of Goods published in Buenos Aires in 2012 by Editorial Abeledo Perrot of Buenos Aires.

III. The world of information and law

Technology evolution is today highly appreciated, perhaps too much, There is a constant effort to simplify and accelerate business and therefore life course itself.

The digital revolution does not allow anything else that what can be done in brief. You can only communicate summaries of any thought, and also limiting the amount of text. Hence the success of Facebook, Twitter or the online journal Huffington Post.

Electronics is the present and close future revolution. The World Wide Web continues to evolve since the page *http://info.cern.ch*, created by Tim Berness-Lee, appeared twenty years ago-at that time only intended to exchange information.

Predictions say sites in the web will multiply and become cheaper. Tools will be simpler and costs to access the web as well as its main current applications (e-mail, chat, video calls, not forgetting the purpose for which it was born, the traditional: file sharing) will be much lower.

Search engines are wonders, which permit a universal access to information (browser) and the HTML is the primary language to write web pages.

The website will be developed, possibly the same way as the Big Bang, that is, with a plurality of new expressions.[3]

Even Courts tend to improve themselves through computer systems.[4]

All companies going after these developments will help free the end user from middle men. Business activities on these tracks are essential, but also essential is the fact that companies compete against each other in the market, so there is not a single voice out there that can decide what can and cannot be done on the network.

Recently, the G8 has met with the CEOs of the companies developing new technologies to regulate various issues regarding the web, such as inter

[3] One of them is the looming David Gelernter of Yale, who is leading a trend called "lifestream" (current life) that seeks to explain a proposal for the future development of the Internet through a chronological flow of documents that function as a set of life experiences, which are stored to be shared by the digital community. This idea is shared by the engineer and writer Eric Freeman. To Galernter and colleagues, all of our activities will be in the future reflected in the Web, which today is, as defined by him, a "a huge diffuse nothing".

[4] See internal court decision 31/11 of December 13th, 2011 on electronic notifications of the Supreme Court. Rossi, Guido, "Capitalism and diritto Umani" in Revista delle società, year 56/2011, page 4. Rossi, Guido, *op cit.*, page 15. Fargosi, Horace P., "Business Law of the century" in the Commercial Code, Hammurabi, Buenos Aires, 2005, vol. 1, page 127. A clear example are the "twelve priorities" that has set the European Union on April 13, 2011 for the growth of the block (COM-2011-206 final).

net neutrality.[5]

Electronic advances are not the most important in the new millennium. The bottom line is the need to educate.

It´s necessary to distinguish between information, knowledge and wisdom.

T.S. Eliot in his poem The Rock, asks: "Where is the wisdom we have lost in knowledge? Where is the knowledge we have lost in information?".

The lives of most of us go by and encounter us immersed in the search for information, entertainment and news. One could say… How many people are stunned with entertainment with no future? With banal or ephemeral thoughts, expressions of personal issues or daily news with no importance?

We do not agree with these thoughts. We think there is always personal enrichment. And there is no clear way from error to certainty; the only way is from a complexity to another.

However, it is appropriate to remark that this enrichment is not only the consequence of information and knowledge, but also from education and study, creativity and an intelligent use of science. Comprehension becomes paramount and education a vital need.

IV. The globalization

The legal system should be structured to regulate human behavior, the modern trend runs along two tracks: first, there is an increasing flexibility in various aspects of law from which, the one in international law is the more advanced (devices opt in and opt out, etc.) This openness does not mean having unlimited freedom and no controls.

Rules are good, but the new human history should be made around the capacity to understand emotionally the others, the people, and the various sectors.

As pointed out by Rossi[6] in this globalization, both property and trade is in a profound change and this affects the concept of democracy.

The author insists on the idea that, in countries that are considered democratic, violence should be wiped out, inequality and injustice erradicated, while human dignity and rights should be respected.[7] This is accepted and shared by everyone today.

5 See Tomeo, Fernando, "Internet Neutrality" in The Law of September 9th, 2011.

6 Rossi, Guido, "Capitalism and diritto Umani" in Revista delle società, year 56/2011, page 4.

7 Rossi, Guido, *op cit.*, page 15.

Ascarelli pointed in 1952 in his "Studi" "In the current crisis of values, the world demand lawyers for new ideas and not subtle interpretations: it is necessary therefore to go over the fundamentals".[8]

The challenge is to present an adequate set of rules —most of them will be legal ones— to bring humanity to Justice without risking freedom.[9]

It is important to remember UNCITRAL Rules 2010, available as model soft law regarding "international trade agreements", which include the principle of freedom, the obligation of the given word (1.3), respect for mandatory standards (1.4) and the obligation to act in good faith and fairness (1.7) respecting the interpretation to be done in any agreement to one's previous actions in it (1.8).

These rules should be extended to the whole legislation, not only to "contracts" or to those considered "commercial" (Uncitral could not define "commercial" since it is not a concept distinguished in the common law). All the national legislation with the exception of Public law, should use this principles.

Today there is only one law body regarding property, as seen in any interpretation of any judge, be it under civil law or commercial law and that is the living law.

V. The commercial law in the present and future

Commercial law, with all these apparent paradoxes only gives proof of vigorous growth.

The legal concept of merchant, company, consumer trade agents, will always exist, whether they are explicitly legislated or not.

There are a multitude of sources for interpreting the law; therefore more and more expertise is required to be an operator in any legal system.

The simplification in the civil and commercial systems to "legal acts" and "contract" to show the existence of a will is no longer enough. New legal categories should be created.

The new phenomenon of regionalization, integration and globalization, means that there are various legal systems coexisting which should necessarily complement in between each other.

[8] Fargosi, Horace P., "Business Law of the century" in the Commercial Code, Hammurabi, Buenos Aires, 2005, vol. 1, page 127.

[9] A clear example are the "twelve priorities" that were set by the European Union on April 13, 2011 for the block growth (COM-2011-206 final).

The "business incubators" existing in countries of North America and Europe are proven institutions. They are referred to as small businesses, and encourage the growth of the economy as a whole.

Trade deals are diverse and they involve private, mixed and public companies. The concept of "market" is being discussed, particularly "markets" (national, regional, international).

Also, two new concepts emerge: the "consumer" and the "stakeholder", the latter unknown in the recent past, used to refer to all persons not necessarily being members of the company, but having some kind of link or participation regarding it.

The partnership, formerly the business center, now is evolving in different ways all allowed by law.

There has been a profound change in customs and habits which will give birth to a new law, to a new society, which is still brewing around those who use the tools of the digital age.

Education should be in the spot. Education brought unlimited progress in the welfare of large parts of the world.

Other regions, tragically back warded, are mired in illiteracy, hunger, lack of opportunities, war and misery.

Knowledge can give the world a better life. Everyone is entitled to a better life, all human beings should have access to food, clothing, housing and education.

As never happened before, many things can be solved with new energy resources, environmental policies and education.

SOLVING MEXICO'S FINANCIAL PROBLEMS BY ACKNOWLEDGING ITS ECO-ENVIRONMENTAL DEBT

José Fernando García Villanueva

SUMMARY: I. *Main causes that generate eco-environmentaldebt*. II. *Consequences*.

The subject we will analyze today is one of great delicacy and concern for most countries; especially for those who are in external debt since several years ago and whose debts tend to increase constantly.

For any country, external debt is a massive weight to carry. No matter what type of government or governmental tendency is being followed, it is evidently hard for any government administration to lift this weight off.

The main hypothesis of this presentation is that external debts that are currently owed by in debtor countries to creditor countries can be repealed or annulled. This would be possible by applying a legal entity: international debt compensation.

Applying an international debt compensation is only possible if the creditor countries acknowledge that they have an eco-environmental debt with other countries. This debt comes from the massive abuse and consumption of natural resources within other countries' territories; this may be considered an abuse based on excessive exploitation of other countries' natural resources. Throughout this presentation we will focus on the case of Mexico and the possibility of applying international debt compensation between Mexico and its creditors.

Many creditor countries have had and continue to have developed economies by exploiting natural resources within debtor countries' territories.

Consequently, creditor countries have acquired an eco-environmental debt with their debtor countries.

I. Main causes that generate eco-environmental debt

1. *Main ideas*

There are several different concepts, ideas and criteria about what eco-environmental debt is. Different perspectives have been proposed by different authors, such as Martínez Alier, author and researcher of Universidad de Barcelona, as well as specialist of the eco-environmental debt phenomenon. Martínez Alier explains that:

> *The eco-debt, is* "*the debt contracted by industrialized countries with other countries due to the past and present plundering of natural resources, the exported environmental impacts and the free use of environmental global space as waste deposit. The eco-debt originates at the colonial period and it has increased ever since*."[1]

There are other proposals concerning this concept:

The concept of eco-debt originates from the popular movements of southern countries, especially in 1990 at the Chilean Institute of Political Ecology (Instituto de Ecología Política de Chile), which was a subject approached at the summit celebrated in Rio de Janeiro. This idea has geographically expanded as a drop of ink over a piece of paper which has reached from social movements to academic, political and institutional circles.[2]

> *"People from the Southern half of America have become creditors of this debt and the Northern counties have become debtors. The foundations of this debt are the current industrial production model, the exhaustive production of waste such as greenhouse gases emissions, capitalism and free trade*".[3]

Some other components of this eco-debt are the current plundering of natural resources and the socio-environmental local damages; as well as the extraction of non-renewable resources, such as mineral or fossil combustibles (oil), the destruction of land and the pollution of water sources.

[1] Martínez Alier, Joan, *¿Quién debe a quien Deuda ecológica y Deuda externa*?, Barcelona, Icaria Editorial, 2003, p. 14.

[2] Lago Rosa y Barcena Iñaki, "Deuda ecológica y modelo energético: los casos de Nigeria y Bolivia", Primera Jornada de Economía Crítica, Bilbao, Eco Cri, p. 1. *http://www.ucm.es/info/ec/ecocri/cas/lago_y_barcena.pdf*, consultado el 31 de octubre de 2011.

[3] Alianza de los Pueblos del Sur, "Que es la deuda Ecológica", *Conferencia Mundial de los Pueblos del Sur, el Cambio Climático y los Derechos de la Madre Tierra*, May 12th, 2008, *http://www.deudaecologica.org/Que-es-Deuda-Ecológica/*, retrieved June 20th, 2010.

Another manifestation of eco-debt is the abusive appropriation of common spaces such as the atmosphere or oceans which have been used to absorb gas emissions creating a greenhouse effect. Authors, such as Martínez Alier, question who is in debt with whom. Martínez Alier, a Spanish economist, has done some mayor work for this eco-debt owed by rich countries to Third World countries to be acknowledged. Martínez explains, throughout his research, how northern countries' ambition has driven them towards the use and exploitation of southern countries' natural resources, as he mentions that:

> *…external debt has been accumulating since the 1970s and the 1980s. This debt still represents a decisive handicap concerning economic policy in Latin America. The amounts that have already been paid are bigger than the amount that was owed originally. Nonetheless, the total external debt has continued to increase. Whereas external debt is a well-known problem, eco-debt is a new idea.*[4]

Eco-debt is the result of a specific way of consuming and producing, to which modern society has become accustomed since several years ago. Poor countries have become victims of rich countries' plundering of their natural resources. At the same time, capitalist economic forces have aligned in a way that they have completely penetrated the way we act and think; guiding us towards totally irresponsible consumption. The excessive consumption of products derived from natural resources has resulted in the exhaustion of these resources through the years.

2. *The Disproportioned Exploitation of Natural Resources*

To understand the subject of eco-debt and its relationship with external debt, it is important point out that this problem irrefutably emerges from historical aspects. This brings to light the term Historical Debt. It concerns the historical claim of a debt by Third World countries to northern industrialized countries due to the plundering which took place during the colonization in the 16th century.[5]

During the colonial period, European conquering countries took over vast amounts of minerals from America's territories "*such as gold, silver, precious stones, fine woods and other genetic resources plundered from the colonies' lands. Ad-*

[4] Martínez Alier, Joan, *¿Quién debe a quien…*, *cit.*, p. 41.

[5] *Ibidem*, p. 7.

ditionally to the plundering of natural resources, local populations required to pay a tithe to European conquerors".[6]

The constant sacking of New Spain and the main cities of America was a historical and economic phenomenon. Conquerors realized that the New World was a source of wealth and great amounts of natural resources. As a result, they organized a mayor exploitation of gold and silver with the goal of extracting and taking as much gold and silver as they were able back to their countries. Due to this massive plundering of natural resources, Europe, and especially Spain, became world powers since the 16th century and for many centuries to follow.

Nowadays, the recognition of indigenous communities right of property concerning natural resources within their territories may not be the most popular or supported subject. Yet, the mere discussion about the recognition of this right 500 years ago was unthinkable.

"It is implausible that, only since the first half of the 21st century, indigenous communities and populations' rights, such as the right to self-determination, are constitutionally recognized in Mexico".[7]

Other theories which reinforce the idea of an eco-debt have already been offered. These theories approach ideas of debt concerning other aspects and concepts of debt as well as the eco-debt, but ultimately they are intimately bounded to the eco-debt itself. These ideas have been presented at the 2008 Jubilee South/Americas Reunion at Buenos Aires, Argentina; in which it was expressed that:

"Today, developed countries not only are in debt with developing countries for the resources that they have exploited through the centuries from their territories, but they are also responsible for the environmental crises that we presently need to face".[8] This remark falls directly and unavoidably under the concept eco-debt. Then, we ask ourselves as mentioned by Martínez Alier who owes who what?

The idea of an eco-debt is strongly tied to other types of debt; joined all together, they outline a much more complex idea of eco-debt, which is associated with several elements. These elements illustrate the different factors which, happening within the same phenomenon, corroborate the approach initially developed within this thesis: economic compensation of the eco-debt through a legal support of the eco-debt and the external debt.

6 Alianza de los pueblos del sur, acreedores de la deuda ecológica, "Deuda histórica", *http://www.deudaecologica.org/Deuda-histórica/*, retrieved June 3th,2010.

7 Reforma Constitucional de fecha 14 de agosto de 2001 al artículo 2o.

8 Information retrieved from: *http://www.jubileosuramericas.org/item-info.shtml?x=88819*, retrieved June 4th, 2010.

Historical debt: This debt is the result of the plundering, devastation, destruction, slavery, death, cultural genocide and the acquisition of other ideas which had an impact on indigenous communities from end to end of the American continent during the colonial period.

Debt due to social impacts: This debt comes from the impact resulted from the extraction of natural resources, especially minerals, petroleum and forestry, among others on three overlapped fields: environmental, economic, and cultural.

Debt due to intellectual appropriation and usufruct of ancient knowledge: This debt is related to the appropriation of seeds and traditional knowledge and use of these seeds ass medicinal plants upon which biotechnology and modern agro-industries are based.

Debt due to impacts resulted from the imposition of technological packages from the green revolution: This debt is concerned with the use and consumption of "improved" seeds, toxic pesticides and genetically modified foods within the agricultural sector.

Debt due to use and degradation of lands, waters, air and human power: This debt comes from the establishment of monocultures used to export production. This has put at risk food self-reliance and cultural sovereignty of Southern communities.

Carbon-debt due to atmosphere pollution: This debt is concerned with the emission of greenhouse gases by industrialized countries (some of which still do not apply the necessary measures to diminish these emissions) which have accelerated the climate change.

Debt due to damages: This debt approaches the production of chemical, nuclear and biological weapons as well as toxic substances and waste which are often dropped in Southern countries.

All these debts come together shaping one debt: the eco-debt.[9] There are several authors and researchers such as Aurora Donoso from Ecuador, Karin Nansen from Uruguay, José Augusto Padua from Brazil, Miguel Palacín from Peru and Daniela Russi from Spain, who participated at the 2008 Jubilee South/Americas Reunion. Within the same year and with a firm alliance with the Southern people, these authors and researchers claimed that, and I share their opinion, the eco-debt owed by the North is much larger than the external debt owed by the South. "*Although real and vast, the eco-debt is hard to put down in numbers. Many of the aspects of the eco-debt along*

[9] Alianza de los Pueblos del Sur, "Que es la deuda Ecológica", Conferencia Mundial de los Pueblos del Sur, el Cambio Climático y los Derechos de la Madre Tierra, June 12th, 2008, *http://www.deudaecologica.org/Que-es-Deuda-Ecologica/*, retrieved June 20th, 2010.

with a historical debt throughout centuries of colonialism and exploitation simply do not possess a mere monetary value".[10]

According to this subject Martínez Alier mentions that:

> …concerning this subject, institutions such as the International Monetary Fund and the World Bank only consider debt in terms of money. Whenever they demand the payment of the External debt, it would be necessary to demand the payment of the Ecological Debt in terms of money as well.

It seems that for now, the eco-debt cannot be calculated. Nonetheless, we know that, based on the historical debt and the current situation, the eco-debt is superior to the external debt owed by poor countries to rich countries.

It is worth mentioning that the estimated value of the natural resources consumed through human action is being currently studied by the field of ecological economics. But then again, in reality, the value of the lost lands used for agriculture, polluted waters and seas and extinct species (flora and fauna); have a value that a monetary number cannot illustrate.

This is an intrinsic value and an economic quantification will always be unsatisfactory. Environmental damage has systematic repercussions. In other words, it could result in the disappearance of entire species including flora and fauna and, consequently, several food chains. This would affect biodiversity, create alterations in ecosystems, as well as a considerably loss of natural resources. Finally, in would affect humans and our way of life.

Accordingly, mayor efforts are needed to find the true value of the eco-debt so that an economic compensation based on legal allegations concerning the eco-debt and the external debt can be approached in an immediate future by debtor countries and creditor countries.

The legal aspect of the eco-debt is of most importance if we expect rich countries to recognize this debt. If so, an agreement on a form of compensation between the external debt and the eco-debt, so that poor countries can settle their external debts and lift this weight off from their economies, can be achieved.

3. *Carbon-debt*

"*This debt is acquired by industrialized countries because their activities have polluted the atmosphere out of proportion by the excessive emission of greenhouse gasses which have deteriorated the planet's ozone layer and increased the greenhouse effect*".[11]

[10] Martínez Alier, Joan, *¿Quién debe a quien…*, *cit*., p. 7.

[11] *Ibidem*, p. 14.

According to specialists in the subject, the carbon-debt originates from the disproportionate energetic consumption of the Northern countries. Burning fossil-fuels generate energy, but it also generates massive CO_2 emissions which are the main cause of the uprising greenhouse effect. This type of pollution has global consequences because it is related with an increasing number of external natural phenomena (torrential rains, long periods of drought, etc.) which affect poor countries situated at the tropics and with fragile infrastructures more than they affect rich countries. Such is the case of Southern countries in America who have minimal responsibility compared to rich countries concerning this kind of pollution.

"Carbon credits are an international attempt to mitigate the growth in concentrations of greenhouse gases and therefore decontaminate the environment. This mechanism for decontamination can be supported by the Kyoto Protocol which states a decrease of gas emissions that accelerate global warming".[12]

> Some authors consider the carbon market as the new business of ecological disasters. Polluting companies and intermediaries are making millions of dollars from the carbon market (in 2008 the carbon market raised up to 90,000 millions of dollars); but it is impossible to calculate in numbers how much CO_2 emissions are decreasing. There is the possibility that this reduction is not happening at all. Decreasing CO_2 emissions is not possible when the merchandise is based on materials from forests, territories and protected areas acquired by using title deeds or mortgages concerning these territories and forests.[13]

This is a deceptive design. It was not created in favor of the people and the environment. Its main function, quite opposite to helping people, is actually to promote the CO_2 emission business and not to reduce these emissions. It, in fact, contributes to the ozone layer problem by allowing the continuous use of fossil fuels.

Dr. Witker mentions that the transactions concerning carbon credits and the carbon market have no official value over the price of a ton of CO_2, whether it is emitted or reduced. Everything is handled by contracts for buying and selling of carbon credits.[14]

[12] Witker, Jorge "El derecho económico y los bonos de carbono", *Administración pública contemporánea*, México, UNAM, Instituto de Investigaciones Jurídicas, 2010, p. 687.

[13] Oilwatch, Red de resistencia a las actividades petroleras, "El Mercado de Carbono Voluntario", *Boletín de Resistencia*, num. 59, March, 2006, *http://www.oilwatch.org/index.php?option=com_content&task=view&id=604&Itemid=48&lang=*, retrieved June 7th, 2010.

[14] Witker, Jorge, o*p. cit.*, p. 689.

4. *Biopiracy*

Every species all around the world have information encrypted in their cells. This information is known as: genetic code. The genetic code is a map to navigate the formation process and the functionality of organisms.

These genetic characteristics are the result of thousands of years of interaction between different species. Additionally, "they are the result of animal or species evolutionary process. Within this map, we can find the species' detailed identity, such as the design for producing chemical defenses, the ability of adapting to different climates, nutritional characteristics, immunological defenses and the specific behavior of the species, among others".[15]

Throughout studies, genetic characteristics can be reproduced, manipulated and transferred to other species by using lab research and techniques which have been developed for the last 25 years in industrialized countries. For example, naturally, plants transport and pass on their information through their seeds. The farther the seeds reach from the plant, the farther the plant will spread its features.

"*The new generation biotechnology is being affected by unexpected mutations due to remarkable scientific advances on understanding live cells metabolism, the current expertise of genetic advances and genetic manipulation, as well as live cells economy. This way, cellular biology and genetics reach maturity*".[16]

Since several years ago, man has done various scientific researches whose objective is to modify some characteristics of vegetables. The aim of these researches is to modify food to improve its nutritional value. Biological diversity is highly related to the commercial market and intellectual property plays an important role.

The failure to comply with the intellectual property laws concerning biotechnology is considered biopiracy, which is "every genetic and biologic resource extraction process that has happened, and continues to happen, without the approval of and negotiation with the communities that lawfully own such information and leads to an intellectual property monopoly".[17]

In 1992, in Rio de Janeiro the Convention on Biological Diversity was brought to light and signed by 150 countries. One of this Convention's main objectives is to protect biological biodiversity and to regulate what transnational companies were doing concerning to this subject. "The first regula-

[15] Martínez Alier, Joan, *¿Quién debe a quien…*, *cit.*, p. 25.

[16] Douzou, Pierre, *Las biotecnologías*, México, Fondo de Cultura Económica, 1986, pp. 12 and 13.

[17] Martínez Alier, Joan, *¿Quién debe a quien…*, *cit.*, p. 66.

tions concerning bioprospecting and conservation were created through this international agreement".[18]

Biopiracy is, with no doubt, an illegal way of appropriating indigenous knowledge and culture, which have been passed from generation to generation and whose use must promote the development and growth of indigenous populations instead of; as it usually is the case; create more utilities for international companies.

In Mexico, the National Polytechnic Institute has developed a "Professional Interdisciplinary Unit of Biotechnology (UPIBI); created in 1987, this unit focuses on the formation and education of scientific and engineering professionals specialized on applied biotechnology and bioengineering in the industrial world. Within this unit, products and processes of the food industry, the pharmaceutical industry and the newest biotechnological technics are studied and analyzed. They also study the use and development of technology for the environmental conservation. Within this unit engineering bachelors such as environmental engineering, biomedical engineering, biotechnological engineering, food engineering and pharmaceutical engineering are studied".[19]

The European Court of Justice "has banned Monsanto's honey contaminated with pollen from MON 810 maize. German beekeepers and farmers have detected contaminated honey due to the natural process of pollination and wind transporting the contaminated pollen from the sowing of transgenic maize corps to the honey and other crops".[20]

5. *Environmental Liabilities*

Environmental liabilities are the debt resulting from the extraction of natural resources such as oil, hydrocarbon, minerals (gold, silver, iron, steel, etcetera); forestry resources; marine resources and genetic resources among others.

Environmental liabilities are known as "the set of environmental damages, in terms of water, land, and air pollution, as well as the deterioration of

[18] Barreda, Andrés, "Biopiratería, bioprospección y resistencia: Cuatro casos en México", *Revista Migración y Desarrollo*, *http://rimd.reduaz.mx/coleccion-desarrollo-migracion/enfrentando la globalización/Enfrentando11.pdf*, p. 124, retrieved September 30th, 2010.

[19] Instituto Politécnico Nacional; Unidad Profesional Interdisciplinaria de Biotecnología; Main Page *http://www.biotecnologia.upibi.ipn.mx/*.

[20] Greenpace.org "Prohíbe Corte de la Unión Europea miel contaminada con maíz transgénico", September, 2011, *http//www.greenpeace.org/mexico/Noticias/2011*, retrieved November 2nd, 2011.

resources and *ecosystems due to a company's usual activities or unexpected accidents throughout the company's history*".[21]

The economic value of environmental liabilities is debatable because of two main reasons: firstly, ecosystems and human interaction with them have a very high complexity and uncertainty; secondly, the monetary value of environmental damages has unavoidable structural limitations. To determine, monetarily speaking, environmental deterioration is no *pecata minuta.* According to this subject, Martínez Alier suggests several exceptionally pertinent questions such as: What is the monetary value of human life? And, what is the monetary value of landscape deterioration?

In reality it is very difficult to give a value to these concepts therefore, it is necessary to revise the concept of compensation from it very core. "We can ask ourselves if the damages concerning health, cultural death or irreversible degradation of the environment are adequate, pertinent and useful concerning a monetary compensation".[22]

6. *Toxic Waste Export*

Toxic waste market is a lucrative industry based on a central strategy of the world's economic order, which intentionally encloses lands and resources creating a polluting rights market and allowing, consequently, labor and nature export.

There is such a mayor opposition to toxic waste dumping and dangerous waste incineration that, in some places around the world, it has resulted in massive political movements. Neither government regulations nor the capitalist market have been able to provide adequate protection of natural systems and communities affected by environmental pollution.

The Basel Convention on the "on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal" was adopted in 1989 and it came into effect in 1992. This convention provides the normativity concerning toxic waste. Currently, 149 countries have ratified it; even so, the United States of America is the only developed country who has not yet ratified this convention.

Toxic waste export from industrialized countries to poor countries and toxic products export create a bigger eco-debt held these countries because this debt originates from the massive pollution produced by them in poor countries or developing countries territories.

[21] Martínez Alier, Joan, *¿Quién debe a quien*…, *cit*., pp. 35 y 36.

[22] *Ibidem*.

II. Consequences

1. *Socio-economic Consequences*

Solving the external debt problem may be the main objective of the international community because this problem needs to be approached directly through international trade and international cooperation since its vast repercussions affect a large part of the world's population. The reality is that most of these countries' income becomes part of the payment of the external debt and this considerably reduces a nation's possibility of using those resources for developing productive sectors.

This results in very serious economic consequences for poor countries' citizens, which translate into a long loss of purchasing power, devaluations, recession processes, lack of liquidity and lack of goods and services. The aim of reducing the government budget deficit entails less public services and social benefits for the acquisition of basic needs.

The worst case scenario for a country is to reach the point in which it needs to ask for international loans to be able to feed its population.

According to the social aspect, this translates into social movements due to the population's discontent, loss of economic and social positions, massive migration in search of better paid jobs and the heritage of the debt to future generations.

2. *The Future of the External Debt (social movements of indignation 2011)*

It is a fact that during the 1960s negotiations with developing countries for obtaining the largest amount of resources possible in exchange of money were very common. These loans had very low interests rates and consequently, many countries such as Mexico took more loans that it was able to pay. When in 1994 Mexico was unable to pay its external debt the international financial community becomes afraid that other countries may be in the same situation as Mexico, "*Mexico's economic situation in 1995 resulted in a deterioration of banking institutions' liquidity and solvency. Special measures which allowed international banks to deal with the losses were implemented. From 1995 to 1996, banks were required, according to the law, to build preventive reserves equivalent to 60% of their loans in arrears or 4% of their loans receivable portfolio depending on which amount was the highest*".[23]

[23] Quintana Adriano, Elvia Arcelia, *Aspectos Legales y económicos del rescate bancario en México*, México, UNAM, Instituto de Investigaciones Jurídicas, 2002, p. 129.

Solutions proposed during this period were only palliative measures and not real long-term solutions. The World Bank and the International Monetary Fund have acknowledged the crisis magnitude and in several occasions they have mentioned the option of reducing poor countries' external debt to a point in which they can reach economic sustainability. In several forums the condonance of public debt, unpayable by poor countries, has been mentioned.

The most indebted countries are being pressured to get currencies destined to pay their debts and to import essential products. International financial institutions offer assistance to countries in this situation and they use their influence to oblige them to accept structural adjustment and stabilization policies.

"In the case of Mexico, the 1994 crisis led to a financial crisis outline with the aim of allowing authorities to start a rescue program summarized in a set of points which were approved by international banks and organisms such as the Inter-American Development Bank".[24]

The international financial system excludes several countries and millions of people from private investments. This is justified by arguing that these countries do not possess the ideal conditions required by investors.

Civil societies against the economic and social tendencies of their governments have started very big and important social movements all around the world especially in central Europe. They reproach governments of acting based on guidelines dictated by the World Bank and the International Monetary Fund which result in the exploitation of poor countries and the economic control of their natural resources.

As debts have become gigantic and unpayable, the world claims a global change of the political —economic— financial structure of both: debtor countries and creditor countries. The following is an illustration of these claims:

> *Tens of thousands people demonstrated last Saturday, October 15th 2011 in several cities around the world to claim (a global change) inspired by indignant Spaniards and the "Occupy Wall Street" movement started in New York. The demonstrators demand the end of the banks' empire, more jobs and social inclusion. In Spain, at la Puerta del Sol located in Madrid, the Indignants Movement was born some months ago. This movement has reached many cities around the world such as London, Paris, Rome, Los Angeles, Barcelona, Berlin,*

[24] *Ibidem*, p. 130.

Frankfurt, Lisbon, Santiago de Chile, Ottawa, Toronto, Vancouver, New York, Washington, Lima, Buenos Aires, San Jose de Costa Rica and Mexico City, among others.[25]

This events show a global society tired of a scarcity and famine environment, with no optimal way out of the economic imbalance; they reflect a capitalist system that, for the time being, faces strong difficulties and provides no immediate solutions.

One of the main problems that need to be solved is that of a legal economic compensation. International financial entities, represented by the World Bank, the International Monetary Fund and the Inter-American Development Bank, currently control the world's markets and economies. They are the ones that dictate specific guidelines and policies to be followed by debtor countries. Therefore, if a country does not follow these guidelines, it is removed from the loan market, which gravely affects its economy. Debtor countries have attempted to declare debt moratorium or the condonance of the external debt because no matter how much they negotiate with international financial representatives they are simply unable to pay the debt.

3. *Acknowledgement of the Eco-debt*

The origin of the external debt is quite old; it started in the 16th century. The eco-debt is part of the historical debt as well. The current life quality that developed countries enjoy is in great part due to the flow of natural, financial and labor resources generated by third world countries.

Presently, inequity and exploitation of poor countries continue to exist, but today, other more subtle and efficient methods are being used. These methods consist on subjugation and control techniques, supported by malicious governments, over developing countries in favor of rich countries.

Nowadays, the decisions we take have global dimensions. Actions taken today will include, determine and, sometimes, damage humanity and society as a whole. If rich countries decide to recognize the eco-debt, they would be benefiting themselves because, when having an unpayable debt (internationally speaking), creditor countries may have to face greater crisis than the ones they have seen so far.

Today, we live in a new era of world history; within which, a smaller number of workers is needed to produce the same amount of products and

[25] Mora Tavares, Eduardo, "Indignados avanzan con impulso global", *El Universal*, México, Sunday, October 16th, 2011, first section, pp. A-4, A-16.

services required by the world's population. Technological advances and the international market are leading us into a world in which the lack of job possibilities is a current and usual state for us all.

4. *Legal-economic-financial compensation as a solution for the external debt and the eco-debt dilemma*

Compensation is a legal element which originates from Roman times and it is a technique to annul debentures when, between two people (individuals and legal entities) are both in debt one with the other. This way they have the right to compensate the debtor's debt with the creditor's debt reaching the smallest amount of debt possible between the two parties. This compensation can be defined as "*a way to extinguish reciprocal debentures or obligations which have an effect based on the amount of one debt being partially or totally equivalent to the amount of the second debt*".[26]

The term *compensation* comes from Latin *Compensati,* which means: the action of compensating, "*Equality between the given and the received; between what is owed and what it is credited; between the damage caused and the repayment obtained from it; reimbursement and balancing*".[27]

According to Rojina Villegas compensation is:

> *A method to annul reciprocal obligations to avoid a useless money or wealth movement which would be impractical considering the amount of time taken for these transactions. Additionally, compensation is justified according to equity amongst both debts; asking a debtor to pay the debt when he or she is creditor of his debtor would be unfair and risky because it would leave him exposed to insolvency or avoidance to pay from his debtor*.[28]

The field of international law also approaches compensation according to the United Nations.

The legal precept of compensation happens throughout the U.N.'s Compensation Commission which is an important international element for it is in charge of the reposition or compensation of debts due to unjust military actions such as the case of Kuwait.

The U.N.'s Compensation Commission located in Geneva, Switzerland approved a compensation consisting on $203,8 million dollars in favor of

[26] De Pina, Rafael, *"Diccionario de Derecho"*, 10th edition, México, Porrúa, 1981, p.100.

[27] Guiza Alday, Francisco Javier, *Diccionario de Legislación y Jurisprudencia*, México, Orlando Cárdenas Editor, 1995, p. 144.

[28] Rojina Villegas, Rafael, *Derecho Civil Mexicano*, 8th edition, México, Porrúa, 2001, num. V, vol. I, p. 629.

the people affected by the Iraqi invasion to Kuwait in 1990 and the Iraqi occupation.

According to this, the following conclusion can be provided:

1. Countries who have asked for monetary aid have been dominated and controlled by foreign banking entities as well as financial organizations such as the World Bank and the International Monetary Fund throughout the credits these organizations have provided. These credits have generated massive external debts owed by poor countries, in addition and more importantly, many of these debts were unpayable when the credits were grated and continue to be unpayable today.

2. Since the 1940s, the power of international financial organizations over developing countries has grown. They have provided these countries with resources which have only increased poverty by creating an even bigger external debt which is surely unpayable for most of the debtor governments. The external debt amounts have grown to a point in which even the payment of interests has become overwhelming. The power that international financial organizations have over debtor countries has significantly reduced the debtor countries *national sovereignty*. This concept needs to be redefined today within a new context. In the case of Mexico, as well as other countries, the intentions of these organizations' intervention are questionable amongst with their participation and involvement in the country's economic and political development of debtor countries.

3. Mexico's external debt originates during the second half of the 18th century. Since then, it has continuously increased due to the generated interests. A revision of Mexico's external debt has been negotiated in several occasions.

Currently, during the sexennial presidential term of Felipe Calderón, the amount owed concerning Mexico's external debt has reached $182 thousand million dollars in 2011.

As this debt becomes a strong argument, international financial organizations have controlled the use resources favoring projects that benefit creditor countries. Favoring foreign countries is a policy that debtor countries have suffered over the years. Consequently, debtor countries are being controlled by the demands of creditor countries or policies from international financial organizations.

4. To get creditor countries to acknowledge the eco-debt is no easy task. Economic interests have been the core of their power, progress, wealth and control over the world over the years. To a great extent, their power is based on the exploitation of conquered countries' natural resources; dominated and subjugated by conqueror countries' economic and financial policies.

5. The current economic-financial system will not last much longer. It will not be long (8 to 10 years) before the financial system collapses because of the debtor countries lack of liquidity, along with other factors. With no liquidity and no money supply, external debts will be paid with the debtor country's natural resources. This situation can result in a global chaos.

The most obvious example of this situation is the current cases of central Europe and the USA. The previously mentioned *indignant movement* is an example of social protest which claims a new economic order to the authorities. The present economic order that rules the occidental world since many years ago favors great powers and generates wealth for few people within international companies.

6. The main reason why creditor countries need to acknowledge the eco-debt is that the world is suffering of a general crisis. Most of human activities are submerged into a great conflict: Financial, nutritional, climatic, social, energetic, politic, etc. This suggests that this crisis is based on a behavioral pattern by which materialism predominates at any cost.

7. The development of a precept of economic compensation due to damages and legally supported at an international level is suggested as a solution to the problem of external debt and compensating it with the eco-debt. To accomplish so, creditor countries need to acknowledge both the eco-debt and the external debt so that favorable and payable debts can result from this compensation.

8. These actions would result into a new and different Economic World Order, changing the ways in which we produce, exploit, distribute and consume as a society. The creation of a new entity, alien to present economic and politic interests is necessary to accomplish this change; so that this entity could truly deal with the needs of change claimed by humanity. Constituted by highly moral international members of the civil society, this entity could lead the world into economic change and handle such great responsibilities. The suggested entity is for this task is the "Creditor and Debtor Countries Organization (CDCO)" integrated, regulated, administrated and handled by international, professional, highly moral people who will represent the debtor countries as well as the creditor countries. This autonomous and self-managed organization would be in charge of solving the conflicts between debtor and creditor countries.

9. The main question is: Why would the world's rich and dominant creditor countries would accept to acknowledge the eco-debt? What would they win by doing so? What would they accomplish? Which benefits this would bring them?

These questions are answered by the following arguments:

A. If we do not find a solution to debtor countries' external debts payments son enough, the world's financial-economic system will collapse as it happened in 2008 in the USA with the real estate market.

B. Without having a constant money supply, debts will be redocumented and debts are only real within financial documents which recognize the debt and "assure" its payment in a fixed and definite future. But this does not assure that the debtor country will be able to pay the debt once that point is reached.

C. The lack of liquidity results in rich countries using the debtor's natural resources to produce economic resources. Consequently, the debtor country's internal wealth is only apparent and as the life cycles of nature are not being respected, the possibility of continuing to pay the external debt with natural resources grows smaller. When the due date stated at the external debt financial documents will come, financial institutions will realize that debtor countries lack liquidity to pay their debts. As a result, all that financial institutions have are huge amounts of financial documents (paper) illustrating unpayable debts and enormous amounts of money lost. This will severely affect the institution's loans receivable portfolio.

10. We are reaching to the end of economic, social, political and financial systems as we known them. Accordingly, the need of decreasing the world's economy is unquestionable if we want to change our consumerism into a sustainable way of life.

Therefore, it is recommended to eliminate both debts between debtor countries and creditor countries: ecological and external. It is the healthiest option to reactivate once more economic and financial status creating a new starting point for all economies with a cero-debt new beginning.

My hypothesis is the following: if creditor countries would not accept these propositions, it is evident that the present economic structures such as the stock markets, the financial markets and banking markets will collapse. The breakdown of international commerce would be imminent if debtor countries declare themselves in moratorium.

Furthermore, the lack of work opportunities, money, food, services, housing, health, goods and essential requirements for life would cause social problems resulting in a radical change of political structures.

Today's society needs to learn how to decrease production and consumption so that we can reach life standards as we used to have in past decades. The abuse of banking and financial markets may lead human society and future generations into an irreparable situation.

We still have time to change our future if creditor countries recognize that their current financial actions will have a boomerang effect (coming back to them) and will have repercussions against them.

New ways to produce and consume need to be created and generated by respecting the environment of the natural resources that we still have and the wealth they generate; applying concepts of sustainability in an vigorous fashion and applying sever sanctions against offenders.

11. The legal entity known as compensation due to damages is feasible and suitable for solving the current economic-financial problems such as debtor countries' external debts.

Through the legal entity known as compensation due to damage, an equity point between external and eco-environmental debts can be reached. This action would greatly relieve the present economic situation of debtor and creditor countries. We would start over from cero and be able to talk about the new international economic order which has been needed for many years. This may be the optimal solution for implementing international changes in the world's economies and promoting a joint effort for increasing development and solving the world's most important problems such as famine, health, housing, education, violence and the high cost of living. We would be able to approach the subject of equitable human rights and the wellbeing of every population.

The last G-20 reunion at Los Cabos, Mexico and the Rio+20 conference celebrated last June show how developed-creditor countries strongly impose their economic interests over the development and wellbeing of developing-debtor nations. Internationally, their economic objectives are to continue to increase their economy at any cost. These actions will soon enough have repercussions within the creditor countries internal economy if they do not develop and apply new measures immediately.

Humanity's dream of living in a just and equitable society with less hunger, more health and job opportunities is still possible. It all depends on our actions being the result of our respect towards our fellow human beings and our environment. We need to understand the great responsibility that we have among each other and that our actions will affect, one way or another, our future generations. Furthermore, our children will judge us based on the decisions we make and the actions we take today, whether we act responsibly or irresponsibly.

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IDEOLOGICAL MOVEMENTS IN PRIVATE LAW

Hans GIGER

SUMARY: I. *Fundamental outlines*. II. *Information as a pivot especially according to the Legal recognition*. III. *Consequences of the ideological change*. IV. *Outlook*.

I. FUNDAMENTAL OUTLINES

Time after time, the relation between economics and law has been the cause of problems and controverses. Information is the pivot around which all interpersonal transactions revolve. Like a magic formula it can conjure up, or dispel, conflicts. History lets us know that there are periods of a strictly progressive socialization which later will convert, as a result of change in attitude, into contractual freedom controlled especially by individual responsibility. As a member of the International Academy of Consumer and Commercial Law (USA), I try to implicate the idea and necessity of free commercial activities. Due to the fact that European and American influences spread out in the Swiss market, it seems to me the right time to point out the risks of a threatening socialization of law. Therefore the introductory part of these concises reflections focuses on the problems of legislating more in a fundamental manner; reflections somehow which repeats thoughts already formulated in former publications. When charting the route between sensible social protection and excessive tutelage, the legislator should be coerced towards a nondirigiste consumer protection based on the responsibility of the individual for his own actions. The new Swiss Consumer Credit Draft manifested new efforts of socialization (part II of the book). Social protection is increasingly characterized by the transfer of power and ultimately by tutelage. This could inevitably entail the socialization of the law and lead to difficulties of judgement, uncertainty on the part of the business community and of consumers, and to painful problems for trade and business - with the familiar effects on

private, economic and, last not least, also social matters. Ultimately, it could cause the economy to slow down and unemployment to rise.

II. Information as a pivot especially according to the Legal recognition

1. *Information as an instrument of power*

Information has a wide reach: it constitutes the core of education and training, and, indirectly, of personality. It forges man's image of himself and of his surroundings, and it shapes his views and decisions; a factor with far-reaching implications. Man is an integral part of a social system; he participates in the world around him, and he communicates. As from a certain level he does so through the medium of language.[1] Information is the pivot around which all interpersonal transactions revolve. Like a magic formula, it can conjure up, or dispel, conflicts. Control and manipulation of information are stepping stones towards the levers of powers. The fundamental importance of the right, and the will, to process and disseminate undistorted information is, sooner or later, brought home to the citizens of all states to a varying extent, particularly when it comes to decisions in the areas of legislation and legal cognition. In the course of any decision-making process (which entails processing of information, followed by the development, declaration and implementation of an intention), information is susceptible to distortion because each individual judges according to his own standards and in the light of his particular education, environment and personality. The more scope he has for exercising his judgment, the more likely it is to be arbitrary. It was to eliminate this risk that man created systems of law designed to apply to all facets of human co-existence.[2]

2. *Legislation as a "snapshot" of the current status of human Existence*

The application of a specific law is concerned with the problem —inherent in every society— of creating a broad and effective system of laws for regulating conflicts. In a democratically governed state, the "theoretical order" devised for all citizens by themselves is derived from public opinion.[3] In other words, the individual members of society themselves set the rules

1 Giger, *The defence of intellectual and moral habitat*, 477; Meese and Seiverth, Methods, 7.
2 For details see Giger, Legislation and responsibility, 1 ff.
3 Giger, *The protection of weaker parties*, 18 ff.

under which they wish to live.[4] Public opinion thus represents the views held by all citizens of a state and expressed by their representatives, on the manner in which human co-existence, and more particularly legal attitudes, have to be regulated so as to ensure a minimum of friction. The creative act of legislating is nothing more than a "snapshot" of the current status of human existence, with all man's needs, wishes, knowledge, insights, beliefs and intentions. Judging by the present state of formal legislative processes, experience shows that the reality[5] has usually changed by the time the law is brought into line to satisfy a particular need for correction. Thus, the revised or newly created law represents a "theoretical system" *for a reality that has been superseded*.[6] "Reality inevitably encompasses the attitude towards the value that the individual citizen assigns himself in relation to the collective, a value which also defines his relation to the prevailing order with regard to material goods, possession, and autonomy in transactions. It is the work mentality of the individual, more than anything else, that ultimately conveys the appropriate recognition and labeling signals.

3. *Evolution from the competition-minded to the welfare state*

A. *Caracteristic marks of the competitionminded state*

Any state of affairs and any development are shaped by factors which can be reliably held to communicate what constitutes a society and what the underlying state of mind of this society is. They are indicators —hence signals— which characterize the stage reached in a particular process of development. They communicate the individual criteria of judgment. The typical hallmarks of the meritocracy are familiar ones: its sights are set on improving the quality of work and prosperity. To achieve this, certain traits are indispensable: commitment, dedication, sense of achievement, conscientiousness, diligence, avid pursuit of know-how, interest in work, creativity, insistence on quality as well as quantity - to mention only a few of the milestones that mark the thorny road to success and prosperity. Add to this a competitive nature, in which strengths are genuinely measured against

[4] This —as everyone knows— is, of course, fiction. Public opinion is determined according to the delegation principle in that it is actually formed by representatives of the people (parliament).

[5] Legislation to take account of a particular situation is often initiated decades before it actually comes into effect.

[6] See also Giger, *Analyses of the regulations on arrears in rent law*, 155 ff.

those of the rivals at the highest possible level. Respect for the achievement of others, contempt for envy and jealousy,[7] and rewards for boldness and the courage of one's convictions, initiative and imagination are further essentials for the development and continued existence of the meritocracy. A society which evolves along such lines is shaped by a positive approach to work, making it prosperity-conscious and pro-business.

B. *Unlimited freedom as a principle*

The transition from meritocracy to an affluent society requires optimum competitive conditions. Entrepreneurial success can be achieved in many cases only through the relentless deployment of effective instruments. This presupposes a system of laws that guarantees more or less unlimited freedom of action. It is the rights of the powerful that have the upper hand.[8]The powerful are respected, honored, fostered and accorded privileges in the social hierarchies, economic structures; even in the laws and their application. The principles of the free market economy prevail. It is not regulated by a restrictive legislation. No limits are placed on innovation, and the resources that are mobilized to achieve success are solely limited by the imaginative scope of the entrepreneur. In this free play of forces, every decision constitutes an individual risk for which the entrepreneur bears the responsibility. He lives therefore in a constant state of tension between success and failure. His actions are, however, not shaped exclusively by his responsibility for them or by the fact that the rewards for his success accrue to him only slightly diminished and that he alone is answerable for any failures, which can even destroy him. Rather, society even accords him responsibility for others. Given the overriding goals of safeguarding supply and creating prosperity, he has, basically, to integrate himself with a minimum of friction into the world of production and sales. The boom of the 1970s showed that optimum economic conditions evolve in societies which are built up on the principles of freedom.

[7] Envy and jealousy are cancers of society because they give rise to unfair competition so as to eliminate superior rivals through non-achievement oriented information and claims. For details see Giger, *The defence of the intellectual and moral habitat*, 469 ff., particularly 480 ff.; also Wilhelm Korff, Friedrich, *A study of envy*, 69 f.; Gonzalo Fernández de La Mora, *The leveling effect of envy*, 1 ff.

[8] This was particularly true at the time of the first industrial revolution and the subsequent economic growth.

C. *Necessity of checking the unfettered freedom by individual responsibility*

It gradually came to be realized that unlimited power in the hands of individuals could not be held in check by individual responsibility. The need for corrective measures[9] is evident wherever individual decisions encroach upon, and even harm, the interests of others. In response to this need, it was pointed out that everyone had the same rights when it came to competing for market shares in the broadest sense of the term.[10] The argument that unfettered freedom nullifies the general right to freedom because the weak are unable to assert this right against the strong was initially ignored. However, the almost reflex effect of untiring efforts aimed at ideological conversion led to qualification of the concept of individual freedom, and protection of the weak became more and more of a catchword.[11] That was not the end of it. The trend towards an imperceptible undermining of the commitment to freedom, re-inforced not least by the inflationary growth of new social rights,[12] found its way into the traditional system of laws, initially through individual laws and groups of laws, and later through actual systems of laws.[13] The specter of, for instance, *special treatment of certain categories of people* such as "consumers" was evoked in order to accord them a special position.[14] This set in motion a development that has not yet run its course,

9 Giger, *The Limits of private autonomy in cartel law*, 11 ff.

10 Giger, *Increased social protection*, 9 f.: concerning the model image of the independent consumer.

11 Giger, *The protection of weaker parties*, 25 ff.

12 Giger, The threat to contractual freedom in consumer credit law 489 f.: "I expressed my doubts about the KKGE (the draft of the law on consumer credit) because I felt it undermined principles on which our state and legal system were built up. It seems to be a foreign body in the Swiss Code of Obligations: a priori balance of power is being substituted for the free play of forces even where this is still effective. It also signals danger for our market economy, which is conceived, generally speaking, as being self-regulating. In view of the present difficulties, it needs to be stimulated, rather than trimmed, by legal regulations if it is to survive in the long term".

13 Giger, *The planned consumer credit bill*, 18 ff.

14 Bibliography of critical and other literature concerning restrictions on economic and contractual freedom: Blankenburg *et al.*: *Rechtsberatung. Soziale Definition von Rechtsproblemen durch Rechtsberatungsangebote*, Neuwied und Darmstadt, 1982. Boller Jürg, "Verhältnis zwischen Wirtschaft und Presse", in *Bilanz* No. 11, 1983, 187 f.; Botschaft des Bundesrates an die Bundesversammlung betreffend den Entwurf zu einem Bundesgesetz über den Konsumkredit 12.6.1978 (communication quotes); Brandau Bodo Walter, "Die Bestimmung des auffälligen Missverhältnisses aus den marktwirtschaftlichen Daten des Konsumentenkreditgeschäftes und der Schutzwürdigkeit des Verbrauchers", in *FLF* (*Finanzierung, Leasing, Factoring*), 30th year No. 3, Dortmund, 1983, 79 ff.; Bunte H. J.: "Probleme der Ratenkreditverträge", in *Wertpapier-Mitteilungen* (*Zeitschrift für Wirtschafts- und Bankenrecht*), Supplements Nos. 1-5, Frank-

and the far-reaching implications of its destructive effect on progress are, for

furt a.M. 1984, 3 ff.; Canaris Claus-Wilhelm, "Schranken der Privatautonomie zum Schutz des Kreditnehmers", in *ZIP* (*Zeitschrift für Wirtschaftsrecht und Insolvenzpraxis*), No. 9, Cologne, 1980, 709 ff.; Dauner-Lieb Barbara, *Verbraucherschutz durch Ausbildung eines Sonderprivatrechts für Verbraucher*, Berlin, 1983, 13 ff.; Giger Hans, "Bedrohung der Vertragsfreiheit im Konsumkreditrecht", in *Schweizer Monatshefte*, 63rd year Vol. 6, Zurich, 1983, 483 ff.; Giger Hans, "Freiheit und Zwang im Konsumkreditrecht. Überblick und kritische Würdigung der Gesetzesvorlage", in *Neue Zürcher Zeitung*, No. 232 (6.10.1978), p. 35; Giger Hans, "Grundsätzliches zum immateriellen Umweltschutz. Die Verteidigung des geistig-moralischen Lebensraumes", in *Schweizerisches Umweltschutzrecht*, Zurich, 1973, 467 ff. and 632 ff.; Giger Hans, "Massenmedien, Informationsbetrug und Persönlichkeitsschutz als privatrechtliches Problem. Neue Aspekte im Bereich des privatrechtlichen Persönlichkeitsschutzes", in *ZSR* (*Zeitschrift für Schweizerisches Recht*), NF 89, Basel, 1970, 33 ff. and an extended version (particularly as regards defensive measures and sanctions), in *Juristen-Zeitung* 26, Tübingen, 1971, 249 ff.; Giger Hans, *Ratenkredit als legislatorisches Problem. Ein Alternativentwurf, Band 9 der Schriftenreihe zum Konsumentenschutzrecht*, Zurich, 1982 (2nd ed. Zurich 1983); Giger Hans, "Rechtliche Stellung des Konsumenten in der geplanten Neuordnung", in *ZBJV* (*Zeitschrift des bernischen Juristenvereins*) 116, 1980, 199 ff.; Giger Hans, "Sozialschutzwürdigkeit - ein gesetzgeberisches Problem", in *FLF* (*Finanzierung, Leasing, Factoring*), 30th year, No. 5, Dortmund, 1983, 179 ff.; Giger Hans, *Systematische Darstellung des Abzahlungsrechts unter besonderer Berücksichtigung des Fernkurs-, Unterrichts-, Mietkauf- und Leasingvertrags*, Zurich, 1972; Giger Hans, "Überforderter Konsumentenschutz? Ein Beitrag zum Schutz des Schwächeren", *Schriftenreihe zum Konsumentenschutzrecht über* "*Wirtschaftsfreiheit und Konsumentenschutz*", vol. 13, Zurich, 1983, 10 ff.; Giger Hans, *Une protection sociale renforcée - ligne directrice du législateur pour le nouveau droit du crédit à la consommation*, Berne, 1979; Hartwich, Hans-Hermann, *Sozialstaatpostulat und gesellschaftlicher status quo*, Cologne/Opladen, 1970; Hedemann, Justis Wilhelm: *Flucht in die Generalklausel*, Tübingen, 1933; von Heinemann Olgard, "Umfall auf Raten. Gedanken zum BGH-Urteil vom 12.3.1981", in *FLF* (*Finanzierung, Leasing, Factoring*), 28th year, No. 5, Dortmund, 1981, 186 ff.; Herzog, Roman, in: Maunz/Düring: Kommentar zum Grundgesetz, GG 20, VIII, Munich, 1980; Heusinger Bruno, *Rechtsfindung und Rechtsfortbildung im Spiegel richterlicher Erfahrung*, Cologne, 1975, 190; von Hippel Eike, *Der Schutz des Schwächeren*, Tübingen, 1982; Holzscheck *et al.*, *Die Praxis des Konsumentenkredits in der Bundesrepublik Deutschland - eine empirische Untersuchung zur Rechtssoziologie und Ökonomie des Konsumentenkredits*, Cologne, 1982; Kessler Roland, "Sittenwidrige Höhe von Darlehenszinsen. Anmerkung zum Urteil des Oberlandesgerichts Stuttgart vom 24.4.1979", in *BB* (*Betriebs-Berater. Zeitschrift für Recht und Wirtschaft*), No. 28, Heidelberg, 1979, 1423 ff.; Knauth Klaus-Wilhelm, "Entscheidung des BGH zum "Bender-Urteil", *in Die Bank. Zeitschrift für Bankpolitik und Bankpraxis* 6, Berlin, 1981, 299 ff.; Kochendörfer Heinz, "Sittenwidrige Höhe von Darlehenszinsen", in *NJW* (*Neue Juristische Wochenschrift*), No. 5, Munich, 1980, 215 f.; Larenz Karl, *Einführung zur Textausgabe des Bürgerlichen Gesetzbuches*, 27nd edition, Munich, 1983, 9 ff.; Leibholz/Rinck, *Grundgesetz für die Bundesrepublik Deutschland*, GG 20, 4th ed., Cologne, 1971, comment 12; Mayer-Maly Theo, *Das Bewusstsein der Sittenwidrigkeit*, Karlsruhe, 1971; Meese/Seiverth, *Methoden*, Munich, 1975; Münstermann Walter, "BGH contra OLG Stuttgart", *FLF* (*Finanzierung, Leasing, Factoring*), 28th year, No. 3, Dortmund, 1981, 101 ff.; Nef Hans, *Gleichheit und Gerechtigkeit*, Zurich, 1941; Olzen D., "Anmerkung (zum BGH-Urteil vom 12.3.1981)", in *JR* (*Juristische Rundschau*), Berlin and New York, 1981, 369 ff.; Ott Sieghart, "Zur Sittenwidrigkeit von Konsumentenkreditverträgen. Eine Stellungnahme zum Urteil des BGH vom 12.3.1981 - III ZR 92/97", in *BB* (*Betriebs-Berater*), Heidelberg, 1981, 937 ff.; Palandt/Heinrich, *Kurzkommentar zum Bürgerlichen Gesetz-*

the time being, only a matter for conjecture.

D. *Change of the mentality structure*

Any social protection law integrated into our traditional legal system has an inherent tendency to change the mentality structure underlying our laws. This is partially due to the "proliferation mechanism" with which it is associated. But what does this actually mean? There is certainly no question of "contagion" in this connection. But the very existence of social protection laws inevitably leads by way of justice with its "leveling out" effect, the need for uniform legal structures and the pilot effect, to a steady expansion, and thus progressive socialization, of the law. If a piecemeal policy entirely shaped by practical needs is pursued, the insidious undermining of the tra-

buch, 40th ed., Munich and Berlin, 1981; Peetz Hans-Günther, "Konsumentenkredit und Restschuldversicherung in der Rechtssprechung des Bundesgerichtshofs", in *ZIP* (*Zeitschrift für Wirtschaftsrecht und Insolvenzpraxis*), Cologne, 1980, 605 ff.; Reifner Udo, *Alternatives Wirtschaftsrecht am Beispiel der Verbraucherverschuldung. Realitätsverleugnung oder soziale Auslegung im Zivilrecht*, Neuwied und Darmstadt, 1979; Reifner Udo, "Die Rückabwicklung sittenwidriger Ratenkreditverträge", in *JZ* 39, 1984, 637 ff.; Rittner Fritz, "Der Beitrag zur Restschuld-Lebensversicherung und Darlehensvertrag", *Supplement DB* (*Der Betrieb*), No. 16, Düsseldorf, 1980, 3 ff.; Rittner Fritz, Zur Sittenwidrigkeit von Teilzahlungskreditverträgen. Die Grundsatzentschei-dung des BGH vom 12.3.1981 DB (Der Betrieb) (Düsseldorf 1981), 1080, in DB (Der Betrieb) No. 28 (Düsseldorf 1981) 1381 ff.; Saxer Lydia, "Missverständnisse im Kleinkreditsektor", *Wirtschaftsfreiheit und Konsumentenschutz*, Vol. 13, der Schriftenreihe zum Konsumentenschutzrecht über, Zurich, 1983, 128 ff.; Schluep Walter R., "Konsumentenschutz in Werbung und bei Vertragsabschluss", *Entwicklungstendenzen im schweizerischen Konsumentenkreditrecht*, Vol. 1 der Schriftenreihe zum Konsumentenschutzrecht über, Zurich, 1979, 185 ff.; Scholz Franz Josef, "Anmerkung zum BGH-Urteil of 12 March 1981", in *WM* (*Wertpapier-Mitteilungen. Zeitschrift für Wirtschafts- und Bankrecht*), No. 21, Frankfurt, a.M., 1981, 583 ff.; Scholz Franz Josef, "*Die* Praxis *des* Konsumentenkredits in der Bundesrepublik Deutschland?", in *FLF* (*Finanzierung, Leasing, Factoring*) 30th year, No. 2, Dortmund, 1983, 35 ff.; Scholz Franz Josef, "*Die* Praxis *des* Konsumentenkredits in der Bundesrepublik Deutschland? continued", in *FLF* (*Finanzierung, Leasing, Factoring*), 30th year, No. 3, Dortmund, 1983, 105 ff.; Scholz Franz Josef, "Der Ratenkredit als rechtswissenschaftliche und rechtspolitische Aufgabe", in *FLF* (*Finanzierung, Leasing, Factoring*), 31th year, No. 3, Dortmund, 1984, 75 ff.; Schulz Harald, "Kredit mit Restschuldversicherung in der Rechtsprechung des BGH zu § 138 BGB", in *FLF* (*Finanzierung, Leasing, Factoring*) 28th year, No. 4, Dortmund, 1981, 154 f.; Schulz von Thun Friedemann, *Miteinander reden: Störungen und Klärungen. Psychologie der zwischenmenschlichen Kommunikation*, Hamburg, 1982; Serick Rolf, *Eigentumsvorbehalt und Sicherungsübertragung*, III: Die einfache Sicherungsübertragung, 2. Teil, Heidelberg, 1970, 14; Watzlawick *et al.*, *Menschliche Kommunikation*, Bern, 1969; Weitnauer Hermann, *Schutz des Schwächeren im Zivilrecht*, Karlsruhe, 1975, 10 ff., especially 12 and 15; Zwanzig Jürgen, "Sondermacht für Teilzahlungsbanken im Konsumentenratenkredit?", in *BB* (*Betriebs-Berater. Zeitschrift für Recht und Wirtschaft*), No. 25, Heidelberg, 1980, 1282 ff.

ditional system of law is in danger of being overlooked, as are certain basic aspects of the problem.

III. Consequences of the IDEOLOGICAL CHANGE

1. *Implications in fact consisting in a gradual snowballing effect*

The change in attitude itself is a reality and is nothing other than the result of a combination of factors, all of them operating in the same direction: the period following the first industrial revolution was marked by the resurgence of a current of thought for whose proponents the notion of equality of all citizens held a special fascination. Its adherents were intent on dismantling privileges both real and perceived, they sought a "more equitable" distribution of wordly goods, viewed hierarchies in whatever form as inimical and generally set out to establish a new order of priorities. The vanguard of the movement was no longer progress as such but the demand for equal rights. This aim, to begin with covertly expounded by discreet gatherings, gradually developed into a mass movement which vociferously pressed its demands at the work-place, in demonstrations and in other forms of public manifestation. The result was a gradual snowballing, as causes produced effects, and effects in their turn became causes again. Such a chain of cause/effect/cause[15] is notoriously hard to break and automatically creates its own momentum. Hence, the well-known pendulum effect, involving swings from one extreme to the other.

2. *Implications in the law leading to a socializing effect*

It takes a long time for changes in mentality in the social and —even more so— in the economic environment to percolate through into the system and especially into the law, and even then their substance is filtered and often diluted. Anyone seeking to measure the legal perceptions of a nation as reflected in its legislative output must make due allowance for this built-in time-lag. Individual and collective perceptions as well as convictions as to the right way to organize human coexistence are transformed in the democratic law-making process into set rules of conduct. A change in the collective mentality can, it is true, be discerned by making a comparative analysis between existing laws and new laws, but the adjustment itself has to take place over

[15] Like the well-known conundrum of the chicken and the egg.

time. Thus, a change in the law can, by the time it is implemented, already have been overtaken by reality.

There is a further consideration which it is important to allow for in this context: the direction and quality of change depend largely on the character and frequency of the corresponding structures of legal rules. Within a given system, the individual is allowed a varying amount of free scope depending on the local or subject matter jurisdiction. This scope determines essentially whether a legal system is labeled "individualistic" or "collectivist" and, in view of their generic differences, separates —geographically— the Western from the Eastern Hemisphere. In the course of time, this classification has grown more difficult and has acquired another dimension. The outer form, the "packaging", is still based on the predefined scheme. However, the formal belief in a given system, under the pressure of exceptions which erode its basic principles, often suffers from e creeping change in substance due to a gradual swing in attitude with regard to the perception of right and wrong.

IV. Outlook

1. *General remarks*

In recent decades, not only in doctrine and practice but also in legislation, there had been a growing development in favor of subjecting legal activities and economic freedom to greater regulation.[16] It has supplied unmistakable signals that a change in the perception of what constitutes the "right law" derives from the analysis of existing legal rules. The change in mentality finds expression in the transition from the state based solely on the rule of law to the social state,[17] from the rules relating to the system and to protection to a system of social protection and from the rejection of to the advocacy of provisions embodying special rights and privileges.[18]

[16] Giger, Legislation and legal rulings in the year 2000 176: "It (the development, Ed.) is underlined and advanced by the activities of those parties who set themselves up as spokesmen for consumers and, instead of quality of work and prosperity, preach for an improvement in so-called quality of life. They demand shorter working hours, more free-time, longer holidays, more pay for less work, and thus undermine the very pillars of prosperity. Many of them will also openly admit to being hostile to business, to seeking to reduce performance and to rejecting prosperity. Such an attitude had to lead to a radical change in mentality, especially as it encountered little resistance".

[17] Giger, Commentary on the planned consumer credit bill 18 ff. (on the development); also Giger, The protection of weaker parties 32 ff.

[18] Giger, Increased social protection 29: "On peut très généralement comprendre sous le concept de législation de protection sociale tout système juridique d'exception

2. *Turning-points*

Anyone who has been keeping track of legal developments in Switzerland, even if only from afar and through the intermediary to the press, cannot have helped noticing in the past few years growing signs of indignation at the plethora of laws[19] promulgated primarily in response to pressure for social protection. This is a reaction to what is clearly perceived to be an extreme development; a reaction not only confined to parliamentarians[20] but also visible in broad segments of the population[21] and one which has also mobilized scholars and academics.[22] There is widespread exasperation not just at the formal but also - and more so - at the material excesses perpetrated which have resulted in the citizen being progressively deprived of his legal capacity.[23]

(Sondersysteme) qui, lorsque certaines catégories particulières d'individus sont parties à un rapport de droit, limite impérativement leur liberté contractuelle par des normes plus sévères qu'habituellement, dans le but d'équilibrer une inégalité de fait entre les parties contractantes".

19 The plethora of legal rules renders the instruments of the law progressively more complicated and impenetrable. The result is that the consumer cannot assert his rights —or only with difficulty— because he has no option but to rely on costly expert assistance. The regulatory mania thus has a boomerang effect. Cf. Giger, The deluge of laws as a time bomb p. 19 ff.

20 Cf. in this connection publications by Bank Julius Bär, Increasingly shallow legislation 3: "In order to finally rid itself of the burdensome debate surrounding a given bill, a majority of the chamber will force the adoption of a provision which it knows perfectly well to be controversial in the secret hope that this "fateful clause" will prove to be lethal and bring about the bill's speedy demise when it is submitted to the plebiscite. And the fact is that many a bill thus presented to the people by a peevish parliament has been found by the voters with their at times surprisingly sound instincts to be wanting —and has come to grief— by no means to the detriment of the area it was supposed to have regulated".

21 The attentive reader will detect the signals in the growing number of reports in the daily newspapers.

22 Buser Walter, The deluge of Laws 6 ff.; Hirschi Fred, Do paragraphs destroy legal consciousness? 17 ff.; also Kopp Elisabeth, The "deluge of Laws" - another slogan? 34.

23 Cf. on this point Giger, Tendencies towards a state credit policy 23; Giger, The creeping socialization of private Law 41; as well as publications by Bank Julius Bär. On the question of "hypertrophy" of legislative activity, 2: "Complaints about the overactive regulatory machinery of the state —at all levels, from laws, to decrees right down to the narrower bureaucratic area of implementing provisions, etc.— are today a common feature of contemporary analysis of public policy and indeed are justified. The sheer output of legal material and other standards is truly impressive and, were it not for those irksome "troublemakers" who sound the warning bell, the citizen might easily fail to perceive that he is being progressively robbed of his legal capacity. It is instructive here to recall the case of Sweden where even Conservatively minded people have had their natural resistance to government tutelage stifled by the overzealous social and fiscal embrace of the state".

It took quite a while for the legislative authorities to react to these developments and take remedial action. This reaction manifested itself to begin with in the varying degrees of success with which they fended off the blatantly excessive demands of parliamentarians who are die-hard proponents of social protection.[24] During the various stages on their journey into the statute books, numerous bills were, however, "defused", and encroachments on economic and contractual freedom deemed to be unacceptable failed to receive legislative blessing.[25] The *desire for change* communicated by level-headed citizens and scholars to a responsible majority of parliamentarians reached its culminating point in the debate surrounding the Consumer Credit Bill.[26] The rejection of a bill after more than eight years of permanent and intensive parliamentary debate represents a milestone in the history of Swiss legal policy.[27] This event, the like of which occurs only

[24] Cf. the opinion voiced by Oehler Edgar in the context of the parliamentary debate on the Consumer Credit Bill: "I cannot escape the impression that in this type of contract as elsewhere the work of the legislator does not wholly correspond to the political realities. It is imperative to take account of the actual circumstances and future developments" (Minutes of the delibe-rations of the National Council Commission on 23 April 1985, No. 78.043, p. 907).

[25] During the legislative process, the draft of the Federal Anti-Trust Act (Message of 13 May 1981), for example, was watered down in those areas where it would have encroached unduly on freedom; the popular initiative "concerning protection of the conditions of notice in the law governing contracts of employment" and in favour of amending the provisions governing the employment relationship in the Swiss Code of Obligations (Message of 9 May 1984); the popular initiative for the "protection of tenants", on the amendment of the law governing rental and lease relationships in the Code of Obligations and on the Federal Act on Measures to Prevent Abuse in Landlord/Tenant Relationships (Message of 27 March 1985); also the Federal Unfair Competition Act of 19 December 1986 (Message of 18 May 1983).

[26] Consumer Credit Bill (Message of 12 June 1978); definitively rejected by parliament in the final vote on 4 December 1986.

[27] The dynamics of this development have been succinctly described by Saxer Lydia. On the slow death of the Swiss draft consumer credit bill (p. 46) in a retrospective comment entitled "The Slow Death of the Swiss Consumer Credit Bill". She sums up the main lessons to be learnt in this concluding paragraph: "The events surrounding the Consumer Credit Bill highlight typical dangers inherent in the process of political opinion-shaping. Following a situation where there had been too little legislation in the area of social protection, the pendulum swung back into the opposite direction: a veritable orgy of regulation that has left no scope for the free will of the individual, that as deprived him de facto of his legal capacity. The citizen —declared to be capable of making up his own mind and constantly called to the polling booths— should not just be protected from the dominance of a stronger contracting party, but especially from himself. The endeavors of the authorities to achieve perfection ended in a debacle. Within the population, there is widespread disenchantment with the state which finds expression among other things in the call for less government interference. Various political parties subscribe to the maxim 'More freedom - less government'. The observer consequently gains the impression that, by voting down the Consumer Credit Bill, a number of center-right parliamentarians sought to demonstrate that they were not just paying lip-

every twenty or thirty years, was a shot across the bows for all those who still imagine that they can continue to undermine our fundamental freedoms with impunity. The result had been the EU-compatible Swiss Legislation of 8. October 1993. It seems to be a fact, that the new conception of the Federal Law on Consumer Credit, set in power the 1st January 2003, is unfortunately again founded on the conviction, that previous consumer protection law has shown an undue confidence in consumer's ability to make decisions for themselves.[28] Protection of mature consumers against abuse is no longer the guiding principle. Instead, the new law is far more interested in the legal tutelage of almost the entire population of discerning, capable adults, people which the Report condescendingly describes as "manipulated", and by implication unfit to exercise their own judgement.

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service to the fight against overregulation but were actually turning words into deeds in order to preserve a free legal and economic order. For Switzerland's consumer credit sector, this demonstration represents a mark of confidence; for the future, however, it is also a commitment to pursue on a free-will basis a business policy acceptable for all parties".

[28] Accompanying *Report* 14/15.

———, "Massenmedien, Informationsbetrug und Persönlichkeitsschutz als privatrechtliches Problem. Neue Aspekte im Bereich des privatrechtlichen Persönlichkeitsschutzes", in *ZSR*, NF 89, 1970, S. 33 ff.

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THE VISIBLE HAND OF EUROPEAN REGULATORY PRIVATE LAW(ERPL) - THE TRASNFORMATION FROM AUTONOMY TO FUNCTIONALISM IN COMPETITION AND REGULATION

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SUMMARY: I. *The hypothesis: erpl a self sufficient private legal order enshrining a new order of values*. II. *Creative destruction*. III. *The driving forces behind ERPL: economisation (internal market) and politicisation (governance). IV. The subject matter: the "visible" european private law*. V. *The construction of 'general principles of ERPL'. VI. Towards the gradual substitution of national private legal orders. VII. The outlook of the new order: three layers of European regulatory private law*. VIII. *Research desing*.

I. THE HYPOTHESIS: ERPL A SELF SUFFICIENT PRIVATE LEGAL ORDER ENSHRINING A NEW ORDER OF VALUES

There is a strong coincidence between ideological preconceptions of European constitution building and European private legal order building through the Draft Common Frame of Reference[1] which has not turned into the project on a Common European Sales Law (CESL).[2] The dictate at the moment

* This is an updated version of the original application for funding to the European Research Council, which was sucessfully improved in December 2010. The basic ideas behind the project are more fully developed in The Visible Hand of European Private Law, in Yearbook of European Law 2009, volume 28, P. Eeckhout/T. Tridimas (eds.), 2010, 3-60, translated into Italian, in Collana "Studi storici e guiridici" diretta da Guido Alpa e Roberto Mazzei, Seminari del Consiglio Nazionale Forense, 2010, 125-192, into Finnish, Lakimies 3/2010, 330-356, into Japanese, Hokkaido Journal of New Global Law and Policy, Vol. 12, 30 July 2011.

1 Draft Common Frame of Reference, Online Edition, 2009.

2 COM(2011) 635 final.

seems to convey, more than ever, a quest to embark on constitutional pluralism and private law pluralism, bearing different headings in the private law discourse: "Private Law and the Many Cultures of Europe" (*Wilhelmsson/E. Paunio/A. Phjolainen*),[3] "Private Law Beyond the State" (*Michaels/Jansen*),[4] or "Open Method of Co-Ordination" (*van Gerven*).[5] However, outside political and academic debates, European constitution building and European private law construction steadily continues via secondary law making with the support of the Member States and via by the ECJ and national courts. My project focuses on ERPL beyond the boundaries of autonomy and freedom of contract guided national private legal orders (*L. Raiser, H. Collins*).[6] I start from the following hypotheses:

— ERPL is developing through regulation and new modes of governance in subject matters usually regarded as being beyond traditional private law, for example consumer and anti-discrimination law, regulated markets, private competition law, state aids, public procurement, property rights and unfair commercial practices, risk regulation and standardisation of services,
— ERPL is striving for self-sufficiency, it is EU made and EU enforced, via old and new modes of governance,
— ERPL yields its own order of values, enshrined in the concept of access justice (Zugangsgerechtigkeit).

The focus of this socio-legal project lies in the search for a normative model which could shape a self sufficient European private legal order in its interaction with national private law systems.

- It aims at a new–orientation of the structures and methods of European private law based on its transformation from autonomy to functionalism in competition and regulation.
- It suggests the emergence of a self sufficient European private law, composed of three different layers (1) the sectorial substance of ERPL, (2) the general principles —provisionally termed competitive contract law— and (3) common principles of civil law.

[3] *Th. Wilhelmsson/E. Paunio/A. Phjolainen* (eds.), Private Law and the Many Cultures Europe, 2007.

[4] *R. Michaels/N. Jansen*, Private Law Beyond the State? Europeanization, Globalization, Privatization, (54) American Journal of Comparative Law 2006, 843.

[5] *W. Van Gerven*, Needed: A Method of Convergence for Private Law, in A. Furrer (Hrsg.), Europäisches Privatrecht im wissenschaftlichen Diskurs, 2006, 437.

[6] *L. Raiser, Die Zukunft des Privatrechts, 1971; H. Collins*, Regulating Contracts, 1999.

- It elaborates on the interaction between ERPL and national private law systems around four normative models: intrusion and substitution, conflict and resistance, hybridisation and convergence.

II. Creative destruction

The ERPL challenges the basis of our understanding of private law. Is the European Union —with the support of the majority of the Member States— 'destroying' 'our' national private law systems? What kind of private law is the European Union creating? Recalling de-juridification, de-politicisation and de-judicialisation (*Joerges*),[7] can it continue to be regarded as law? (*Walker*)[8] Is it a private legal order of big companies and informed customers/consumers who behave like small businessmen? Where do the truly weak groups stand and what role should be granted to small and medium sized companies?

I propose the use of *Schumpeter's* formula of creative destruction[9] as the starting point of analysis. Taken literally this formula would mean that private law, and its conception over centuries as an order inherently linked to the idea of a nation state, is drawing to an end. The European legislator would then be the 'terminator', who is undermining the ideological basis of the different national private legal orders, the overall assumption that *Privatautonomie*, *freedom of contract* and *autonomie de la volonté* are the sole and decisive denominators.[10] The standard justification for the opposite position is that ERPL does not develop in a legal vacuum. It is said to be based on and dependent of the national private law systems.

Much depends on the understanding, the role and the function of the state in a market economy. The European Union is not a fully-fledged state, but it is a strong regulator of private law relationships. In this sense, the European Union has much in common with the idea of the 'market state' (*Patterson/Afilao*).[11] If we assume that the European regulator is disconnect-

[7] *Ch. Joerges*, The Challenges of Europeanisation in the European Private Law, Duke Journal of Comparative and International Law 24 (2005), 149.

[8] *N. Walker*, Legal Theory and the European Union (2005) OJLS, 581.

[9] *http://transcriptions.english.ucsb.edu/archive/courses/liu/english25/materials/schumpeter.html*.

[10] See e.g. J. Basedow, Freedom of Contract in the European Union, 6 European Review of Contract Law, 2008, 901.

[11] *D. Patterson/A. Afilalo*, The New Global Trading Order, 2008. The relationship between the market state and European private law is more fully developed in H.-W. Micklitz/D. Patterson, From the Nation State to the Market: The Evolution of EU Private Law, EUI Work-

ing national private legal orders from their ideological basis, the question remains then as to what is '*constructive*' in the destruction process? I begin from the premise that the EU is yielding a new concept of private law, one which is distinct from national preconceptions and one genuinely anchored in the European legal order.

III. The driving forces behind ERPL: economisation (internal market) and politicisation (governance)

The driving force behind the changing patterns of private law result from the economisation of private law via the Internal Market Programme and from its politicisation as enshrined in EU governance (*Weiler*).[12] Governance builds on networks rather than hierarchy, participation and mutual learning rather than command and control, iterative rather than discrete processes. "*Ökonomisierung*" and "*Politisierung*" set the frame within this project for a deeper understanding of what actually occurs in the field of visible private law.

(1) Economisation and private law: The strong market–approach has somewhat superseded "les grandes idées politiques", which has guided the project of the "United States of Europe", at least until the early nineties. The Internal Market Programme has become the (most stable and consistent) driving force behind the European integration process. This has been even more so since the 2004 enlargement —the joining of ten (now 12) new Member States from Middle and Eastern Europe— and the failure of the European Constitution project. The Lisbon Agenda 2000,[13] the backbone of the "new economic approach", could be understood as a revival and reinvigoration of the Internal Market Programme, albeit in light of the 21st century with emphasis on industrial policies. More forcefully than ever before, the European Commission is using the different sectors of economic law to render Europe 'the most competitive economy of the world' (language introduced in the Lisbon Agenda).

Private law was and still is needed to give shape to the Internal Market - what I have termed the economisation process. However, the private law referred to is not that which exists in national legal orders, that guided by

ing Paper 2012/15 = to be published in B. van Vorren/St. Blockmans/J. Wouters (eds.) The EU's Role in Global Governance: The Legal Dimension, OUP 2012/2013.

[12] *J.H.H. Weiler*, The Transformation of Europe, Yale Law Journal (100) 1991, 2403.

[13] *http://europa.eu/legislation_summaries/education_training_youth/general_framework/c10241_en.htm*.

private autonomy and freedom of contract. Rather it has two faces: it is regulatory in the sense that it is required in order to constitute the Internal Market, and it is competitive since the philosophy behind the regulatory measures relies heavily on market freedoms and competition. The strengthened market bias is paving the way for the infiltration of the Anglo–American understanding of the role and function of law (*Stürner*),[14] which has normative implications: in the changing paradigm of justice, in the increasing importance of economic efficiency (via economic analysis of law in Europe), in economic impact assessments which forestall European law making; and once might even go so far as to imagine a gradual resemblance of European law to common law systems as opposed to continental codification.

(2) Politicisation of private law: The Internal Market Programme and "European Governance" emerged at the same time. Governance should close gaps between the capacity of the EU to promulgate rules and its ability to enforce them (*Héritier*).[15] The so-called New Approach on Technical Standards and Regulations of 1985[16] eventually led to the adoption of the so–called "comitology"; the regulation of administrative co-operation via committees. There is a direct link from "comitology" via "governance" to "European Constitution building", as reflected in legal theory (*Joerges*),[17] and European Governance mainly as a process of politicisation. This means, with regard to law and the role of the legal system in the European integration process, that the importance of law in the European integration process is decreasing whilst the impact of politics is increasing. There is no document of the European Commission establishing a link between governance and private law. However, one might argue that governance in private law compensates for the lack of traditional regulatory approaches in various boundary fields of private law as well as with regard to its main terrain, i.e. the right of obligations (DCFR).

Governance has a twofold impact on private law: it is fostering constitutionalisation of private law through constitutional and human rights (*Grundmann*)[18] and it is establishing new modes of law making and law enforcement (*Cafaggi*).[19] The question remains to be answered whether governance may only be democratically legitimated if basic procedural requirements such

[14] *R. Stürner,* Markt und Wettbewerb, 2007.

[15] *A. Héritier*, Explaining Institutional Change in Europe, Oxford University Press, 2007.

[16] OJ C 136, 4.6.1985, 1.

[17] *Ch. Joerges*, The Challenges of Europeanisation in the European Private Law, Duke Journal of Comparative and International Law 24 (2005), 149.

[18] *St. Grundmann* (ed.), Constitutional Values and Contract Law, 2008.

[19] *F. Cafaggi*, (ed.) The Institutional framework of European private law, OUP, 2006.

as transparency, participation and accountability are safeguarded and if the enforceability of these parameters via individual and/or collective rights is secured.[20]

IV. The subject matter: the "visible" European private law

The fields of analysis are united by a predominant Internal Market perspective combining the four freedoms with competition.

(1) A new order of values: ERPL is not bound to a model of social justice in the sense of distributive justice as it is known in the national legal orders in the form of the materialisation of contract law. ERPL is dancing to a different theoretical tune. Its scope is to ensure access to the Internal Market for those who cannot manage to pass the threshold by themselves. ERPL formulates a normative programme for setting access barriers aside. I have chosen the term *'access justice (Zugangsgerechtigkeit)'*, which goes beyond a libertarian concept of freedom, placing the realisation of access and the surmounting of possible impediments in the hands of individuals.[21] Access justice requires activity on the part of the EU in order to deconstruct possible barriers to the internal market. Private autonomy in ERPL is always only ever regulated private autonomy. It is not, unlike national orders, a given. Regulated autonomy serves the paradigm of access justice.

(2) The scope of regulatory private law: Elsewhere (*Yearbook of European Law*),[22] I have set out the fields inclined to ERPL: 1) consumer law; 2) non-discrimination law; 3) regulated markets: telecommunication, energy, transport; insurance, capital markets and company law; 4) property rights and unfair commercial practices law, 5) private competition law, state aids and public procurement; 6) regulation of health and safety; and 7) standardisation of services outside regulated markets. Each of these areas specifically contributes to ERPL, via mandatory rules, via co- and self-regulation.

V. The construction of 'general principles of ERPL'

These general principles (*Tridimas*)[23] reflect the functional approach of the ERPL. ERPL constantly blurs the lines of demarcation between legal fields,

[20] for a discussion M. Dawson, New Governance and the Proceduralization of European Law: The Case of the Open Method of Coordination, phd EUI Florence 2009.

[21] H.-W. Micklitz (ed.), The Many Concepts of Social Justice in European Private Law, Elgar 2011.

[22] See reference in fn. 1 and St. Grundmann, Europäisches Schuldvertragsrecht, 1999.

[23] T. Tridimas, The General Principles of EU Law, 2nd edition, 2006.

public and private law, statutory regulatory law and private regulation (the instrumental use of private law via private actors), regulatory law and private-autonomous law, between legal effects and interdependencies of apparently adjacent legal fields, between individual and collective legal constructs, and even between bilateral and a multisided contractual model.

(1) The instrumental protective control approach: The addressees of European private law regulation are vulnerable people, in particular part-timer employees, pregnant women, young people and children, but also business people. The protective approach is to be understood as instrumental. The addressees are the duty-bearing beneficiaries of regulatory private law. They ought to be reintegrated into the labour market. Consumers should assist the breakthrough of cross-border exchange of goods and services. Business people should gain access to new markets, which have thus far remained closed. Protection is always functional, it pertains to the tasks of the particular addressees in their own sectors of the economy.

(2) The interlocking of advertisement, pre-contractual information and contract conclusion: The legal medium through which this aim is achieved is information regulation. Contract related directives and regulations aim to improve the legal position of the weaker assisted by a network of informational duties. The closer to the point of conclusion, the greater the duty to provide information. Duties of transparency, pre-contractual information duties and actual conclusion of contract rules converge. The scope of this paradigm change, initiated by regulatory private law, can be seen in the necessity to rethink the need to fence off the legal effects of unfair commercial practices from its impact on contract law.[24] Actions for injunction, setting an end to unfair commercial practices, might gain importance in private law follow on disputes.

(3) Competitive and contractual transparency: Competitive transparency ought, like the framework rules on competition, state aids, and public procurement law, guarantee pre-contractual competition. Competitive transparency ought to put a contracting party in a position so as to be capable, prior to concluding the contract, of recognising and weighing up the pros and cons of a potential contract with various contractual partners on the basis of the information provided. Contractual transparency, on the other hand, ought to place parties in a position of understanding the reciprocal rights and duties that flow from a contract once it is concluded.[25] Competi-

[24] H.-W. Micklitz/N. Reich, N. Reich, AGB-Recht und UWG – (endlich) ein Ende des Kästchendenkens nach EuGH in Perenicova und Invitel? EWS 2012, 257-264.

[25] A major German insurer (ERGO) has set up a program which it is heavily advertising and which aims explicitly at improving the comprehensibility of insurance contracts.

tive and contractual transparency are not only intertwined on account of their content, they are interlocking because of the formation of legal remedies. A breach of the principle of competitive transparency in the prelude to a contract can have effects in the context of contractual transparency and therefore on the validity of the contract itself.

(4) Standardisation of contracts via information duties: Since the 1980s, ERPL has tried and tested informational duties as a means of rectifying the instrumentally protection-orientated approach, in particular in the field of services. The informational duties are so narrowly drafted, that they actually come close to providing a contractual template.[26] ERPL subjugates, the contract to various purposes. Only a closed and relatively consistent contractual model, identical throughout the EU, can guarantee that such contracts are concluded and that the corresponding sectors achieve the sought after aims. The standardisation meets the interests of the trade. Rather than autonomy and free negotiation of contractual rights and duties being decisive here, the ensuring of functionally calibrated contract for the relevant purpose is key.

(5) Elimination of market distortions: Black and grey lists with incriminating contractual stipulations have had a rather more invalidating effect. Here, we are concerned with the elimination of contractual features which have been earmarked as undesirable from the perspective of the Union legal order. Traditionally, the instruments of legal control are analysed under the perspective of social calibration of contract law. ERPL is equipped with three types of rules, which should be weeded out with the help of their particular contractual techniques, a) horizontally, just as they come to be expressed in the unfair terms and the unfair commercial practice directives,[27] b) thusly related to certain branches, such as in insurance law,[28] and c) contract type-related prohibitions, which are distributed over all of European private law.[29]

(6) Post-contractual cost-free or cost-reduced withdrawal and cancellation rights: The free or economical reasonable escape from a contract is one of the key

[26] That is why it does not suffice to criticize the rise of information duties under a law and economics perspective. It might well be that information duties are expensive for business and useless for consumers, but this does not deprive information duties from being used as building blocks for the elaboration of model contracts, see H. Collins (ed.) Standard Contract Terms in Europe, A Basis for an Challenge to European Contract Law, Wolter Kluwer, 2008.

[27] Directive 93/13/EEC on unfair terms in consumer contracts, Directive 2005/29/EC on unfair commercial practices.

[28] J. Basedow/T. Fock (Hrsg.), Europäisches Versicherungsrecht, Band 1 und 2, 2002.

[29] E.g. mandatory provisions in the time sharing Directive 2008/122/EC, the package tour directive 90/314/EEC or the consumer sales Directive 99/44/EC.

instruments of competitive contract law. Reduced risk in contract conclusion and reduced risk in contract escaping correlate. ERPL tends to make the entry into a contract as easy as possible, in that the addressee no longer bears or bears only a very easily discharged duty to research the information relevant to the contract; rather, the information is available to him/her by law. By means of the cordoning off of unfair commercial practices and contract law, which can occur as a result of the interpenetration of the legal effects of individual and collective legal protection, pre-contractual protection against dis- or misinformation takes on a new quality. If this mechanism for whatever reason fails, the needy addressee has the option of quickly and easily stepping back from the contract, free of costs or at low costs. The ECJ *(Quelle, Messner, Putz/Weber)*[30] has confirmed such an interpretation.

(7) Legal protection through ADR, judicial and administrative enforcement: As the European Union has no explicit competences for regulating enforcement, perhaps, with the exception of transborder issues, enforcement is integrated into the subject matter of regulation. Outside continental private legal orders, substantive and procedural law are not really separated. Slowly, the institutional framework is taking shape, in which collective legal protection can be situated. Emphasis is shifting from judicial to administrative enforcement via regulators, maybe even in the upcoming domain of collective compensation. In relation to the calibration of individual legal protection, ERPL rules provide for subject related individual rights and remedies. These individual rights and remedies are never meant to be exhaustive. The respective directives and regulations repeat in mildly varying terms, the ECJ-coined formula that legal protection must be effective, deterrent and proportionate. Far more concrete are the attempts of the EU to oblige the Member States to develop suitable non-coercive conflict resolution mechanisms. At the time of writing the EU is about to introduce an EU wide harmonised mechanism for Online Dispute Resolution and Alternative Dispute Resolution.[31]

VI. Towards the gradual substitution of national private legal orders

My suggested perspective, one which looks at the national private legal orders from the perspective of ERPL, allows for the formulation of a set of hypotheses which suggest deeper, if not dramatic, changes in private law

[30] ECJ Case C-404/06 - Quelle, ECR 2008, I-2685; ECJ Case C-489/07 - Messner, ECR 2009, I-7315; ECJ joined Cases C-65/09, C-87/09 - Putz/Weber 2011 ECR I-nyr.

[31] *http://ec.europa.eu/consumers/redress_cons/adr_policy_work_en.htm*.

matters. What I am trying to formulate are *conceptual and normative assumptions* on the possible future development of the ERPL to displace national private legal orders thereby turning the different fields into self-sufficient legal orders widely disconnected from the national private law strand. This could be realised via the downgrading of international private law, via the substitution of minimum with maximum harmonisation, and last but not least via the transformation of directives into de facto regulations.

(1) Decreasing the role of international private law: From an orthodox view, Rome I (Regulation 593/2008 on contractual obligations) and Rome II (Regulation 864/2007 on non-contractual obligations) are milestones in the development of a bottom-up European private law via the balancing out of conflicts between 27 divergent legal orders and their values. There is room for international private law, as long as the application of the rules, whether private or public, does not stop at the border. Only where national rules are bound to their territorial scope is international private law out of play (*Muir Watt*).[32] However, ERPL is intended to set common European standards which are bound, if at all, to the territory of the European Union (*Ingmar*).[33] That is why Rome I and Rome II are only of limited significance coming into play only where EU law does not lay down the standards itself, either by minimum or maximum harmonisation, or by anchoring the country of origin principle. The EU legislature did not even allow for the acknowledgment in Rome I or in Rome II of the DCFR as a voluntarily 28th private legal order. For the perpetuation of varied value-orders there remains little scope.[34]

(2) Better regulation through increased consistency and coherency: Since the promulgation of the Lisbon Agenda 2000, the EU has made it its task to legislate more coherently, and to avoid a fragmentation of results to similarly rooted problem cases. The European Commission even offers a particular website on 'better regulation'.[35] The efforts toward rendering the various fields of ERPL more consistent and strengthening its efforts in view of establishing better implementation practices in the Member States are obvi-

[32] H. Muir Watt, Integration and Diversity: The Conflict of Laws as a Regulatory Tool, in F. Cafaggi (ed.), The Institutional Framework of European Private Law, 2006, 107; Ch. Joerges/F. Rödl, Zum Funktionswandel des Kollisionsrechts II: Die kollisionsrechtliche Form einer legitimen Verfassung der post-nationalen Konstellation, in: Calliess/Fischer-Lescano/Wielsch/Zumbansen (Hrsg.), Soziologische Jurisprudenz. Festschrift für Gunther Teubner zum 65. Geburtstag, 2009, 775.

[33] ECJ, C-381/98 – Ingmar ECR 2000, I-9305.

[34] See H. Muir-Watt/R. Sefton-Green, Fitting the frame: an optional instrument, party chance and mandatory default rules, in H.-W. Micklitz/F. Cafaggi (eds.), European Private Law After the Common Frame of Reference, 2010, 201.

[35] *http://ec.europa.eu/governance/better_regulation/index_en.htm*.

ous. Implicitly the European Commission pushes for the verticalisation of the different areas, thereby making the horizontalisation at both the EU level i.e. between the various areas —and at the national level i.e. between the EU rules and the national private legal orders— more difficult. A tried and tested means to separate horizontal national and sectoral EU regulatory law, would be the conversion of EU directives into EU regulations. A general tendency in this direction cannot be detected, even if the Brussels Regulation, Rome I, Rome II, bits and pieces of energy and telecommunication law, as well as the entirety of passenger law have been promulgated in the form of regulations. However, the European Commission[36] is gradually shifting the focus from that of replacing directives with regulations.

(3) Expanding competences through regulatory techniques: The European Commission paid great attention to the principle of mutual recognition as well as the country of origin principle, but failed in the end. Currently, it is concentrating its efforts on the anchoring of the principle of full harmonisation in regulatory private law.[37] The consequences of the about-turn from minimum to maximum harmonisation are serious. Regulatory competence passes to the EU, which oversees the implementation process and can engage the ECJ's controlling function. New juridical battle lines are drawn, partly triggered by the ECJ and ideologically (not argumentatively) in line with the Lisbon Agenda (*Gonzales Sanchez, Gysebrecht, VTB, Mediaprint, Plus Warengesellschaft*),[38] as the question becomes increasingly prominent, to what extent does full harmonisation or mutual recognition stretch? There is a close relationship between favouring or at least admitting full harmonisation and rejecting mutual recognition. The rejection of the principle of mutual recognition, which contains a conflict of law element in respect of differences, comes at a price. Paradoxically enough, it promotes the trend towards (full) harmonisation.

(4) Governance through EU induced private regulation: EU induced private regulation, i.e. the regulations and directives in the various fields setting incentives for private regulation, appear as just another means to prolong the instrumental use of regulatory law in completing the objectives of the Internal Market. Transplanted into the perspective of better regulation which strives for coherency and consistency, direct or indirect state induced private regulation

[36] COM (2007) 502 final.

[37] For an overall discussion G. Howells/R. Schulze (eds.), Modernising and Harmonising Consumer Contract Law, 2009.

[38] ECJ, Case C-183/00 Gonzales Sanchez ECR 2002, I-3901, ECJ Case C- 205/07 Gysbrechts ECR 2008 I-9947; ECJ Case C-261/07 and C-269/07VTB-VAB ECR 2009, I-2949; ECJ Case C-540/08 – Mediaprint ECR 2010, I-10909; ECJ Case C-304/08Plus Warengesellschaft ECR 2010, I-217.

though being part of the better regulation approach seems to point exactly into the opposite direction – incoherency and inconsistency. Whilst it seems true that sector related private regulation must fit the needs of the particular business in question or the particular purpose the EU rules are designed for, it seems equally necessary to underline that the principles of transparency, participation, accountability and judicial review should apply equally to all forms of private regulation, whatever the subject matter might be (*Cafaggi, Joerges*).[39]

(5) Creeping competences through new modes of law making and law enforcement: Academic attention is focusing on new modes of law making, both inside state induced private regulation and outside (*Cafaggi/Muir Watt*).[40] What is much less visible is that the European Commission is becoming more and more involved with law enforcement. Conflict resolution; be it individual or collective shall be managed. This seems to be the European Commission's idea via regulatory agencies within the respective fields of competence. Where there are no European regulatory agencies, or where the European regulatory agencies have no formal regulatory competences, the European Commission steps in and formulates enforcement strategies and enforcement programmes outside its formal competences putting pressure on the Member States and their enforcement entities, be they administrative or not, to direct their attention to those issues which, according to the European Commission, deserve prior attention in securing compliance with the respective European rules. In this sense, the European Commission is developing entirely new modes of enforcement governance, it is out-sourcing enforcement to private companies, and establishing networks within which the lines between administrative and profit orientated private enforcement strategies are intermingled.[41]

VII. The outlook of the new order: three layers of European regulatory private law

Neither the Member States nor the European Commission have grasped the nettle with regards to clarifying the relationship between the legal or-

[39] Ch. Joerges, The Challenges of Europeanisation in the European Private Law, Duke Journal of Comparative and International Law 24 (2005), 149; F. Cafaggi, (ed.) The Institutional framework of European private law, OUP, 2006.

[40] F. Cafaggi/H. Muir Watt (eds.), Making European Private Law, Governance Design, 2008; F. Cafaggi/H. Muir Watt (eds.), The Regulatory Function of European Private Law, 2009.

[41] See H.-W. Micklitz, Administrative Enforcement of Private Law, in R. Brownsword/H.-W. Micklitz/L. Niglia/St. Weatherill (eds.), Foundations of European Private Law, Hart Publishing 2011, 563-591.

ders. This task has fallen to national and European courts, as well as to the academia. I will define the different layers of European regulatory private law and national private law which have been yielded out of the ongoing process of the Europeanisation of private law. This could easily be understood as an attempt to recognise a kind of new 'Ordnung' in the chaos (*Möslein*)[42] which results from the ongoing destruction of national private legal orders.

(1) Self-sufficient sectoral European market orders: The European Union regulates central areas of economic life, without considering the interpenetration of public economic and private law, overstepping the boundaries between state made law and private made law through new forms of governance in the rule setting via co-regulation and enforcement via outsourcing and privatisation. My suggestion is that behind this lies the implicit normative and conceptual assumption that sectoral orders may, broadly speaking, stand for themselves. I would suggest the following trend towards self-sufficient sectoral legal orders: *horizontal orders*: a) consumer law together with unfair commercial practices and b) anti-discrimination law, these two areas are at the forefront of the current analysis; *vertical orders*: a) regulated markets – telecommunication, energy, transport and financial services, b) pre-market risk regulation for chemicals, pesticides, foodstuff, consumer goods, post market control and product liability, c) private competition law, state aids and public procurement and d) regulation of services via European standards bodies.

Self-sufficiency has two strains, law making and law enforcement. Law making no longer lies in the hands of the European Union alone. Through co-regulation and self regulation a variety of rule setting institutions join in. The law making process has become heteronomous. The combination of public law making and private law making via co-regulation paves the way for the internationalisation of standard setting. Secondly self-sufficiency refers to the phenomenon that each market order may —this again is my assumption— function without a direct link to national private legal orders. That is why it does not suffice to look at the substantive law. A full understanding of the closeness of the sectoral market orders requires the inclusion of enforcement in the analysis: via regulatory agencies or via self-regulatory bodies, via individual or collective actions, via conflict resolution through litigation in courts or before administrative authorities or via dispute settlement through agencies, through self-regulatory bodies or through collective actions.

(2) General principles in European regulatory private law: The suggested *general principles* (see point 5. In this text) shall ideally reveal common denominators

[42] F. Möslein, Contract Governance and Corporate Governance, JZ 2010, 72.

between the various fields of European regulatory private law. They shall operate like a thread sewing the still heterogeneous areas together and allowing for mutual transplants across the narrow boundaries of the dispersed areas of European regulatory private law. Inherent to such thinking is the idea that European regulatory law is guided by a philosophy that, methodologically speaking, justifies cross-border (between the different areas of European regulatory private law) fertilisation. Setting consumer law aside it seems as if the Member States have followed the European approach in separating regulatory private law from the body of the national civil codes – as far as they exist. This facilitates the development of a self-sufficient European regulatory private legal order considerably.

(3) General principles of civil law: At a time when the political future of the CESL is still unsecure, while simultaneously however, references from the national courts to Luxembourg in private law matters are heavily increasing, the ECJ has taken a bold step forward, on proposal of Advocate General *Maduro*, the ECJ refers in *Hamilton*[43] for the first time, to the '*general principles of civil law*'. In two further judgments decided in 2009, *Messner*[44] and *Audiolux*,[45] both on proposal of AG *Trstenjak*, the ECJ confirmed its preparedness to elaborate on the notion of 'general principles of civil law'.

The ECJ does not provide much guidance as to the origins of the 'general principles'. AG *Trstenjak* and, in relying on her opinions, the ECJ start from a comparative law approach via references to PECL, the DCFR and the Acquis Principles. There seems to be a certain preparedness to upgrade the DCFR to some sort of expert restatement of soft law standing. In such a perspective, the DCFR could serve as a constant source of 'inspiration' for developing principles, but not for seeking guidance to clear cut solutions. This move has raised much concern and debate in private law theory.[46] Outside and beyond the comparative analysis of European 'rules' the widely recognised constitutionalisation process of private law[47] provides

[43] ECJ Case C-412/06 - Hamilton, ECR 2008, I-2383.

[44] ECJ Case C-489/07 - Messner, ECR 2009, I-7315.

[45] Case C-101/08 – Audiolux, ECR 2009, I-09823.

[46] U. Bernitz (ed.) General Principles of EU law and European Private Law (forthcoming 2012), see also St. Weatherill, The principles of civil law as a basis for interpreting the legislative acquis, ERCL 2010, 74.

[47] O. Cherednychenko, Fundament Rights, Contract Law and the Protection of the Weaker Party: A Comparative Analysis of the Constitutionalisation of the Contract Law with Emphasis on Risky Financial Transactions, doctoral dissertation – Utrecht University, 2008; Ch. Mak, Fundamental Rights in European Contract Law. A Comparision of the Impact of Fundamental Rights on Contractual Relationships in Germany, the Netherlands, Italy and England, Alphen aan den Rijin: Kluwer Law International, 2008.

for an additional source, via the European Economic Constitution and the Charter of Fundamental Rights. The former opens the door to the case law on the four freedoms in all its ambiguities and in its impact on private law (*Steindorff*),[48] the second to the increasing importance of the Charter in the interpretation of EU law. In *Kücükdeveci*[49] the ECJ recognised the horizontal direct effect of the Charter, thereby overcoming reservations voiced in the Lisbon Treaty against the applicability of the Charter.

VIII. Research desing

In the overall project which started in September 2011 and which will last until August 2016, I will demonstrate (1) the transformation of European private law from autonomy to regulation and competition and (2) the emergence of a new order of values enshrined in the concept of access justice/Zugangsgerechtigkeit. This twofold shift produces tensions between the alleged market bound European private law and the state bound national private legal systems.

In a *first* step I will sketch four normative models on the relationship between the two legal orders —conflict and resistance— intrusion and substitution —hybridisation— convergence and their theoretical grounding in legal theory and institutional economics. These four normative models constitute the areas in which socio-legal research needs to be undertaken. In a *second* step I will link the four normative models to particular types of institutions:

- Conflict and resistance to differing orders of values,
- Intrusion and substitution to regulated markets,
- Hybridisation to remedies and
- Convergence to co/self-regulation.

This allows me to transform the overall theoretical frame into a concrete research design around the four normative models and their particular links to European regulatory private law. Based on the findings in the four sub-projects, in the *third* step, I will give shape to the suggested transformation process, from autonomy to regulation and competition and to the emergence of a new order of values.

[48] E. Steindorff, EG-Vertrag und Privatrecht, 1996; A. Hartkamp, European Law and National Private Law, Kluwer 2012.

[49] There is a wealth of literature on horizontal direct effect of fundamental rights, mainly in connection with the constitutionalisation debate, see fn. 48.

As the project is now lasting for more than a year the following is more than a description of the envisaged method it is likewise a progress report on a project in action. We have set up our own website which reports on the ongoing activities.[50]

(1) Step 1 – Four normative models and their theoretical grounding: The four normative models are intended to capture the set of variants available in the relationship between European regulatory private law and national private law. They reflect of what I have termed European regulatory private law. A first workshop organised in May 2012 in Florence is aiming at deepening and clarifying the meaning of the four models.[51]

Conflict and resistance: This is suggested as one of the possible reactions of the Member States. The perspective is that the Member States do not give way to the intruding European regulatory private law. Instead, they provoke a clash between the European regulatory private law and the national law and set limits to where the intruding law ends and where the national laws begin.

Intrusion and substitution: This is suggested to be the perspective of the current EU law-making and law enforcement strategies, enshrined in the idea of a self-sufficient order composed of three major elements: (1) the horizontal and vertical sectoral rules; (2) the general principles enshrined in the horizontal and vertical sectoral rules; (3) the general principles of civil law.

Hybridisation: This is suggested to be an overall normative model of a composite legal order, within which the European and the national legal orders both play their part in some sort of a merged European-national private legal order. Hybridisation means that the legal character of the respective rule is neither European nor national. It bears elements of both legal orders and is therefore supposed to be hybrid.

Convergence: This is suggested to be a process of mutual approximation of the two different legal orders. They are not merged like in the concept of hybridisation, they still exist side by side, but they are drawing nearer to each other. Convergence is not bound to mandatory standards and default rules. It instead enshrines in particular the new modes of governance, co-regulation and self-regulation, which are enhanced by limited and limiting state powers.

[50] *http://blogs.eui.eu/erc-erpl/*.

[51] H.-W. Micklitz/Yane Svetiev (eds.), A self-sufficient European private law – A viable concept? EUI Working Paper 2012/31.

A *common theoretical background*

The four categories share a common theoretical background. The idea is to combine legal theories on the transformation of private law into economic law (*L. Raiser*)[52] with theories analysing private law beyond the state (*Michaels/Jansen*).[53] In order to fully grasp the change in paradigm the project draws on institutional economics as an analytic framework. A first workshop organised in September 2012 was devoted to the deepening of the methodological approach.[54]

The concept of 'institutions'[55] that I intend to use in order to get to grips with the 'substance' of European regulatory private law —understood as the rules regulating the structure of human interaction, composed of formal (legal) and informal (social) constraints and their enforcement— complies with the institutional design of legal orders, notwithstanding their origin, be it European or national. In this light, legal theories help to understand and to explain the transformation process on a more abstract theoretical level. The insights of institutional economics allow for an analysis of how exactly the transformation process of the two legal orders occurs or in the language of institutional economics how the 'institutional change' reaching beyond national political economies manifests itself.

The strong sometimes even static association of a particular type of national political economy does not leave much room for the interpenetration of different political economies. In such a perspective, the non-convergence thesis of legal orders defended by *P. Legrand*[56] and the categorisation of the varieties of capitalism developed by *Hall/Soskice*[57] share a common origin. This variant will have to be analysed under the category 'conflict and resistance'. National political economies, just as national legal orders, stand side by side. The different 'autonomies' enshrined in Member States' private legal orders would then have to be mobilised against European regulatory

52 L. Raiser, Die Zukunft des Privatrechts, 1971.

53 R. Michaels/N. Jansen, Private Law Beyond the State? Europeanization, Globalization, Privatization, (54) American Journal of Comparative Law 2006, 843.

54 *http://blogs.eui.eu/erc-erpl/activities*.

55 "Institutions: The rules of the game: the humanly devised constraints that structure human interaction. They are made up of formal constraints (such as rules, laws, constitutions), informal constraints (such as norms of behaviour, conventions, self-imposed codes of conduct), and their enforcement characteristics", *http://www.coase.org/nieglossary.htm*.

56 P. Legrand, European Legal Systems Are Not Converging (1996) 45 ICLQ 52.

57 P. A. Hall/D. Soskice (eds.): Varieties of Capitalism: The Institutional Foundations of Comparative Advantage, 2001.

intrusion. National legal orders, being understood as institutions, are suggested to build barriers against the incoming tide of European regulatory private law – to paraphrase the famous word of *Lord Denning*.[58]

Just like private law theory is becoming increasingly involved with the debate on private law beyond the state, research in institutional economics is reaching further and further beyond the boundaries of national political economies, thereby emphasising 'institutional change' and/or 'institutional flexibility' (*Lane/Wood*)[59] The more radical strand of the new research in institutional economics yields the question whether private legal orders would have to be understood as institutions, disconnected from the nation states and organised around markets, not around states. Particularly telling are the findings on regional and sectoral varieties of capitalism (*Crouch/Schröder/Voelzkow*).[60] This comes near to observed trends in European regulatory private law striving for normative self-sufficiency, here captured in the model of 'intrusion and substitution'.

Somewhere in the middle lies the task of combining an emphasis on institutional flexibility with retention of the idea that there exits distinctive types of political economy, resulting from the country's history, enshrined in the common knowledge and the common culture (*Hall/Soskice*).[61] The combined approach, the so-called historical institutionalism, introduced two categories into the debate —hybridisation and convergence *(W. Streek/K. Thelen,*[62] *in legal theory N. Reich,*[63] *v. Gerven*)— which have become fashionable in legal doctrine, often without disclosing its origin in institutional economics. In institutional economics both hybridisation and convergence imply the need to look at the formal constraints, the informal constraints and the enforcement characteristic in order to get a full picture of the institutional change. Both concepts seem to be well suited in catch-

[58] ...when we come to matters with a European element, the treaty is like an incoming tide. It flows into the estuaries and up the rivers. It cannot be held back.. (1974) 2 AII E.R. 1226, 1231.

[59] Ch. Lane/G. Wood, Capitalist diversity and diversity within capitalism, Economy and Society, 39 (2009) 531.

[60] C. Crouch/M. Schröder/H. Voelzkow, Regional and sectoral varieties of capitalism, Economy and Society, 39 (2009), 654.

[61] P.A. Hall/D. Soskice (eds.): Varieties of Capitalism: The Institutional Foundations of Comparative Advantage, 2001.

[62] W. Streek/K. Thelen (eds.), Beyond continuity: Institutional change in advanced political economies, 2005.

[63] N. Reich, Horizontal liability in EC law: Hybridization of remedies for the compensation in case of breaches of EC rights, CMLRev. 2007, 705.

ing the compartimentalised character of European regulatory private law, whilst insisting on the genuine national character of private legal orders, thereby yielding hybrid institutions or provoking convergence of inherently different institutions.

(2) Step 2 – The four normative models (conflict – intrusion – hybridisation – convergence) and their impact on the different subject matters: Combining legal theory and institutional economics allows for building correlations between the relationship between intrusion – conflict – hybridisation – convergence and the different areas of European regulatory private law:

- Conflict and resistance: value conflicts between different forms of capitalism are suggested to emerge in consumer, anti discrimination, unfair commercial practices law, private competition, state aids and public procurement law, thereby confirming the static assumptions of particular forms of capitalism to which Member States belong,
- Intrusion and substitution: self-sufficiency might succeed, if at all, in regulated markets (energy, telecom, financial services), thereby overruling and out-ruling national private legal orders
- Hybridisation: remedies in consumer, anti-discrimination, private competition, state aids, public procurement might be developed out of European regulatory private law and national private law, thereby leading to a truly integrated legal device,
- Convergence: co-regulation in risk regulation and standardisation of services, self-regulation in those areas where party autonomy/freedom of contract/autonomie de la volonté still prevails, thereby maintaining the specificities of the European and the national legal orders, but bringing them more closely together.

The four normative models linked to subjects, countries, working hypotheses and projects

The chart provides for an overview of the intended research. It indicates the subject matters where the research will be located, highlights the countries which have —tentatively— to be taken into consideration, spells out the dominant working hypotheses and concretises the research projects. It likewise identifies not only the concrete topics on which the project is now focussing but also attributes the different projects to those collaborators who are working on the respective issues.

	Subjects – institutional design	*Countries – institutional design*	*Emphasis – dominance - relevance*	*Research projects – innovative and paradigmatic*
Conflict + verbitzance of MPL against ERPL	Consumer Anti-discrimination Unfair commercial practices Private competition state aids, public procurement	Defence of freedom : UK and new MSt. Defence of justice: D, F, Nordic countries	Testing clash of values bfc (consumer, anti-discrimination) bfb access for SME's and consumers	1 project: on social and economic discrimination (undertaken by H. W. Micklitz and G. Comparato)
Intervalism + substitution of ERPL du MPL	Regulated markets Energy Telecom and postal services Transport Financial services Universal services	More likely a rather homogeneous approach in all Member States Conflict and resistance stronger in Nordic countries, France and Italy	Testing self sufficiency bfc bfb	1 project: on regulated markets (telecommunication) by Marta Cantero 1 project: cutting across regulated markets (Yane Svetiev)
Hybridisation (ERPL + MPL mutually complementary tools and remedies)	ERPL to a varying degree	More likely in homogeneous legal orders and fully substituted national orders	Testing hybrid remedies	1 project: on remedies cutting across the different ERPL
Convergence (approximation of ERPL and MPL)	Risk regulation Standardisation of services Self-Regulation	More likely in old MSt. with consistent legal order Self-Regulation more likely in UK and new Member States	Testing CoR in risk regulation or standardisation Self-Regulation in autonomy guided areas	1 project: on standardisation of services (Rowena van Leeuwen)

Four research projects, suggested countries, co-operation partners and research profiles

The research projects must be paradigmatic in that they reflect the theoretical concept of European regulatory private law (the three layers: the self-sufficient sectoral market orders, the general principles and the common principles of civil law) and innovative in that they enter into new fields of private law research. Co-operation partners will be needed in the selected countries.

- 1 project on social and economic discrimination, building on 'Politics of Judicial-Co-operation', lays down the theoretical ground for the suggested new understanding of ERPL. The major objective would be to test the hypothesis of conflict and resistance in countries with a liberal economy (UK), a strong social-welfare market economy (Nordic countries, Germany) and in countries to be located in the middle ground (France, Italy). The innovative potential lies in the combination of social and economic discrimination. The intention is to define the new order of values, which is said to govern European regulatory private law, thereby cutting across the different areas of European regulatory private law. Since this sub-project lies at the heart of my own research on access justice (Zugangsgerechtigkeit), I will execute it myself. Guido Comparato, who defended his phd on 'Nationalism in private law' is focussing on the paradigm of inclusion/exclusion thereby complementing the access justice dimension.

-1 projects on regulated markets, building on 'Kundenschutz auf liberalisierten Märkten'.[64] The major objective here would be to test the hypothesis of self-sufficiency of the emerging European private legal order. One will focus on the telecommunication sector (Marta Cantero). The other cuts across the different sector related rules and covers the following countries: United Kingdom and Sweden (administrative governance), France and Italy (political governance), Germany (judicial governance). It is executed by Yane Svetiev who combines deep knowledge of regulated markets with behavioural economics.

- 1 project on remedies in European regulatory private law to test the reach of hybridisation, cutting across judicial, administrative and political

[64] J. Keßler/H.-W. Micklitz, Kundenschutz auf den liberalisierten Märkten —Vergleich der Konzepte, Maßnahmen und Wirkungen in Europa— Energie, VIEW Schriftenreihe, Band 23, 2008; J. Keßler/H.-W. Micklitz, Kundenschutz auf den liberalisierten Märkten – Vergleich der Konzepte, Maßnahmen und Wirkungen in Europa –Personenverkehr/Eisenbahn, VIEW Schriftenreihe, Band 24, 2008; J. Keßler/H.-W. Micklitz, Kundenschutz auf den liberalisierten Märkten Vergleich der Konzepte, Maßnahmen und Wirkungen in Europa – Telekommunikation, VIEW Schriftenreihe, Band 25, 2008.

enforcement/governance and encompassing individual as well as collective enforcement, building on 'New Frontiers in Consumer Protection'[65] and 'Das Verbandsklagerecht in der Informationsgesellschaft'.[66] The role and function of remedies in a complementary institutional design that brings together judicial, political and administrative enforcement is underresearched. The countries to be investigated will be selected along the lines of the different enforcement/government structures, UK, NL, Nordic countries, Germany, Italy or France. It is executed by Betül Kas.

- 1 project on co/self-regulation in the field of standardisation of services, testing the convergence hypothesis, building on 'Internationales Produktsicherheitsrecht' and 'Service Standards: Defining the Core Elements'. Co/self-regulation in the field of services is still a black box. The project allows for the investigation of SME's which are mostly concerned. Previous research on liability of services provides for a promising base.[67] Outside and beyond the UK, Germany, France or Italy as well as Nordic countries, particular emphasis will be put on the new Member States since old Member States are very much concerned by cross-border services affecting their legal orders. The project is executed by Barend van Leuwen.

Research methodology

The starting point for the analysis of the four projects results from classical legal methodology, with particular emphasis on European law and comparative private law. Secondly, the four projects bear a strong factual (sociolegal) dimension rooted in the combination of legal theory and institutional economics. The making of the law, the choice of the instrument and the application/enforcement of these rules have to be carefully reconstructed. This can only be successfully completed when key actors are interviewed, avoiding sole reliance on written documents. Qualitative research produces outcomes that allow for meeting the generalising approach of legal research to be applied to society as a whole. This entails the selection of one appropriate rule, measure or decision/judgment, one which ideally reflects the whole policy enshrined in the selected field of research from cradle to grave,

[65] F. Cafaggi/H.-W. Micklitz (eds.), New Frontiers of Consumer Protection – the Interplay be-tween Private and Public Enforcement, Elgar, 2009.

[66] H.-W. Micklitz/ A. Stadler (authors and editors, Das Verbandsklagerecht in der Informations- und Dienstleistungsgesellschaft, 2005, Landwirtschaftsverlag Münster.

[67] U. Magnus/H.-W. Micklitz, Liability of the Safety for Services, VIEW Schriftenreihe, Band 21, 2006.

and then to carefully reconstruct that particular rule/measure/decision/judgment. I have successfully applied such a research method in 'Politics of Judicial Co-operation'.[68] In the project I will co-operate with Th. Roethe with whom I have developed this particular approach.[69]

Reconstruction in essence means that the material has to be as complete as possible, including the rule/measure/decision/judgment and the comments of academics, in order to define the arguments of the parties and to give shape to the role of the key actors (public officials in agencies, judges in courts). Reconstruction is a term borrowed from qualitative sociological methodology. The term refers to more than a mere compilation of empirical data, it seeks to decipher the structure of meaning in the ongoing process of argumentation which shapes the case at issue. This type of socio-legal analysis includes the interpretation of laws, documents, interviews with the parties concerned and the results of discourse and bargaining processes.

(3) Step 3 - A private law theory built on the functional turn from autonomy to regulation and competition: The findings of the four projects constitute the *first building block* in my intention to develop a normative model which suggests the emergence of a new private legal order. The sub-project on conflicting values is genuinely *horizontal*. It establishes the foundation on which the transformation process is based to varying degrees and in various forms as spelt out in the other three *vertical* sub-projects, the one on regulated markets, the one on remedies and the one on co/self-regulation of services. In this sense, the first premise of the suggested transformation process would have to be met.

What remains is the *second building block*, the merging together of the study on conflicting values with the other three sub-projects in order to discover whether the European transformation process, analysed in light of the four normative models conflicting values, intrusion and substitution, hybridisation and convergence, is guided by a common philosophy and a common set of values and principles enshrining competition and regulation and allowing for the understanding of private law as a coherent system or whether European regulatory private law can only be understood in its market related context, as a polycentric order, paying tribute to the many constitutions and the many private legal orders of Europe, thereby undermining any idea of the unity of private law.

[68] The Politics of Judicial Co-operation in the EU – the Case of Sunday trading, Equal Treat-ment and Good Faith, 2005, Cambridge University Press.

[69] H.-W. Micklitz/Th. Roethe/St. Weatherill (eds.), Federalism and Responsibility – A study on Product Safety Law and Practice in the European Community, Graham & Trotmann, London, 1994.

Therefore the second building block aims at a new orientation of the structures and methods of European private law, based on its transformation from autonomy to functionalism in competition and regulation. *Therefore* the second building block is meant to reconsider and redefine the role and function of national private legal orders which varies according to the respective market order. *Therefore* the second building block intends to develop a multi–level vertically and horizontally integrated model which defines the role and function of national private legal orders that enshrine different values and one which takes into account the process of Europeanisation in the legislature, academia, and civil society (*Maduro*).[70] *Therefore* the objective of the research project as a whole is the development of a flexible co-ordination system of European regulatory private law and national private law as well as its theoretical implications. *Therefore* it entails a theoretical dimension which refers back to the sensitive relationship between economisation of private law via the Internal Market Programme and politicisation of private law via governance. It allows me to contribute not only to the development of a private legal theory but also to the constitutional dimension of the European integration process.

First horizontal block: conflict and resistance: new order of values, enshrined in the concept of access justice (zugangsgerechtigkeit)
Various sub projects on regulated markets, on remedies and on standardisation of services
Second horizontal building block: new–orientation of the structures and methods of european private law, based on its transformation from autonomy to functionalism in competition and regulation

[70] P. Maduro, 'Interpreting European Law: Judicial Adjudication in a Context of Constitutional Pluralism', European Journal of Legal Studies, No. 1, Issue 2, 2007.

HARMONIZATION OF LAWS AND COMMERCIAL PROCEDURAL DEVELOPMENTS IN TIME OF ECONOMIC CRISIS

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SUMMARY: *General*. I. *Concepts of Procedural Law*. II. *The Standard Legal Procedural*. III. *Concepts of Action, Pretension and Demand*. IV. *The Commercial Processes in the Mexican Legislation*.

GENERAL

On the occasion of the sixteenth: meeting of the International Academy of law and protection to the consumer to be held in the distinguished faculty of law of the Universidad Nacional Autónoma de México, in which there is skilful coordination of the Dr. in law and emeritus teacher Elvia Arcelia Quintana Adriano, how difficult is to expose on short pages the harmonization of laws and its procedural developments in the commercial area in the historical moment in which we live, stressing the need of orality and immediacy in the business processes, which will start with a concept of procedural law, namely:

I. CONCEPTS OF PROCEDURAL LAW

The Procedural Law Must be located as a science and as positive law, and this may be formulating a concept of mercantile law, such as starting-point of the present investigation.

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The Procedural law is conceived like a science, due to the fact that it is conformed by a set of truths in a unified systematized form, of which it derives that in the ambience of the Procedural law, this one arises like a set of truths and juridical doctrines, which study of object, it is the jurisdictional function.

The procedural law is closely linked to the positive law, or the set of legal rules concerning the jurisdictional process. Highlighting the essential notes of the legal and procedural standards, among others, the following:

They Perform public order, by virtue in which they regulate a function of the State and because they take that as a final purpose the administration of justice to achieve social peace.

They are of impositive character, without allowing its non-observance permitting agreement between the parts, but only in cases authorized by them.

They are adjective in determining the form of procedural acts, however, in some occasions we found assumptions that belong to the substantive law and to the subjective law.

They are autonomous, by virtue that the rights and obligations that from them arise, are not subordinated to the exercise of the action to suit in the procedural act.

In a collateral way we have to study the so-called fundamental concepts applicable to the Procedural Law, for which, I appeal to the thinking of Mr. Eduardo Pallares, who stated:

> Both the rules of positive procedural law, such as the doctrines and the jurisprudence that are interpretated and applied lay in the following fundamental concepts:
>
> 1. Legal Relationship. All relationship existing between human beings with legal importance.
>
> 2. Interest. The relationship that exists between a person and something that can satisfy their needs.
>
> 3. Subjective Law. Faculty that the law grants to a person to demand the other one what he should do or stop doing something.
>
> 4. Power. Legal possibility, granted by the norm to a person to command others to perform or refrain from doing something. (Subjective Law jurisdictional authorities) can be seen a domain on the other´s will.
>
> 5. Litigation. Conflict of interest with legal implications, which is manifested by the claim of one of the parties concerned and the resistance of the other.
>
> 6. Obligation. Link of rights that compels the will of the persons to do or not do anything. The link is imposed by the law for the sake of the holder ó incumbent in the fulfillment of the obligation.
>
> 7. Substantive Law and Adjective Law. The first one determines the rights and obligations of the persons. While the adjective conforms the juridical acts and the judicial procedures.

8. Objective Law. Linking it to the set of juridical norms properly ordered (it is understood by juridical norm the rule of conduct and mandate, imposed by legitimate authority, in order to obtain the social peace inside the justice).

9. Mandate. Identifying himself as the act by which the power is exercised (jurisdictional authority) or to impose their will to the others.

10. Faculty. Possibility to work in the field of freedom, (contrary to the term of obligation, meaning that men acts as he wants when it comes to the faculty, and duty when it comes to obligation).

11. Subjection. Is the state in which there is a person with respect to another that exercises power over it and by virtue of which you must obey the law.

12. Freedom (Jurisdictional Body). The state against the subjection and also to the obligation.

13. Free Power and Linked Power. I understand under the concept of Free Power when the holder can exercise it or not according to his will, independently that remains like a powered and obligatory link. In the sense of the use of him in the form and terms that the law determines.[1]

Of the previous reflections it is clear that, the procedural law has the character of a linked science, with a Positive law, and fundamental concepts that allows to define in the following way:

It is a right of technical - juridical content, in which it is established a jurisdictional function, a procedure that must be fulfilled by the persons whom it is directed, as well as to the institutions that must fulfill it.

In such a virtue, a concept of Procedural Commercial Law would remain integrated in the following way:

Right of technical - juridical content, in which a jurisdictional function is established, with the procedure that must be fulfilled, deciding controversies between merchants or between not business-minded persons, who practice or perform acts and operations that the law recognizes like Commercial.

II. The Procedural Juridical Norm

1. *Concept of Procedural Juridical Norm*

Previous to the study of the interpretation and integration of the Procedural Juridical Norm, it is necessary to understand the concepts of Juridical Norm, and to the effect, following the lineaments of Mr. Rafael Preciado Hernández it is indicated:

[1] Pallares, Eduardo, *Apuntes de derecho procesal civil*, 2a. ed., México, Editoral Botas, 1964, pp. 16-21.

> Norm in a generic sense is the obligatory rule, or the rule that prescribes a duty. Any norm is, consequently a rule for next genre, and the prescription of a duty for its specific difference.[2]

Within the world of the law, it is considered that the juridical norm is the expression of the Law itself. As a consequence juridical norms prescribe what the members of a society or community should do for the common good through a rightful social order.

For Mr. Rafael Preciado Hernández means "establishing that this is a fully human order".[3]

The previous ideas allow establishing that the procedural juridical norm is, that juridical norm that establishes a coordination of the human actions directed to the achievement of justice and the common good, by conduit of a jurisdictional organ previously established.

2. *Interpretation of the Procedural Juridical Norm*

In any juridical norm it is not perfection with which it is written, or the clarity of its concepts which automatically creates its positive application; the casuistry in which it may fall, the rapidity with which it has been processed or drafted a norm and its validity in a historic moment, impose the necessity of being interpretated, purifying the materiality of their provisions with the spirit that integrates with the system or to which it belongs.

To the effect Mr. Joaquín Escriche indicates as interpretation of the Law the following:

> The convenient clarification of the text and spirit of the law to know the true meaning that the legislature intended to give in other way the straightest and most fruitfulness understanding of the law according to the letter and the reason.[4]

In the same way Ludwing Enneccerus, in his Civil Rights Treaty defines the interpretation of the juridical norm in the following terms:

> …Clarify its sense and precisely that sense which is decisive for the law, and therefore also for judicial resolution. Such clarification is also conceivable to

[2] Preciado Hernández, Rafael, *Lecciones de filosofía del derecho*, México, UNAM, 1984, pp. 73 y 74.

[3] *Ibidem*, pp. 98 y 99.

[4] Escriche, Joaquín, *Diccionario razonado de legislación y jurisprudencia con suplemento*, España, 1873.

> the Constitudinary Law, deducing its true sense of acts of use, the testimonies and the usus fori recognized continuous v. But the main object of the interpretation form it the laws.[5]

Out of the previous thoughts it is shown that, interpretation applies: to unravel the content of an expression, in consequence, the expression would inplied the specification of a thing to give to understand, from that perspective, the role of interpreting will usher in the analysis of the elements that integrate the expression.

Mr. Eduardo García Máynez quoting Edmundo Husserl indicates, as an element of an expression the following:

> a. The Expression in its physical aspect (the sensitive sign, the sound joint in the spoken language, the signs written on the paper etcetera.).
>
> b. The Significance. What the expression means in the sense of it all. I consider that it is the language that exists between the expression and the meaningful object.
>
> c. The object (several expressions can have the same significance but different objects".[6]

The items above, are not always related or interconnected between them, Putting our interest for the purposes of this research the second element, relative to the significance of the interpreted object, for say the norm that the text expresses in a case previously interpretated.

I believe that the interpretation of the law aims to find out its meaning, in its subjective and objective and progressive content.

To the subjective, objective and progressive contents, I give them the following connotations:

> a) *Subjective.* In accordance with the spirit and proper sense of the norm, which in this case the gives to the legislator.
>
> b) *Objective*. because it must be interpreted in relation to other laws, that constitute the legal system in a given State or Nation; and
>
> c) *Progressive*. By virtue of the fact that an old law must give up or leave the place to a new trend, in accordance with the historical moment in which we live.

[5] Enneccerus, Ludwing, *Tratado de derecho civil, Barcelona*, Boch, parte general, vol. 1, p. 202.

[6] García Máynez, Eduardo, *Introducción al estudio del derecho*, cita a Edmundo Husserl, 4a. ed., México, Porrúa, 1958. pp. 315 y 316.

There are different kinds of interpretation, we will continue the classification that stated don Eduardo Pallares:

a. By the method that is used to determine the meaning of the Law; There have been classified them in:

— Grammatical. The one that is founded in a main way on the sense of the letter of the law.
— Judaic. It is the grammatical carried away until it´s finally ends with an exaggerated respect of the text.
— Logic. Which is sometimes identified with the scientific, is the one that gives more importance to the concepts and doctrines contained in the law, than the grammatical sense.
— Systematic. interprets the various articles of the law, treating them as an integral part of a whole (of the law or the code that are a part of) and the same law as a constituent element of the right of a given country. This interpretation is performed by matching a few precepts with others, and seeking to discover the principle that gives them organic unity.
— Historical. Seeks to discover the meaning of the law, taking into account the historical precedents that determined its function (preparatory work of the legislators, the speeches of processing etcetera).
— Historical Progressive. Is based on a conception of the law diverse to the previous one, the meaning of the law is not immutable, and the interpreter must take account of these changes, to discover the meaning in the era in which the interpretation is performed, not the one he had when it was created.
— Scientific. Doctrine of the jurisprudents and the principles of the science of the law.
— Theological. It is carried out bearing in mind the social one followed by the legislator who has ictated the norms (it can be convined with the other species of interpretation or be a part of them).
— Abnormal. Takes place when the laws are defective, because they employ particular words or improper, contain antinomies or lead to absurd results (the antinomy understood as a contradiction between two precepts of a same law or between two or more laws of the same date, declared in force.

b. By the person or authority who originates

— Authentic is the one that makes the own legislator.
— Judicial. Which are carried out by the courts.
— Doctrinal. The one that the Jurists realize.

c. By the effects it produces in the application of the law.

— Extensive. When its effect is to expand the meaning of the law, that is, to apply it to cases not covered by it.
— The restrictive. Its application limited to cases provided for by law.

— Derogative. To Modify the sense of the Law.
— Analogical. Implying that when the same reason happens, the same disposition of the law must meet also, in my opinion it allows me to establish the particular thing one will be allowed to establish that the analogical ambience is not part of the interpretation and its real application is inside the integration of the procedural norm.
— Finally we have the simply declarative that state, without extending, nor restricting and less modifying'.[7]

3. *Integration of the Procedural Norm*

In the field of legal life happens that, in some cases the judge to resolve a specific case, founds that there is no applicable disposition, and as an in consequence he will need to use or go to other sources of the law as the custom, usage, the general principles of law, with which he was allegedly 'filling the gap' of the law.

In principle should be that there is no vacuum rinsing or loophole in the law as the law itself, but rather comes to emerge in the law, and as a consequence when the judge do not find precept to interpretate goes to some integratory activities given by the law, of which one must conclude, that when dispenses with the applicability of the norm, we are dealing with the integratory investigation of the law.

I will follow Mr. Eduardo García Máynez on having studied the integration methods:

a. *Analogy*. "Consists in applying to a case not provided the provision concerning a situation envisaged, when between this and that there are similarities and there is the same legal reason to resolve it in the same way, proving beyond doubt that such a procedure is outside the scope of the interpretative work, since there is only interpretation when there is a precept which this task can refer".[8]

As a consequence, the analogy as a method of integration of the Law, attributed to situations partially identical (one planned and another not foreseen by the law), the legal consequences that points out the rule applicable to the case.

I think that when the analogy emerges a new norm is born, whose so- called expressed in abstract the characteristics of the case that was not planned, but between one and another only arose a partial identity.

[7] Pallares, Eduardo, *La interpretación de la ley procesal y la doctrina de la reconvención*, México, Editorial Botas, 1948, pp. 26-28.

[8] García Máynez, Eduardo, *op. cit.*, p. 356.

In this virtue, it should not be used the concept of analog implementation of a legal rule to a case not provided, but to the creation or analog formulation a new norm.

b. *General Principles of Law*. Continuing with the lineaments that sets Mr. Eduardo Garcia Maynez he states:

> "*It has been identified as the just and natural law stating that natural law is one that in the absence of a provision formally valid, the judge must formulate a principle with inherent validity, in order to resolve the specific issue subject to their knowledge.*
>
> *Therefore it is excluded from the legal possibility of the judge to rule in accordance with his personal views*".[9]

We must understand that the general principles of law will arise to resolve an unexpected issue, assigning the judge the quality of legislator, because it will fail the point in dispute as the legislator would have done so, to have been able to hear the case under its jurisdiction.

c. *Equity*. Quouting Aristóteles, Mr. Eduardo García Máynez establshes:

> "*The Equity has the function of a legal corrective. It is a remedy that the judge applies to remedy the defects arising from the generality of the law. Laws are in essence, general and abstract enunciates*".[10]

On this basis, it appears that the equity has its own autonomy, regardless of being part of the General Principles of Law, it really is the first principle or the supreme, because it serves as the base to the others.

4. *Foundation of the interpretation and integration of the legal Norm in the Mexican Law*

This point by itself would be grounds for a long study, any time that is related to the constitutional guarantees, and in particular with the fundamental principles in any legal proceedings, as would be the guarantee of a hearing and the principle of legality, limiting the study to see whether our Constitution regulates both the interpretation as to the integration.

In this order of ideas comes to transcribe the article 14 of the Constitution and the program will then brief comments to the effect.

Article 14. To no law shall be given retroactive effect to the detriment of any person.

9 *Idem*.

10 *Idem*.

> "…No one may be deprived of life, liberty, or of their property, possessions or rights, but through trial followed before the previously established courts, in which the formalities are completed essential of the procedure and in accordance with the laws issued prior to the fact.
>
> In the criminal trials is hereby prohibited to impose, by simple analogy and even by a majority of reason, any penalty that was not decreed by law exactly applicable to the offense in question.
>
> In the civil trials, the final sentence shall be in accordance with the letter, or the interpretation of the law and the lack of this will be based on the General principles of law..."

In the study of article 14 of the Constitution, it is clear that the solutions or resolutions to disputes arising between the parties, should be with basis of laws issued prior to the fact.

Similarly, it is appreciated, in the third paragraph of the precept in study, the law is the only source of the criminal law or that the criminal law lacks gaps. Hence, it is prohibited the implementation of penalty by simple analogy and even by a majority of reason.

The criminal law should be applied literally; but that does not mean it cannot be interpretated, because the legal legislation is an expression of the law and that only prohibits the integration in the criminal law, as it is by definition lacking gaps.

But I have to conclude by noting that, within the judicial discretion, it is given a certain margin of freedom to the judge, that within their own legal norm, apply the appropriate penalty, on the basis of special circumstances that may arise in any delincual act.

With regard to the fourth paragraph of article 14 of the Constitution, can be seen as a primary criteria the obligation to submit to the text of the law, and consequently that the judge has to resolve in accordance with the law, when it is expected the controversial legal situation.

If the meaning of the law may generate doubt, the own article 14 of the constitution authorizes that emerges the figure of the legal interpretation, looking for the meaning of the law that are not necessarily identified with the will of the legislator, but preventing if the interpretative work reveals the judge mercantil the case submitted to it for its solution is not foreseen in the norm of law, has the obligation to fill the so-called 'lagoon', thus resulting in the course of integration.

The legal corrective value which is attributed to the figure of the interpretation is correct, since it is a remedy that the judge applies, in order to remedy defects arising from the generality of the law, but still inaccurate

that is suppletory of the norm, any time that the judge applies the equity once more becomes legislator, and in this sense his acts generating his own concept and applicable to the case in dispute.

In the field of Commercial Law it is set in article 1st. Of the Commercial Code that its provisions are applicable to commercial acts, which the absence of provisions, shall apply to the acts of trade the Federal Civil legislation.

In the commercial procedural ambience it is regulated in the articles 1054 and 1063 of the Commercial Code, with the quality of supplementary legislation, the Federal Code of Civil Procedures, with the provision that in case of nonexistence or shortcoming in the regulation, one will refer to the local Code of Civil Procedures.

III. Concepts of action, pretension and demand

It is important to make the distinction between action, pretension and demand, as they are usually used as synonyms, causing distortions in the application of the Juridical Norm.

1. *The action*

The action has multiple meanings within the legal literature, taking a remote origin, since it existed in Rome since primitive times.

In the Roman Law arise three periods: the case of the actions of the law, the formulary system and the so-called extraordinary procedure.

The actions of the law were identified in five, as follows:

- Action by Sacrament was considered the oldest, and served to enforce real and personal rights.
- The judicis postulatio that was intended, to obtain from the magistrate the promulgation of a judge.
- The conditio which was seen as, the proper procedure and special to exercise personal rights.
- The manus injectio in wich we look for the seizure or apprehension of the person of the debtor, to compel him to enforce a judgment, pay off a debt confessed, or to force him to appear before the judge.
- The pignoris capio corresponded to an enforcement procedure or way of compulsion.

In this first phase called of actions of the law, it is a procedure and not a right; with a series of acts, formulas and solemn pantomimes without which was not possible to obtain justice.

Such actions of the Law are valid since the origin of Rome until the promulgation of the Aebutia Law in years 577 or 583 BC.

Formulary system

Begins with the Aebutia Law and it reaches up to the year 294 BC. At the time of Dioclesiano.

Mr. Eduardo Pallares pointed out that the formulary procedure form had been as main characters the following:

> …The parties were not obliged, when presenting their pretensions, to use certain sacramental phrases, nor to perform pantomimes of any kind as in the previous system. They employed the vulgar language.
>
> As a general rule there is a distintion in this system between the two different periods: the first, before the magistrate, it was called 'in-jure', the second, before the judge or the jury, had the name of 'in-judicium'.
>
> In the first period it was formulated the litis. The actor expressed its demand and the convict his answer. The two parties asked the magistrate the appointment of a judge or a jury to decide the dispute.
>
> The 'in-jure' procedure was concluded with the most important part of it, which consisted in the magistrate giving the actor the formula (action).[11]

Extraordinary Procedure

In this phase the pretor did not send the parts before the judge so that he could decide the litigation, He, himself had to resolve.

Within this phase, it is given Celso´s definition: "reclaim what belongs to us".

We note the strong influence of Roman Law until our days, establishing the following concept of action: 'The right to pursue in trial as to what is due to us or what belongs to us'.

The previous allows appreciating:

- It is considered the action as the right of the actor against the defendant and not to a legal faculty to put in action the judicial body.
- Linked to the subjective right that is asserted in court, failing which, the action is declared inadmissible;
- Procedural actions that existed since that epoch in the substantive scope were disregarded which determined rights and obligations that arise from contracts and the quasi-contracts.

[11] Pallares, Eduardo, *Apuntes de derecho procesal civil*, *cit*. pp. 42-44.

The foregoing, allows to establish that "The Action" was conceived as private law.

There have appeared other legal institutions, such as "The Procedural Action", which we will study at this point.

Giuseppe Chiovenda understands the procedural action such as:

> The legal power of convert in unconditional the will of the law with respect to its performance or, in other words, the legal power to make the condition for the action of the will of the law.[12]

Ugo Rocco believes that the right of action can be understood as follows:

> *The right to seek the intervention of the State and the provision of jurisdictional activity, for the statement of certainty or the realization of the coercive interests (material or procedural) protected in the abstract by the standards of objective law*.[13]

Eduardo J. Couture points out that the procedural action arises under three different meanings:

> a) As a synonym of the Law. In the sense of the word when it says 'the actor lacks action', or it is asserted the "exceptio actione agit", which means that the actor does not have an effective right that the trial must safeguard.
>
> b) As a synonym of pretension. This is the more usual sense of the word, in doctrine and in legislation; it is found frequently in the legal texts of the nineteenth century that maintain their force, even in our days; Then we speaks of 'civil action and criminal action', of triumphant 'action and discarded action'. In these words the action is a pretension that you have a valid right and on behalf of which one promotes the respective demand. In a way, the meaning of the action, such as pretension, is projected toward the demand in a substantial sense and could be used interchangeably by saying 'demand founded or unfounded', demand (of guardianship) of a legal or personal right', etcetera. If, we say, the usual language of the forum and of the school in many countries.
>
> c) As a synonym of faculty to provoke the activity of the jurisdiction. It is said, then, of a legal power that has every individual, and on behalf of which it is possible to go before the judges in request for the defence on fundamental Constitutional rights or it´s pretension; the fact that this pretension is founded

[12] Chiovenda, Giuseppe, *Ensayos de derecho procesal civil*, trad. de Santiago Sentis Melendo, Buenos Aires, Ediciones Jurídicas Europa-América Bosch y Compañía, 1949, t. I, pp. 6 y 7.

[13] Rocco, Ugo, *Tratado de derecho procesal civil*, 2a. reimpresión inalterada, trad. de Santiago Sentis Melendo y Mariano Ayerra Redin, Buenos Aires, Editorial, Temis-Bogotá, Palma-Buenos Aires, 1983, t. I., p. 272.

> or unfounded does not affect the nature of the power to actionate; they can promote their actions in justice even those deemed mistakenly assisted of reason.[14]

Enrico Redenti brings the notions expressed by Eduardo Couture, in the following form:

> With the action (Procedural activity) it is proposed to the judge the action (pretension), and he will tell if there is an action (right).[15]

Out of the concepts exposed, when making a comparison with the Roman system they distinguish the following elements:

- The action as an institution of public law;
- It is incorrect identify the action with the right that seeks to have the actor while formulating his demand;
- It is an independent right, of the litigation rights that the parties are looking to enforce;
- It is irregular to think about the existence of several procedural actions any time that there is only a general and abstract (implementation of an autonomous right to the exercise a pretension that implies the jurisdictional activity);
- The passive subject of the action will never be the defendant but the judicial authority, without fail to note that on the defendant, may have the effects of the action;
- Finally, I consider the procedural action as an institution of public character that emerges from a constitutional sphere, in which, it is pointed out; that no person may do justice by themselves nor to exercise violence to claim their right, due to the fact that they have the power and duty to go to the courts, where justice will be administered by applying the judicial norm that corresponds to the general law and abstract that follows.

2. *The Pretension*

Mr. Carlos Ramírez Arcila quotes Francesco Carnelutti stating:

> *The pretension is a requirement of the subordination of one foreign interests to another own.*[16]

[14] Couture, Eduardo J., *Fundamentos de derecho procesal civil*, 2a. ed., Buenos Aires, Palma, 1951, pp. 9 y 10.

[15] Redenti, Enrico, *Derecho procesal civil*, Buenos Aires, Ejea, 1957, p. 52.

[16] Ramírez Arcila, Carlos, *Teoría de la acción*, Bogotá, Temis, 1969, p. 19.

Out of the exposed concept, It is simple to appreciate the existence of a legal act that identifies with the statement of will, by virtue of which it is claimed the title of an abstract right and material that is contained within the demand. Without involving that if it is not credited in the field of law and in the material law tue pretension may not exist of justice not be credited to the right material the claim does not exist, but only that dismisses the same and perhaps it may not have been credited.

Carlos Ramirez Arcila interprets the concept pretension in simple and logical manner, transcribing these reflections:

> Carnelutti teaches us that the pretension is an act, not a power; something that someone does, not that someone owns; a manifestation not a superiority of will. Not only the pretension is an act and, therefore, a manifestation of the will, but one of those acts that are called statements of will.
>
> Such act —adds Carnelutti— "not only is, but that not even implies the right (subjective); the pretension may be proposed by both who has as by who does not have the law claims necessarily the pretension, since there can be pretension without law; to the side of the unfounded claim we have, as a phenomenon, the inert law".[17]

The pretension can tend to the subordination of the foreign interest to of the one who makes her suit, and being able to be satisfied by extrajudicial or judiciall way; but departing from a consistent reality in which there are pretensions without law and law without pretension. The previous thought leads us to conclude that, the existence or nonexistence of the law that the actor tries to exercise normally, only turns out to be crystallized, at the moment when the judge emits a favorable judgment.

3. *The demand (Claim)*

At this point I will only address the Demand in the doctrinal field of procedural law, in the following way:

On having studied inside the Mexican Juridical Dictionary the concept, José Ovalle Favela demands indicates:

> It comes from the latin demandare, which had a different meaning to the present: 'trust',To 'make good insurance', 'forward'.
>
> The demand is the procedural act by which a person, that is constituted by himselve in actor or demandant, makes a claim by expressing the cause or

[17] *Idem*.

causes as he try to be based to the jurisdictional body, and with which initiates a process and requests a ruling in favor of his claim.[18]

Eduardo J. Couture defines:

The demand is an introductory Procedural Act by virtue of which the actor submits its claim to the judge, with the forms required by the law, calling for a favorable judgment to his interest. Document in which the actor communicates its pretension to the judge, with the forms required by the law, asking for a judgment in favor of his interest.[19]

Cipriano Gómez Lara understands the demand in the following way:

The first act of the exercise of the action, through which the pretensor goes before the courts pursuing that their pretension is satisfied.[20]

Rafael de Pina y Rafael de Pina Vara pont-out:

Demand. The verbal procedural act or ordinarily initial document of the process in which Is brought before a judge a matter (or several if not mutually exclusive) to resolve, prior to the established legal procedures, issuing the judgment that is appropriate, as alleged or proven.[21]

Indeed, the demand is a procedural act that indicates the beginning of an instance, trough which the actor submits his pretension before a competent judicial authority, seeking a judicial determination that is favorable to hisinterests.

IV. The Commercial Processes in the Mexican Legislation

Commercial proceedings are the ones which seek to ventilate and decide disputes arising from commercial acts.

The act of commerce should be understood as an event that produces juridical effects by means of display of the will, in which the parts normally delimit its effects and that they link with the production and in its case, with the exchange of goods and of services destined for the market in general.

[18] Ovalle Favela, José, Voz "Demanda", *Diccionario Jurídico Mexicano*, 4a. ed., México, Porrúa, Instituto de Investigaciones Jurídicas, 1991, p. 889.

[19] Gómez Lara, Cipriano, *Derecho procesal vivil*, México, Trillas, 1984, p. 32.

[20] *Idem*.

[21] De Pina, Rafael y Rafael de Pina Vara, *Diccionario de derecho*, 15a. ed., México, Editorial Porrúa, 1988, p. 212.

Commercial proceedings are classified into Ordinary, Summary, (Special) and Oral.

1. With the quality of ordinary commercial proceedings, it must be understood that procedural processing that instructed and vent in writing, supplying to the parties the widest opportunity to defend their rights and to produce the proof in them, in search of the truth of the facts, by issuing a vinculative judicial decision to the parties.

2. Summary Commercial Proceeding, arises from a document in which it is represented by certainty a liquid right, exigible, determinated or determinable of complete term: legitimizing its holder against the defaulter, to demand judicially the fulfillment of an obligation recorded in the title or document, by means of execution, that is to say, that after the demand has been admitted is ordained a payment request, if it is not obtained, seizure of property, in which case it will be left in deposit of the person who for such an effect indicates the one that exercises the pretension and done the previous thing, one proceeds to the emplacement of the debtor or defendant.

3. Oral Commercial Proceeding, attending on the prevailing social reality in our country, it is known that the juridical safety in the procedural procedure, allows every person to have the right to get the administration of justice from courts that are speedy to give it in the period and terms that fix the laws, allowing that to be emitted resolutions in a prompt, finished and impartial way.

To this effect it has been considered by the Mexican legislature, that through the Oral Commercial Proceeding, compliance will be given to the principles of orality, publicity, equality, immediacy, contradiction, continuity and concentration, and lays down the following procedural stages:

Formulation of demand in writing, attaching evidence in which the actor justifies his pretension.

The Oral Commercial exteriorización Proceeding limits the competence of the judge to businesses whose amount is less than $500,000.00 M.N., with the caveat that it will not proceed the oral trial in case of summary proceedings, special trials or trials in which the amount is undetermined.

Admitted the demand, the emplacement is ordained so that the defendant produces the answer to the same one, formulates exceptions, offers means of proof and in its case make reprimand, all this in writing.

Fixed the litis with the demand, reply, in it´s case, counterclaim and reply to the counterclaim, arises the preliminary hearing in which we seek the debugging procedure with respect to the procedural exceptions, giving

the date a great significance to the alternative means of solution and settlements within which highlights the mediation and conciliation.

If not mediation or conciliation are obtained, purified the legal proceedings with regard to the exceptions, It will be resolved as pertaining to the admission or disregard means of proof, noting day and time for the hearing of trial.

At the trial hearing the means of proof are received orally, complying with the principle of immediacy and getting trough the means of conviction, the parties claim wthat law indicates, citing for judgment, which shall be given within the following 10 days.

Finally, it is important to note that in such legal proceedings, the ordinary resourses do not procede as it coudl be the case of the revocation and appeal.

It is important to mention that it has sought a harmonization of the laws within the evolution of Commercial proceedings, in times of economic crisis, looking for safety and legal certainty.

In Mexico the legislator has considered that within the figure of the "Orality" there is a complience with the principles of Orality, Publicity, Equality, Immediacy, Continuity and Concentration.

It is noted within the evolution of Commercial Proceedings the existence of a Preliminary Hearing in which there is procedural debug and then it is handled the alternative means of dispute resolution such as mediation and conciliation.

It continues to be part of the above Preliminary Hearing looking for the autonomy of the will of the parties, by means of agreements on undisputed facts and evidentiary agreements.

The cited Preliminary Hearing is concluded when the judge quialifies the different means of proof, in terms of their admission.

It should not go unnoticed that within this modernity that is sought to date the procedural processing is registered by electronic means, however, is duly to the judge to apply the electronic medium or use traditional means, in terms of article 1390 bis 26 of the Code of Commerce, and at this moment he would reflect which will allow the greater fidelity and integrity in the information to the Judge in order to issue a resolution according to the truth, identifying the event with reality.

Within the evolution of the Procidural Commercial Law in time of economic crisis, it is positive to comply with the Legislature's concern of the implementation of a Prompt and Expeditious Justice.

In addition to the above, the enforcement in the Hearing of the Trial when receiveving the means of proof truly complies with the principle of

immediacy however, it will be with the pass of time that efficiency of the regulatory system can be determined and if it did achieved its purpose, which is to deliver Justice in Prompt and expedited manner, generating with it legal security fot the parties in dispute.

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DELIVERY OF THE GOODS UNDER THE ROTTERDAM RULES: DEPARTURE FROM THE FUNDAMENTAL PRINCIPLES

Caslav PEJOVIC*

A new and important piece of legislation has been adopted under the auspices of the United Nations Commission on International Trade Law (UNCITRAL). On July 3, 2008 the UNCITRAL approved the Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea (the Rotterdam Rules).[1] This new UNCITRAL legislation has an ambitious goal to restore the uniformity of law governing the international carriage of goods by sea. Presently there are three international regimes governing the carriage of goods by sea: the Hague Rules,[2] the Hague-Visby Rules[3] and the Hamburg Rules.[4] If widely adopted, the Rotterdam Rules may be able to replace these three conventions and restore the uniformity of law.

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1 *http://www.uncitral.org/pdf/english/texts/transport/rotterdam_rules/09-85608_Ebook.pdf*.

2 International Convention for the Unification of Certain Rules of Law relating to Bills of Lading ('The Hague Rules') and Protocol of Signature, signed in Brussels on 25 August 1924 (entered into force on 2 June 1931).

3 Protocol to Amend the International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading, 1968.

4 United Nations Convention on the Carriage of Goods by Sea 'the Hamburg Rules'), signed in Hamburg on 31 March 1978 (entered into force on 1 November 1992), UN.Doc.A/Conf. 8915.

The Rotterdam Rules address a number of issues that have not been regulated by previous international conventions. There are completely new sections which cover the delivery of the goods and the right of control. The growing use of non-negotiable documents and documents in electronic form has drawn the attention of the legislators to these areas that previously had been ignored by all of the international conventions governing carriage of goods by sea. This innovative approach was probably motivated by the need to adjust the international regime governing carriage of goods by sea in such a way as cope with various modern developments, such as the increased importance of container transport, logistics and electronic commerce.

The ambitious and innovative approach of the Rotterdam Rules, which in some sections departs from certain well established principles, has drawn criticism from a number of scholars. A number of other scholars have, however, defended the text and offered various arguments to justify its novel approach. This paper will mainly focus on provisions related to the delivery of the goods, and particularly Article 47(2) which, as one of the most controversial provisions of the Rotterdam Rules, deserves the specific attention it will receive in this paper.

I. General principles related to delivery of the goods

All previous international conventions governing the carriage of goods by sea have failed to regulate the issue of delivery of the goods. Differences among national laws and different practices may have been the reason that this issue was left aside by the drafters of those conventions. At the moment, the rules on delivery of the goods are still based on domestic laws.

In maritime law, there is a well established rule that the carrier can deliver the goods at the destination only against the surrender of a bill of lading by the consignee. Once the master has issued the bill, the carrier has an independent, contractual obligation towards the bill of lading holder which derives from the nature of the bill of lading. Since the bill of lading is a negotiable document, its holder is entitled to require that the goods are delivered to him.

As long as the consignee can obtain a bill of lading before the goods arrive, there should be no problem for him to present it before delivery. However, in practice, for various reasons, it is often the case that the ship arrives at the port of destination before the consignee has obtained the bill of lading. In such situations, waiting for the bill of lading may cause numerous problems to all parties involved. In order to solve this problem, the practice of delivering the goods without the production of a bill of lading has been developed. This practice, however, may also cause a number of problems.

If the carrier delivers the goods without requiring the production of a bill of lading, he does so at his own risk. If the goods are delivered to a person who was not entitled to receive them, the carrier will be liable for breach of contract and for conversion of the goods.[5] In such cases the carrier may be deprived of the benefit of limitation of liability and may not be able to get indemnification from the P&I clubs.

There are some exceptions to the rule that the consignee must present the bill of lading before delivery. The carrier might deliver the goods without the production of a bill of lading if it is proven to his reasonable satisfaction both that the person demanding delivery was entitled to possession of the goods and that there was some reasonable explanation for what happened to the bill of lading.[6] Carriers should, however, be very cautious with respect to this exception.[7]

II. Legal background of the rules on delivery of the goods

The first issue that needs explanation relates to the rationale for the rule that the carrier must deliver the goods against the bill of lading. It seems that the reasons for such an obligation on the part of the carrier are sometimes not properly understood. Hence, in order to examine the issues related to the delivery of the goods against the surrender of the bill of lading, the reasons for this rule should be examined.

The first thing that needs to be addressed in this context is the nature of the bill of lading as a document of title, which is directly related to the issue of delivery of the goods.[8] In common law the bill of lading is characterized as a document of title, which means that the person in possession of it is entitled to receive, hold and dispose of the bill of lading and the goods it represents.[9] In civil law there are documents corresponding to documents of

[5] *Barclays Bank Ltd. V. Commissioners of Customs and Excise* [1963] 1 Lloyd's Rep. 81, *Sze Hai Tong Bank Ltd. V. Rambler Cycle Co. Ltd.* [1959] 2 Lloyd's Rep. 114. See also *Mobile Shipping Co. v. Shell Eastern Petroleum Ltd (The Mobile Courage)* [1987] Lloyd's rep. 655.

[6] *SA Sucre Export v. Northern River Shipping Ltd. (The Sormovskiy)* [1994] 2 Lloyd's Rep. 266.

[7] *Motis Exports v. Dampskibsellskabet AF 1912* [2000] 1 Lloyd's Rep. 121; affirming [1999] 1 Lloyd's Rep.837. See also *East West Corp. v. DKBS 1912* [2002] 2 Lloyd's Rep. 182, at 205.

[8] The author has examined this issue in more details in, Caslav Pejovic, *Documents of Title in Carriage of Goods by Sea: Present Status and Possible Future Directions,* The Journal of Business Law, 461 (2001).

[9] The term "document of title" was first defined by section 1(4) of the English Factors Act as follows: "The expression 'document of title' shall include any bill of lading, dock warrant, warehouse-keeper's certificate, and warrant or order for the delivery of goods, and any other document used in the ordinary course of business as proof of the possession or control

title, but the approach is different. While in common law, there are several types of documents, such as negotiable documents, negotiable instruments and securities, in civil law all these documents are covered by a single type of document.[10] The "*Wertpapiere*" in German law, "*titre*" in French law, "*titoli di credito*" in Italian law, "*yuka shoken*" in Japanese law and so on can be defined as "documents of value" which contain certain rights embodied in the documents themselves (such as the right to obtain delivery of the goods specified in the document, or the right on payment of a certain sum of money). They confer upon the holder the right to transfer these rights to third parties by transferring the documents. By means of a legal fiction, the bill of lading is deemed to represent the goods, so that possession of a bill of lading is equivalent to possession of the goods. The right to obtain the goods from the carrier is not based on the contract of carriage, but on the lawful possession of the bill of lading. The bill of lading enables its lawful holder to use it to obtain physical delivery of the goods at the port of destination, as well as to dispose of them during transit by transferring the bill of lading.

The effect of the transfer of a bill of lading is a result of the special character of the object of sale —goods carried by sea— such that it is impossible to make a physical delivery of the goods while they are in transit to the buyer. The delivery has to be carried out through the carrier as an intermediary, who receives the goods from the shipper (typically the seller) and is bound to deliver it to the consignee (typically the buyer) in exchange for the bill of lading. In fact, the seller performs the delivery of goods by transferring the bill of lading to the buyer, thereby transferring to the buyer the right to demand the delivery of the goods from the carrier at the port of destination. Through the contract of carriage, evidenced by the bill of lading, the carrier undertakes to deliver the goods as described in the bill of lading to the consignee to whom the shipper transfers the bill. After the bill of lading has been transferred to the consignee, it represents the contract between the carrier and the consignee who has an independent right against the carrier to demand delivery of the goods as described in the bill of lading.

The shipper can retain control over the goods after he has delivered them to the carrier, if the bill of lading is issued on his order, until the buyer pays the price or accepts the bill of exchange. The consignee cannot recei-

of goods, or authorizing or purporting to authorize either by endorsement or delivery, the possessor to transfer or receive goods thereby represented".

[10] This difference between civil law and common law is probably a result of the different nature and approaches of these two largest legal families. While civil law often relies on broad concepts, common law has a preference for narrow concepts.

ve the goods from the carrier without the bill of lading, and he will not obtain the bill of lading before he pays the price or accepts the bill of exchange. The seller will lose control over the goods and the right to dispose of the goods at the moment he transfers the bill to the buyer. By acquiring the bill, the buyer acquires control over the goods and constructive possession. Hence, the rule that the goods must be delivered only against the bill of lading serves to protect against the risk that the goods are delivered to someone who is not entitled to receive them. This rule protects both the carrier and the persons entitled to receive the goods.

III. Delivery of the goods under the rotterdam rules

In contrast to all previous conventions, the Rotterdam Rules expressly regulate the delivery of the goods. Article 11 first provides for the carrier's obligation to deliver the goods to the consignee. This obligation is also mentioned in Article 13(1). Most importantly, Chapter 9 is dedicated to delivery of the goods, where this issue is regulated in detail. With respect to the delivery of the goods, the Rotterdam Rules make a distinction between a non-negotiable transport document (Article 45), a non-negotiable transport document that requires surrender (Article 46), and a negotiable transport document (Article 47). This corresponds to the practice that has developed in which in parallel to bills of lading, sea-waybills are increasingly being used. In addition, the Rotterdam Rules envisage the use of non-negotiable transport documents that require surrender (Article 46), by which the use of straight bills of lading has been expressly recognized for the first time by an international convention. Adding to this complexity is Article 47(2) which entitles the carrier (under certain conditions) to deliver the goods without the surrender of a negotiable transport document.

The Rotterdam Rules do not give a precise definition of negotiable documents, focusing more on appearance and whether a document contains words such as "to order" or "negotiable", but failing to define the concept of negotiability.[11] Since there is no universally adopted meaning of the term negotiable documents, obviously the Rotterdam Rules have left this issue to be determined by the governing law.

[11] Article 1(15). "Negotiable transport document" means a transport document that indicates, by wording such as "to order" or "negotiable" or by some other appropriate wording recognized as having the same effect by the law applicable to the document, that the goods have been consigned to the order of the shipper, to the order of the consignee, or to bearer, and is not explicitly stated as being "non-negotiable" or "not negotiable".

Article 47(2) contains several rules that apply "*if the negotiable transport document expressly states that the goods may be delivered without the surrender of the transport document or the electronic transport record…*"This provision applies in cases where the holder of the document fails to claim the goods at the place of destination, or to identify himself in an appropriate way. In such cases, the carrier may ask for instructions from the shipper, or from the documentary shipper. This provision raises a number of complex questions, as it clearly departs from the fundamental principles applicable to negotiable documents.

As has been mentioned above, in maritime law there is a well established rule that the carrier must not deliver the goods in any way other than against the presentation of an original bill of lading. It may therefore be asked why the Rotterdam Rules have departed from this fundamental principle. How common is the practice of containing clauses in negotiable documents which state that the goods can be delivered without the transport document? Are clauses that provide for delivery without production of the bill of lading so prevalent that it has become necessary for the practice to be legitimized by an international convention? Even if such a practice has become widespread, is it a good practice? Was it really necessary to legalize a practice that contravenes the fundamental principles of negotiable documents? How would this affect the role of transport documents in international trade? Would a bank be willing to pay under a letter of credit against a negotiable document which provides that delivery can be made without its presentation? Is article 47(2) the best solution to the existing problem of delivery of the goods without the surrender of a negotiable document? If the negotiable document expressly states that the goods may be delivered without the surrender of this document, this means that this kind of situation was envisaged at the moment the negotiable document was issued. Why then, it may be asked, was a negotiable document issued at all? Wouldn't it have been more practical and simple for a non-negotiable document to have been issued? Was it really necessary to invent a new transport document that would be called negotiable while, in fact, it would not be negotiable in the usual meaning of the term as it would be deprived of an essential feature of negotiable documents: surrender in exchange for the goods? Can a document that does not require it to be presented against delivery of the goods be considered a negotiable document, or have the Rotterdam Rules created a new type of negotiable document which does not have to be presented to the carrier? Was this article necessary at all? This paper will attempt to answer some of these questions.

IV. Charteparties and article 47(2)

Article 47(2) applies only when the transport document "*expressly states that the goods may be delivered without surrender of the document*". If the carrier is unable to locate the consignee, *"the carrier may so advise the shipper and request instructions in respect of delivery of the goods*". The holder of the document should therefore be aware that, if one of the situations mentioned in that provision occurs, the goods may be delivered on the basis of the instructions of the shipper in the event that the carrier is unable to obtain instructions from the consignee.

The impression is that the drafters were influenced by the practice that exists in many charter parties where the carrier has to obey the charterer's instructions with respect to the delivery of the goods. Such a conclusion may be made based on illustrations the authors of the book "The Rotterdam Rules" (who were at the same time the drafters of the Rotterdam Rules),[12] used in the discussion related to Article 47: each of their illustrations referring to Article 47(2) makes reference to the charterer acting as a shipper.[13]

Under the charter party contracts the master should act "*under the orders and directions of the Charterers as regards employment, agency and other arrangements*".[14] The charterer may wish to extend his authority by stating that he shall have the right to order the master to deliver the goods without a bill of lading. This is sometimes done in practice and this right has been recognized by the courts.[15] However, this situation under charter parties should be clearly distinguished from the contract of carriage governed by international conventions. This practice, which is valid in charter contracts where the freedom of contract prevails, may not be recognized as valid in a contract of carriage carried out under a bill of lading.

The identification of the charterer with the shipper can also be questioned, as it should be clear that the shipper and the charterer are not necessarily the same party.[16] There is a clear distinction between the contract of carriage, which has the carriage of goods as its main subject-matter, and the charter contract, which is basically a contract of hire with the use of a ship as its main subject matter. While in the case of charter contracts the

[12] Michael F. Sturley, Tomotaka Fujita, Gertjan van der Ziel, *The rotterdam rules*, Sweet and Maxwell, 2010.

[13] *Ibidem*, pp. 264 and 269.

[14] Gentime, cl. 12. NYPE 1993, cl. 8.

[15] *Enichem Anic SpA* vs *Ampelos Shipping Co Ltd, The Delfini,* 1990, 1 Lloyd's Rep 252.

[16] Article 1(8) defines shipper as "a person that enters into a contract of carriage with a carrier."

charterer may have the right to make orders to the master with respect to the voyage the situation is completely different in liner carriage.

The relationship between the charterer and the shipowner in a charter party contract is qualitatively different from the relationship between the shipper and the carrier. The relationship between the shipper and the carrier is based on a document of a very different nature, the bill of lading, which is not a contract but a document of title. While the shipper may at the same time be the charterer, it is clearly wrong to have provisions related to the shipper with the assumption that the shipper is always the charterer. The application of Article 47(2) may lead to a situation in which the carrier requests instructions from the shipper when the shipper is not the charterer and has transferred the bill of lading. Clearly, in such case asking instructions from the shipper would contravene the fundamental principles on negotiable transport documents.

Article 47(2) is based on the assumption that the shipper has information on the consignee. While in some carriages the shipper may be aware of the ultimate consignee, in many situations that is not the case. One of the key problems with Article 47(2) is that it fails to fully take into consideration the fact that the goods may be resold in transit, sometimes many times. In the commodity trade, the shippers often have no clue who the final holder of the goods will be. They simply charter a vessel in order to load their cargo and sell it in transit. In such cases it makes no sense to ask the shipper for instructions with respect to delivery. After the shipper has sold the cargo to the first buyer in the chain, under Article 51 he has lost the status of the controlling party and is not qualified to give instructions to the carrier related to delivery of the goods. In fact, in the most common case of problems of delivery of the goods without a bill of lading, the shipper's instructions under Article 47(2) have the lowest value. Or, to put in it a different way, the intended effect of the provision on the shipper's instructions might be the least effective in situations where it is the most needed.

Instead of asking the shipper for instructions, there is already a well established practice that bills of lading contain the notify party, whom the carrier must notify when the goods arrive at the port of destination. The notify party is normally in a better position to provide information on the consignee.

V. The houda case lessons

In most jurisdictions, the courts take the position that the shipowner must not deliver the goods other than against presentation of a bill of la-

ding, even if he has been instructed by the charterer to make such a delivery.[17] In *The Houda* case,[18] the charterer ordered the shipowner to deliver the goods without a bill of lading, against a letter of indemnity countersigned by a bank, but the shipowner declined to accept this order. The court at first instance held that while under a time charter the charterer cannot lawfully order the shipowner or the Master to deliver the cargo to a consignee who is not entitled to possession of the cargo, the charterer is not prevented from ordering delivery of the cargo without production of the bill of lading in circumstances where the charterer is entitled to possession of the cargo or gives an order with the authority of the person entitled to possession of the cargo. The Court of Appeal, however, took a different view and rejected the argument that a time charterer could order a shipowner to deliver the goods without production of an original bill of lading, even to a person who was entitled to possession of the goods.

Lord Judge Millet examined the consequences of such a solution:[19]

"*But the real difficulty of the Judge's conclusion is that it leads to this: the charterers can lawfully require shipowners to deliver the cargo without presentation of the bills of lading if, but only if, the person to whom the cargo is delivered is in fact entitled to receive it. If that is indeed that law, it places the master in an intolerable dilemma. He has no means of satisfying himself that it is a lawful order with which he must comply, for unless the bills of lading are produced he cannot know for certain that the person to whom he has been ordered to deliver the cargo is entitled to it. One solution, no doubt, is that, since the master's duty is not of instant obedience but only of reasonable conduct, he can delay complying with the order for as long as is reasonable necessary to satisfy himself that the order is lawful, possibly by obtaining the directions of the Court in the exercise of its equitable jurisdiction to grant relief in the case of lost bills. But in my judgement the charterers are not entitled to put the master in this dilemma*."

The point is, as Lord Judge Millet states in the last sentence of the quote, that the charterer puts the master in a difficult situation. The mas-

[17] *The Stetin* (1889) 14 PD, 142 at 147., *A/S Hansen-Tangens Rederei III* vs. *Team Transport Corporation (The Sagona)*, 1984, 1 Lloyd's Rep. 194, *Kuwait Petroleum Corp.* vs. *I and D Oil Carriers, The Houda,* 1994, 2 Lloyd's rep. 541, *Motis Exports* vs. *Dampskibsellskabet AF* 1912, 2000, 1 Lloyd's Rep. 121, *Allied Chemical International Corp.* vs. *Comphania de Navegacao Lloyd Brasiliero,* 1986, AMC 826 (2d. Cir. 1985), *C-Art Ltd. V. Hong Kong Island Lines America* [1991] AMC 2888 (9th. Cir. 1991), *Glencore Intenational AG* vs. *Owners of the 'Cherry'*, Singapore High Court, Kan Ting Chiu J., April 2002 (available at: *http//:onlinedmc.co.uk/glencore_v_'cherry'.htm*), *International Harvester Co* vs. *TFL Jefferson* 695 F.Supp 735 (S.D.N.Y. 1988), *Cour d'Appel d'Aix,* September 6, 1984, DMF 1986, 157, *Ap. Paris 11 January 1985* (1986) DMF 166 (note by R. Achard), *Trib. Livorno 10 December 1986* (1987) Dir. Mar. 961.

[18] *Kuwait Petroleum Corp. v. I and D Oil Carriers*, *The Houda,* 1994, 2 Lloyd's Rep. 541.

[19] *The Houda*, 1994, 2 Lloyd's Rep. p. 558.

ter takes an obvious risk when he delivers the goods to a consignee which cannot produce the bill of lading. The question one may ask is whether the charterer may require the shipowner to take such a risk. Even though the master may always require that the charterer puts up adequate security before he delivers the goods, the section must still be considered to weaken the shipowner's position. To demand such security will, in most cases, be both more cumbersome and unreliable than to demand that the bill of lading be presented.

The claim that such a delivery is lawful if ordered by the person entitled to possession of the cargo contravenes the fact that the bill of lading is a document of title. It is a well established principle that the carrier is bound to deliver the goods only to a lawful holder of the bill of lading, and he is not bound to investigate who is entitled to possession of the goods. When the consignee is not able to produce the bill of lading, the shipowner as carrier has the option of refusing the charterer's order of delivering the goods without the bill of lading or to deliver the goods in exchange for a letter of indemnity that was offered to the shipowner in the present case. The most serious consequence of this judgment would be that the carrier would no longer be justified in refusing to deliver the goods to a party who is not the lawful holder of the bill of lading, or in the case of a non-negotiable bill of lading to a party who is not named in the bill of lading, when such a party is actually entitled to the goods. Such a radical change would endanger the role of the bill of lading as a document of title and discredit its commercial value. In addition the carrier would be put in an extremely difficult position because he would be forced to judge whether the person to whom delivery is to be made under the charterer's order is entitled to possession of the goods.

This illustration from the charter party contracts in the relationship between the charterer and the shipowner may serve as an indication of potential problems that may arise if the shipper were to be asked to give instructions to the carrier under a contract of carriage. Article 47(2) would make sense in the relationship between the charterer and the shipowner under a charter party contract, and the outcome of *The Houda* case would have been different if there had been an express term in the charter party entitling the charterer to order the owners to deliver the goods without a bill of lading. However, the Rotterdam Rules should not enter that area, because contracts under charter parties are expressly excluded from their scope. It should be noted that the Rotterdam Rules expressly provide that the convention applies to liner carriage (Article 1.3), and that it does not apply to the charter party contracts (Article 6.1).

VI. Deviation from the fundamental principles

The solution proposed under the Rotterdam Rules represents a substantial deviation from the existing and well established practice. It seems that the Rotterdam Rules, in attempting to tackle the issue of delivery without a bill of lading, risked creating confusion by addressing problems that are typical for charter contracts. The drafters of the Rotterdam Rules obviously aimed at solving the problem of delivery of the goods when a negotiable document is not or cannot be surrendered. Normally, in such case the carrier should demand instructions from the lawful holder of the document, which is the consignee and not the shipper. It seems that the assumption of the drafters was that the consignee often does not demand delivery.[20] However, it is more likely for the consignee to not have the document, so that delivery is not possible. If the consignee has obtained a bill of lading, that normally means that he has paid the price, so it would be strange if he did not demand the goods. The consignee may refuse to accept delivery if the goods are defective, but this situation has nothing to do with delivery without a bill of lading. The typical problem with failing to present the transport document is that documents are subject to examination in a letter of credit transaction and where the goods are resold several times in transit the procedure with the document may be time consuming, particularly in the commodity trade.

Charles Debatista argues that under Article 47(2) "*the holder must still possess the bill but need not surrender it for delivery of the goods*" and that possession of the bill of lading is "*manifested through presentation but not surrender*".[21] My reading of this provision is different. In my view, Article 47(2) can apply in situations when the consignee does not have the bill of lading at the moment the goods arrive at the destination, i.e. the consignee does not have possession of the bill and consequently cannot present it. This view is supported by subparagraphs 2(d) and 2(e), which expressly state that a holder becomes a holder after the carrier has delivered the goods pursuant to subparagraph 2(b). In any event, what would be the logic behind a consignee presenting the bill and refusing to surrender it?

The basic requirement of the rule contained in article 47(2) is that the negotiable transport document expressly states that the goods may be delivered without the surrender of the transport document. This clause contravenes a fundamental feature of negotiable documents, as the presentation

[20] Alexander von Ziegler, Johan Schelin, Gertjan van der Ziel (eds.), *The rotterdam rules*, Walters Kluwer, 2010, p. 207.

[21] *Ibidem*, p.146.

and surrender of a transport document is an essential ingredient of negotiable transport documents. The rule that the goods are to be delivered only to the lawful holder of a bill of lading who must present it prior to delivery is essential to the function that the bill of lading performs as a document of title. One of the key functions of negotiable transport documents is enabling the transfer of the right to the delivery of the goods by transfer of the document itself. If the goods can be made deliverable without a negotiable transport document, this key function of negotiable documents would be compromised. This function also represents the basis of security of the holders of those documents, as the lawful holder is guaranteed that nobody else can receive the goods. If it were possible to deliver the goods without surrender of the transport document, that security function of negotiable documents would be undermined.

In cases where presentation is not required at the destination from the very beginning, in practice the document may be marked on its face with a stamp stating "not negotiable". While working for a shipping company I remember seeing a number of bills of lading stamped "not negotiable" on their face. The common understanding was that these were not negotiable documents and that delivery was to be made either to the consignee named in the document, or under the shipper's instruction. It can be said that calling such documents "bills of lading" was a misnomer, as they were, in fact, waybills, and they were not considered to be negotiable documents.

Article 47(2) is designed in such a way as to create a document that is called a negotiable document, but which is not necessarily negotiable, since the goods can be delivered without its surrender. Article 47(2) identifies as a negotiable transport document a document whose surrender is not required. This creates a contradiction -- in the case of negotiable transport documents, the delivery of the goods can be made only against the surrender of the document. Was this kind of acrobatics really necessary? Wouldn't it be better to simply follow the already existing practice that non-negotiable documents are used in this kind of situation? The maritime practice has developed the use of the sea waybill to tackle the problem of delivery of the goods without the surrender of a transport document. The Rotterdam Rules have adopted this solution in Article 45. Was it really necessary to have in addition to non-negotiable documents, a new type of document that would be called "negotiable" but whose surrender would not be necessary?

Such a rule may also open a possibility for maritime fraud. The seller may sell the goods to another buyer leaving the first buyer with a claim against the carrier, who may not be liable at all under the Rotterdam Rules, if delivery was made according to the shipper's instructions. The shipper

may also collude with the first buyer to defraud all subsequent buyers. If the goods are delivered without production of a bill of lading, there is also a risk that the buyer who received the goods before payment is made can later refuse to pay because he has already obtained possession of the goods. Another danger is that the buyer can resell the goods by transferring the bill of lading to a new buyer, so that another party can present the bill of lading and claim the goods from the carrier.

All situations of delivery without the surrender of the document should be treated as risky exceptions. The attitude of the business community towards delivery of the goods without a bill of lading is very negative, a fact that is reflected in the rules of P&I clubs to deny indemnity to the carriers in such cases, as well as the fact that carriers are deprived of the benefit of limitation of liability. Against such a background, Article 47(2) can be considered as an attempt to legalize a practice that has been considered risky, exceptional and bad.

VII. Relation to the right of constrol

The second part of article 47(2) is related to Chapter 10 of the Rotterdam Rules which deals with the right of control. Article 50(1)(a) provides that the rights of the controlling party include the right to give instructions in respect of the goods. Further, article 51(1)(a) provides that the shipper is the controlling party, except in a number of cases expressly referred to in this provision, which includes paragraph 3 of the same article that applies to the case when a negotiable document is issued; in this case the holder of the original negotiable document is the controlling party.

Here again several questions can be raised. If Article 51(3)(a) provides that when a negotiable document is issued the holder of the negotiable document is the controlling party, then why should the carrier ask instructions from the shipper? When the shipper is not the controlling party according to Chapter 10, but the controlling party is a transferee of the transport document pursuant article 57, on what legal basis can such shipper, or documentary shipper, give instructions to the carrier? Moreover, Subparagraph 2(b) provides that the carrier that delivers the goods upon instruction of the shipper is discharged from its obligation to deliver the goods to the holder, even if the transport document has not been surrendered. This is quite puzzling and it is not clear on what ground the carrier can be discharged against the lawful holder of the bill who has an independent right to delivery which is embodied in this document. How could

a carrier possibly be discharged from his obligation to deliver the goods if he were to deliver the goods according to the shipper's instructions? On whose behalf does the carrier hold the goods when a negotiable document is issued: on behalf of the shipper, or on behalf of the lawful holder of the negotiable document? When the shipper is not the controlling party, nor does he have any authority regarding the goods, it is not clear how instructions of such a party can discharge the carrier from its obligations embodied in a negotiable document. What would happen if the lawful holder appeared and claimed delivery after the carrier delivered the goods in accordance with the shipper's instructions to a party who was not entitled to delivery? Subparagraphs 2(c), 2(d) and 2(e) indicate that the carrier may still be held liable against a lawful holder, which seems to contradict subparagraph 2(b). How could the carrier be discharged from his obligation to deliver the goods to the holder if he can be held liable against the holder? In order to avoid misunderstanding and confusion, these provisions could have been drafted in a clearer way.

What would happen if the negotiable document is negotiated several times, as often happens in the commodity trade? The shipper may provide information on the first transferee, but he would normally not be able to give information on other holders of a negotiable document and probably would not know the identity of the last lawful holder of it. And why would the shipper bother to give instructions at all? Why would he risk potential liability under Article 47(2)(c), if the instructions were be wrong?

Article 28 provides for cooperation between the carrier and the shipper, including giving instructions related to the handling of cargo and carriage. Does this obligation extend to the shipper's duty to provide instructions related to the delivery of the goods? From the text it might be difficult to reach such a conclusion, unless "handling and carriage" is construed in a broad sense. Based on Article 29(1) which provides that the shipper will provide to the carrier" *information, instructions and documents relating to the goods"* that are necessary *"(F)or the proper handing and carriage of the goods"*, it can be concluded that these instructions relate to the handling and carriage of the goods. But even though a broad interpretation would include instructions related to delivery of the goods, this does not mean that the shipper is the person who should give instructions related to the delivery of the goods after he has transferred the bill of lading. Finally, article 47(2) fails to give a clear solution for the situation where the shipper would not give any instruction to the carrier.

VIII. Article 47(2) and the CISG

One of the intriguing questions that arises is related to the status of negotiable transport document under Article 47(2) in relation to Article 58 of the CISG; can this document be considered a document "controlling the disposition of the goods" in the sense of Article 58 of the CISG? According to Martin Davies, the drafters of the CISG likely "*had in mind the traditional, negotiable bill of lading issued by an ocean carrier, which is the paradigm document controlling the right to possession of the goods it represents*".[22] A document under Article 47(2) equally likely does not meet this description. The fact that the goods may be delivered without the surrender of a negotiable transport document clearly compromises its negotiable character and the capacity to control disposition of the goods.

While a negotiable transport document under Article 47(1) qualifies as a document "controlling disposition of the goods", a negotiable transport document under Article 47(2) is not a negotiable document in the full sense of the CISG, since disposition of the goods is not carried out on the basis of the document itself, but on the basis of the shipper's instructions. This kind of disposition of the goods, as well as delivery without surrender of a transport document, is typical for non-negotiable documents which do not control disposition of the goods, since this is done by the shipper's instructions to the carrier.

Hence, the "negotiable transport document" under Article 47(2) is not negotiable in the full sense, and as long as disposition of the goods is carried out on the basis of the shipper's instructions, it is not a document that controls disposition of the goods in the sense of Article 58 of the CISG.

IX. Conclusion

A challenging road lies ahead for the Rotterdam Rules. One of the potential problems is related to the way the Rotterdam Rules were drafted. After the task of unification of maritime law was transferred from the CMI to the UN and its agencies, it became impractical and maybe even impossible to make interventions by revisions, such as the Visby Rules. The most efficient and practical way would be to simply revise a number of provisions

[22] Davies, Martin, "Documents that Satisfy the Requirements of CISG article 58", papers from *Uniform Sales Law: the CISG at its 30th Anniversary, a conference in memory of Albert H. Kritzer*, 12-13 November 2010, Belgrade, The Annals of the Faculty of Law in Belgrade - Belgrade Law Review, Year LIX (2011) num. 3 pp. 39-66.

from the Hague-Visby Rules, such as abolishing the nautical fault exception and adding a few more provisions, such as those related to electronic documents. It would however be difficult to expect the UNCITRAL to take such action, even though technically it was possible for the Rotterdam Rules to have simply been a revised version of the Hague-Visby Rules. The UNCITRAL generally has a preference for a more comprehensive approach, which is demonstrated by the text of the Rotterdam Rules. As result, the Rotterdam Rules contain 96 articles and 18 Chapters, compared to the 16 articles of the Hague Rules.

The Rotterdam Rules added a number of new issues, such as the right of control, delivery of the goods, transfer of rights, and volume contracts. The text might be too complex and too complicated to be suitable for use in practice. The commercial practice needs clarity and has a natural preference for simple over complicated texts. Moreover, some provisions, such as Article 47(2), are highly controversial as has been demonstrated in this paper.

It can be said that article 47(2) is controversial in the sense that this provision contravenes some well established principles on negotiable documents. Admittedly, the rule that the consignee must present a negotiable document prior to delivery is outmoded and can cause many problems in practice. Delivery of the goods without a bill of lading is something that should be avoided. The drafters of the Rotterdam Rules have attempted to find a solution to this problem. However, the suggested solution may undermine the value of the bill of lading as one of the key documents in international trade. If purchasers and banks feel that they can no longer rely on bills of lading as negotiable documents of title, to paraphrase Pearce L.J. in the *Brown Jenkinson* case, "*the disadvantage to the commercial community would far outweigh any convenience provided by delivery of the goods without bills of lading*"[23]

The goal of uniformity is a worthy one and the efforts of the drafters of the Rotterdam Rules deserve respect. Instead of unifying the rules that govern the carriage of goods by sea, however, the Rotterdam Rules may end up being just another convention that exists in parallel with all previous ones, which would mean that this convention instead of contributing to the unification of law governing the carriage of goods by sea may, in fact, undermine the already existing chaotic level of uniformity. Under the existing text of the Rotterdam Rules, the road towards the stated goals has too many holes to feel comfortable with the proposed solution. It is a bumpy road that eventually may create more problems that it solves.

[23] *Brown Jenkinson vs. Percy Dalton (London) Ltd.*, 1957, 2 Q. B. 621, C. A.

THE REMEDY OF DAMAGES IN PUBLIC PROCUREMENT

Arie REICH* and Oren SHABAT**

SUMMARY: I. Israeli statutory framewrok and court rulings governing the field of damages for aggrieved bidders – general overview. II. The statutory framework for lodging an action for damages in israeli public procurement law. III. The damages remedy in israeli public procurement case law. IV.

Damages are formally part of the arsenal of remedies that an aggrieved bidder in a public procurement procedure may use in most jurisdictions, such as the EU, the US and Israel. It is also required by the WTO Agreement on Government Procurement.[1] This remedy could have a critical role to play both in the encouragement of potential suppliers to invest in participation in the tender, as well as in curtailing and deterring improper or corrupt behavior by procuring agencies. However, in order for that to happen, the damages that are awarded must be effective and deterring. In spite of the great promise that such damages hold in encouraging greater competition in contracting and in reducing irregularity, the current rules that apply to the award of damages both in Israel and in other countries have made this remedy ineffective and non-deterrent. After reviewing the current Israeli rules and rulings in this field, this paper will examine the current situation in the EU and will focus on the similar problems of ineffectiveness and non-deterrence that exist in these jurisdictions. We will then propose changes aimed at improving the effectiveness of damages in public procurement so as to turn them into a deterrent factor in the fight against corruption.

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[1] See Article XX of the Agreement on Government Procurement, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 4, reprinted in *Results of the Uruguay Round* (WTO, 1994) at 438.

I. Israeli statutory framewrok and court rulings governing the field of damages for aggrieved bidders – general overview

Current Israeli law recognizes the importance of action for damages for infringement of public tenders rules. In certain aspects, Israeli Public Procurement Law even encourages such an action for damages.[2] Paradoxically, damages for infringements of public tenders rules, and in particular damages for loss of profits, are difficult to obtain. This crucial difficulty may be attributed to certain rules to be further analyzed below: (1) the requirement to prove causality; (2) the requirement to seek a set-aside remedy before lodging an action for damages; (3) time limitations for lodging an action for damages, (4) lengthy and costly processes; and (5) generally low awards, even when an action for lost profits has succeeded. It will be seen that at least in relation to some of the factors mentioned below, Israeli law and EU countries generally share close similarities. Therefore, the proposals presented in this paper are relevant and, we believe, valuable for all of these jurisdictions, and perhaps others as well.

II. The statutory framework for lodging an action for damages in israeli public procurement law

Public tenders in Israel for central government authorities as well as for various other governmental and public entities are governed by the Tenders Duty Law, 1992 and the Tenders Duty Regulations, 1993. These pieces of legislation set out in detail the tendering rules to which government entities are bound whenever they want to purchase or sell goods or services.[3] However, they do not deal with the remedies available should the relevant rules be breached. This is a field that has been developed mainly by the courts.

The Administrative Courts Law, 2000, which established the Administrative Courts as part of the District Courts, authorized these courts to hear administrative cases which previously were heard by the Israel Supreme Court, in its capacity as the High Court of Justice. The law provides for two

[2] As will be shown below, the courts will sometimes reject a petition for an injunction against a procurement award based on the reason that if a breach will be proven it can be compensated by an action for damages, thus, implicitly encouraging such actions over petitions for injunctions.

[3] It is to be noted, that the rules that apply to public tenders in Israel originate both from Administrative and Private Law. This dual applicability is widely known as the "normative dualism principle".

types of actions that are relevant to public procurement: 1. "Administrative Petitions", which are petitions against a decision of an administrative agency (such as a contract award decision); and 2. "Administrative Actions", which are actions for damages resulting from infringements of the public procurement rules.[4] Administrative actions are reviewed in accordance with the Civil Procedure Regulations, which provide the procedural framework for the review of most civil actions in Israel.[5] An important and distinctive feature of Administrative Actions is that such actions cannot be lodged with the court in parallel to lodging an Administrative Petition (i.e., a judicial review action which is targeted at setting aside the procuring authority's decision). Practically, this means, that when an aggrieved bidder lodges an Administrative Petition he cannot, at the same time, apply for damages. Thus, in order to apply for damages he is required to ask for the court's approval to convert his Administrative Petition into an Administrative Action[6] or wait until the Administrative Petition is decided. However, as will be shown later, the situation is more complex. It has lately been suggested by the Supreme Court that an aggrieved bidder seeking damages cannot skip the Administrative Petition review stage.[7] That is, she must first submit an Administrative Petition and pursue this petition. Then, and only if she fails to obtain a setting aside decision, by reasons which are not her fault, she may proceed with lodging an Administrative Action.

III. The damages remedy in israeli public procurement case law

1. *Early Case Law on the Damages Remedy*

The damages remedy in Israeli Public Procurement case law dates back to the 1960's, when the Israeli High Court of Justice awarded to a petitioner damages for the breach by the Ministry of Defense of its commitment to sign a contract with the petitioner for road construction. The unequivocal

[4] Article 5 of the Administrative Courts Law, 2000. The Court for Administrative Matters is the competent court for Administrative Actions. However, some actions for damages in connection with public tenders may be submitted to the Civil Courts.

[5] However in the case of a discrepancy between the provisions of the Administrative Courts Law, 2000 and the Administrative Courts Regulations (Procedure), 2000 on the one hand and the Civil Procedure Regulations, 1984 on the other hand, the former will prevail. See r. 30 of the Administrative Courts Regulations (Procedure), 2000.

[6] R. 30 of the Administrative Courts Regulations (Procedure), 2000.

[7] The Broadcasting Authority *vs*. Katimora, *infra* note 23, discussed below in section C(3).

and convincing reasoning of the ruling in the Construction & Development case, as expressed by Judge Berenzon, was based on the need to improve public efficiency and deterring the re-occurrence of such an impropriety:

> "to improve the quality and fitness of action of the public system and boost its level of care and efficiency; as well as to provide further caution and agility in the handling of citizens' matters; and in the responsiveness to their needs. It will also advance and improve the public service level of the State".[8]

Despite the court's unprecedented willingness to award damages for aggrieved bidders in a public tender, the court stressed that in its position as High Court of Justice[9] it may only award damages for "the sake of justice", while the quantum of damages to be awarded shall be calculated according to a general estimate, "without a meticulous examination of the details".[10] What the Court meant was, that it would be willing to award an aggrieved bidder some limited damages based on the court's general and very approximate estimate, without conducting a thorough examination of the factual ground which gave rise to the damages claimed. A later case of the High Court of Justice placed a strict limitation on the scope of an action for damages by an aggrieved bidder. Thus, in the Migda case, Judge Aharon Barak[11] ruled, that only in "extraordinary cases" would the High Court of Justice be willing to employ its power to award damages to an aggrieved bidder.[12] The main reasoning expressed by the Court for its general reluctance to award damages was the lack of procedural means available to the High Court of Justice to perform the necessary judicial fact-finding and damage assessment, as opposed to the amplitude of means available to the Court for Civil Matters.[13]

[8] High Court of Justice 101/74 Construction and Development in Negev Ltd.(*Binui Upituach BaNegev*) *vs*. Minister of Defence, P. D. 28(2) 449,456-457, This and all other quotes from Israeli judgments are the authors' translation from the Hebrew original.

[9] Which does not act as a fact finder and generally does not conduct cross examinations of witnesses on their affidavits.

[10] Supra note 9, p. 458-459.

[11] Judge Aharon Barak later presided over the Supreme Court of Israel from year 1993 to 2006.

[12] High Court of Justice 688/81 Migda *vs*. Ministry of Health, P.D. 36(4)85, 100-101. Nevertheless, the court held that such an action for damages would normally be referred to a competent court (i.e. to a competent Court for Civil Matters), to decide on the action. See also High Court of Justice 2167/90 Micronet *vs*. Ministry of Culture and Education, P. D. 45 (1)45, 54-55.

[13] *Idem*. At the time, the exclusively competent court for hearing disputes concerning public tenders was the High Court of Justice. However, this exclusive jurisdiction rule was later

In a case decided before the Supreme Court known as the Beit Yules case,[14] the court awarded an aggrieved bidder damages for expenses incurred in participating in the tender but refused to award him damages for lost profits, holding that he had failed to prove a causal link between the infringement and the claimed damages.[15]

2. *The Supreme Court's Decision in the Malibu Case –Damages for Lost Profits to Aggrieved Bidders*

The Malibu Decision

A significant milestone in the development of the damages remedy for aggrieved bidders is the Supreme Court's decision in the Malibu[16] case.

The Supreme Court found that the Israel Electric Corporation had unlawfully deprived the respondent from being awarded a contract to build a part of a power plant in one of its facilities. The contract became a "fait accompli" because it was performed by another bidder.[17]

The Supreme Court held, therefore, that the appellant was entitled to recover the profits lost as a result of the unlawful deprivation of the contract award.[18] As will be shown below, the Malibu case has been very strictly

relaxed in the High Court of Justice decision 991/91 David Pasternak *vs*. The Minister of Construction and Housing, P. D. 45(5) 50.whereby the High Court of Justice granted the Courts for Civil Matters jurisdiction to hear such disputes.

[14] Civil Appeal 207/79 Raviv Moshe and Partners vs. Beit Yules, P.D. 37 (1) 533.

[15] This Supreme Court decision was later overturned in Further Hearing 22/82 Beit Yules *vs*. Raviv Moshe and Partners, P.D. 43(1)441 on grounds that are not relevant to this paper.

[16] Civil Appeal 700/89 The Electric Corporation of Israel Ltd. *vs*. Malibu Israel Ltd. and others, P.D. 47(1)667 (hereinafter "Malibu"). At the time when the Malibu dispute was heard, the Courts for Administrative Matters were not established yet. Actions for damages concerning public tenders were, therefore, brought before the Courts for Civil Matters (in this case it was the District Court); appeals were heard in accordance with the Civil Procedure Regulations, 1984. See also supra note 15. This clarifies why the Malibu case was heard by the Supreme Court of Israel as a civil appeal. Nowadays, as will be explained below, similar actions are brought before the Courts for Administrative Matters and (generally speaking) are governed by the Courts for Administrative Matters Law, 2000 and Courts for Administrative Matters Law Regulations (Procedure), 2000.

[17] It is important to stress, that the Supreme Court expressly held that a causal link between the infringement of public procurement law by the Electric Corporation and the contract award deprivation, had been established. Additionally, the contract had already been performed by another bidder. Under such circumstances the court decided that it was appropriate to award damages for loss of profits.

[18] Malibu, *supra* note 17, pp. 689-690. Nevertheless, in upholding the lower instance's factual findings in this matter, the court refused to award the appellant damages for loss of

interpreted by later case law and therefore fails to fully reflect the current legal situation in this field. Nevertheless, it still remains a remarkable case whereby damages for lost profits where awarded to an aggrieved bidder.

Strict Interpretation of the Malibu Decision

Later Israeli case law provided a strict interpretation of the Malibu decision, thereby limiting many aspects of the scope of an action for damages lodged by an aggrieved bidder, even when an infringement of public procurement law was duly proven.

Thus, in the Ports Authority case[19] the Supreme Court quashed the lower instance's decision to award an aggrieved bidder damages for lost profit. It was held, that no evidence was shown to convince the court that the procuring authority "accommodated" its calculations of the bids with prior intention to improperly award the contract to another bidder. It was also held, that neither bad faith nor improper or arbitrary considerations were employed by the procuring authority. The court found however, that the procuring agency unlawfully failed to, inter alia, publish in advance its calculation method of the economic value of the bids. The Supreme Court, therefore, refused to award damages for lost profits and decided to follow the principles laid down in the case of Construction and Development. It, therefore, awarded the aggrieved bidder damages based on a general estimation of the "expenses caused to (him) as a result of the infringements found in the procurement procedure" at the sum of 150,000 NIS (approximately US $40,000). No legal expenses were awarded against the losing procuring agency. The Port Authority case seems to suggest, that only in circumstances of extreme impropriety or bad faith could the court be convinced to award damages for lost profits, while in all other cases of a lower degree of impropriety, an aggrieved bidder may be awarded more limited damages, which may be based on some unknown standard and method of calculation. Furthermore, given the length of the particular proceedings that took place before the first instance and the Supreme Court[20] it is doubtful whether the damages awarded to the aggrieved bidder could actually cover its high legal expenses and expenses incurred in preparing the bid and in participating in the tender.

reputation and for general damages (pp. 691-629).

[19] Administrative Petition Appeal 7357/03 Ports Authority *vs*. Tzomet Engineers, Planning, Coordination and Projects Administration Ltd. P.D. 59(2)145.

[20] The proceedings before the first instance started in year 2001. The Supreme Court ruling was given on September 2004.

Despite the very strict limitations set by the courts on the scope of the action for damages, some actions were indeed successful,[21] however such successful action are only very few and mostly predate the Broadcasting Authority case, which will be analyzed below.

3. *Further Limitations on the Scope of the Damages Remedy*

In the Broadcasting Authority case[22] the Supreme Court overturned another ruling of a lower instance, the Administrative Court, which awarded damages for loss of profit to an aggrieved bidder. The Supreme Court held that a causal link between the impropriety that was revealed in the public tender and the aggrieved bidder's loss could not be established. Furthermore, the court was not convinced that the Broadcasting Authority had accommodated the tender so as to exclude the aggrieved bidder and thus award the contract to its commercial rival. In other words, the court was not convinced that there had been bad faith on the part of the procuring agency.

However, in an obiter dictum, Justice Grunis also remarked that the aggrieved bidder did not fully pursue her petition before the first instance to obtain a set-aside relief. Bringing an action for damages by an aggrieved bidder, without initially pursuing a set-aside relief could, in the court's view, lead to an undesirable result of what the court notoriously named "a virtual winner". The "virtual winner" phenomenon, the court feared, will expose procuring authorities to a risk of paying twice (although not the same amount) for the same project: one to the actual contractor and one to the "virtual winner" who should have won the contract but who in effect has not provided any consideration. Interestingly, Justice Grunis refers to the fact that also in the United States, the vast majority of the cases have denied expectation damages (i.e., compensation for lost profits) from aggrieved bidders and only awarded reliance damages.[23] The court also raises the con-

[21] One rare example is a judgment by the District Court of Tel-Aviv in Administrative Case 124/06 Avigal Manpower Services Ltd. *vs.*, Herzlia Municipality Tak-Mech 2010(1) 14685 (2010), where NIS 1 million was awarded for lost profits, but the court does not elaborate on the reasons which lead it to this decision. See also MA (T.A.) 107/02 Jaljuli Planning and Execution G.L. 1996 Ltd. *vs.* Municipality of El Tira; and C.C. (Jer.) 2220/00 Lighting Factory A. Hecht Ltd. *vs.* The Postal Authority Tak-Mech 2003(2) 16627 (2003).

[22] Appeal on Administrative Petition 9423/05 The Broadcasting Authority *vs.* Katimora Ltd Tak-Al 2007(3) 2403 (hereinafter: "The Broadcasting Authority" case).

[23] The Court refers to the judgment of the Supreme Court of California in *Kajima/Ray Wilson vs.* Los Angeles County Metropolitan Transportation, 1 P.3d 63, 2000; Cal. LEXIS 4551.

cern of two contradicting judgments: one judgment in relation to the administrative petition ruling that Supplier A was justifiably awarded the contract, and one —by a different judge— in the action for damages ruling that Supplier B should have won the contract, and therefore is entitled to expectation damages. The court seems to suggest, that if we were to require the aggrieved supplier to pursue, to the end, an administrative petition against the contract award, the risk for such conflict of judgments would be averted, since the supplier would be bound by the first ruling as a res judicata.

However, the Supreme Court did not in the end base its ruling on this consideration, but rather on the failure of the plaintiff to prove causality. The court therefore awarded the aggrieved bidder only reliance damages, that is, damages for expenses incurred in preparing the bid, at the sum of NIS 75,000, instead of the NIS 1.3 million awarded by the Administrative Court for lost profits. The aggrieved bidder was also required to pay court and attorney fees to the appellant, the procuring agency, at the sum of 10,000 NIS. However, the more troubling aspect of the Broadcasting Authority case, in our opinion, is the suggestion by the obiter dictum that there may be a requirement on the aggrieved bidder to pursue an action for obtaining a set-aside relief, before he can claim damages. The President of the Court, Justice Beinish, also expressed in her concurring opinion agreement in principle with this dictum of Justice Grunis. She writes:

As a rule, it seems that one should not accept the skipping over the phase of the execution, that is a petition to enforce the winning of the tender, to the phase of the administrative action for the purpose of receiving expectation damages.[24]

She also holds that as a rule only reliance damages should be awarded, and only in exceptional circumstances there may be a justification to award expectation damages. In holding so she also refers to a previous decision of hers in the matter of the Port Authority, discussed above, where she held that expectation damages should be awarded only in cases of bad faith on behalf of the procuring agency.[25] However, she too prefers to leave these questions for later deliberation, since there was no need to rule on them in the case at hand. A later decision by the Supreme Court has also expressed concurrence with this dictum, although suggested not to implement it stringently.[26]

[24] Page 7 of the judgment, supra note 23.

[25] Port Authority *vs*. Tzomet Engineers, supra note 20, at 166-168.

[26] Appeal on Administrative Petition 5487/06 Supermatic Ltd *vs*. Israel Electric Corporation Ltd. (12.4.2009). Justice Naor, who wrote the Supreme Court's unanimous opinion,

The Administrative Courts in Israel, which are (generally speaking) the competent courts for legal disputes on public tenders, seem to have accepted the obiter dictum expressed in the Broadcasting Authority case as a binding ruling and also interpreted it very widely, thereby imposing strict limitations on the scope of an action for damages. This approach is clearly reflected in the case of Koach Otzma Ltd.[27] In this case the Administrative Court of Tel-Aviv struck out an Administrative action —an action for damages lodged by a supposedly aggrieved bidder— without considering the merits of the case. Apparently, the plaintiff did follow the obiter dictum expressed in the Broadcasting Authority case and lodged a timely Administrative Petition for a set-aside relief with the Administrative Court. He also applied for an interim injunction in order to prevent the contract from being granted to the winning bidder during the legal proceedings, thus transforming the tender into a "fait accompli". However, the plaintiff failed to obtain an interim relief, which meant for him, that the procuring authority could not longer be prevented from granting the contract to the winner. The plaintiff then withdrew its Administrative Petition for a set-aside relief, which had seemed obsolete to him, as he became unable to stop the contract from being awarded and performed. Furthermore, as aforesaid, it is not possible for an aggrieved bidder to bring an Administrative Action as long as an Administrative Petition for a set-aside relief is pending.

The plaintiff brought instead an Administrative Action - an action for damages. Nevertheless, as aforesaid, the court struck out the action without referring to the merits of the case. In its decision, the court held that the plaintiff's withdrawal of its Administrative Petition for a set-aside relief amounted to giving up its right to be declared the winner in the competition. Since, in the view of the court, no proper explanation was given as to why the plaintiff had withdrawn its set-aside petition, the action for damages was due to be struck out.[28]

tended to agree with the mentioned *obiter dictum* on the requirement to pursue a set-aside relief prior to lodging an Administrative Action for lost profits, however she decided that this requirement should not be applied as a "stringent rule" The appeal was refused on the merits of the case.

[27] Administrative Action (Tel-Aviv-Yaffo) 106/07 Koach Otzma Ltd. *vs.* The State of Israel – Office of Prime Minister, Tak Mech 2008 (3) 9072 (27.8.2008).

[28] See also Administrative Action (Jerusalem) 12/01 Atir Ltd. *vs.* The State of Israel Tak-Mech 2008(4) 13329 (hereinafter: "Atir Ltd."). The judge in this case explained his judgment as follows : "According to this approach, the expectation from the plaintiff to exhaust her enforcement rights timely, prior to bringing an action for damages for lost profit, conforms with the public interest in general and with public procurement law in particular in all

As we will explain below, the requirement to lodge an Administrative Petition for set-aside of the contract award is a major cause for dissuading aggrieved bidders from bringing actions for the remedy of damages.

4. *The Requirement to Lodge an Administrative Petition as a Dissuading Factor from Bringing an Action for Damages*

It will rarely be possible to obtain damages for lost profits if the aggrieved bidder has failed to seek a set-aside relief prior to lodging an Administrative Action. This rule has the effect of imposing a quite heavy restriction on the practical option to pursue an action for damages in Israel. In order to understand this assertion, it is essential to first briefly examine the basic procedural rules governing the lodging of an Administrative Petition.

IV. Review of the Rules Governing Administrative Petitions and Interim Orders in Public Tenders

An aggrieved bidder who wants to file an administrative petition is likely to go through several trials and tribulations. According to the Administrative Courts Regulations (Procedure)[29] an Administrative Petition has to be lodged with the court within 45 days from the date that the contested decision of the procuring authority was published.[30] However, even a petitioner who lodges an Administrative Petition within this statutory period still runs the risk of his petition being struck out without being reviewed on its merits if the court finds that in the circumstances of the case the petition was lodged in delay.[31]

In order to prevent the contract from being awarded and performed by the winning bidder, and thus becoming a fait accompli, the petitioner will

aspects concerning public efficiency, taxpayers' money saving, and the interest of certainty and stability in public activities. Aggrieved bidder's option to wait on the side, that is, to "sit on the fence" while the public authority proceeds to the conclusion and performance of a contractual relationship with the winner in the public tender, and then brings an action for loss of profits only at a later stage, is unreasonable and leads to harsh results. It has, therefore, been ruled more than once, that damages for lost profit should be used as a residual remedy only, in exceptional circumstances whereby it is not possible anymore to bring legal proceedings aimed at declaring the plaintiff as the winner in the tender, or where it is not possible anymore to set aside the tender, particularly in situations of "fait accompli" which are not a result of the plaintiff's conduct" (Atir Ltd., p. 13341).

29 R. 3 of Administrative Court Regulations (Procedure), 2000.

30 Alternatively, the Administrative Petition has to be presented within 45 days of when the contested decision was presented to the petitioner or from the date when it was known to him.

31 R. 4 of the Administrative Court Regulations (Procedure).

normally lodge a petition for an interim order.[32] Such a petition may be rejected without reference to its merits if the court considers it right to do so. Alternatively, the court may also order the respondent to present its response to the petition and summon the parties to a hearing before the court.

The court may also make a ruling on the basis of the parties' written arguments only, without a hearing at court. If the court considers that irreparable damage may be inflicted on the petitioner until its ruling on the merits of the interim order is given, it may grant an ex parte provisional injunction and summon the parties to a court hearing within 10 days of the grant of this injunction.[33] Even if an inter parties hearing is conducted, cross examination of witnesses is very time limited or entirely barred. Therefore, at this very stage, aggrieved bidders' chances to bring evidence on impropriety (and obtain an interim relief) are extremely limited since they mainly rely on oral arguments and written documents, making it easy for the respondents to fend off allegations of improprieties.

A court granting an interim order may, upon its discretion, require the petitioner to provide a guarantee. The purpose of such guarantee is to secure compensation to the respondent for damages that may be caused to him as a result of the interim order, should the court eventually reach the conclusion that it was unjustified. In practice, petitioners are required to provide both a written undertaking in damages (thereby agreeing to fully compensate the respondent) and a bank guarantee at the amount deemed appropriate by the court. The guarantee requirement is normally a substantial financial burden on the petitioner considering that not only has the contract not been awarded to him, but he is also required to finance an expensive bank guarantee for the full duration of the provisional or interim injunction, (the length of which is hard to foresee at the time).

This is not the only heavy financial burden imposed on the petitioner who seeks to enforce his rights through a set-aside relief. According to a recent Israeli Supreme Court decision, a petitioner seeking a set-aside remedy in which he asks to be declared the winner of a tender, is required to maintain a valid bank guarantee throughout the trial proceedings in order to secure the performance of his commitments should he succeed.[34],[35] Additionally, the

[32] R. 9 of the Administrative Court Regulations (Procedure).

[33] R. 9 of the Administrative Court Regulations (Procedure).

[34] A Civil Appeal 7699/00 Tamgash Management Company *vs*. Kishon Drainage Authority Tak-Al 2000(3) 419.

[35] Bidders in Israeli public tenders are normally required to submit, together with their bids, a bank guarantee at a fixed amount for a fixed percentage of the value of their offers.

petitioner will also incur attorney fees, which are often very high, and other expenses ordinarily associated with the handling of a trial.[36]

What are the conditions that have to be fulfilled for a court to be willing to issue an interim order against the implementation of a contract award? First, the aggrieved supplier must show an arguable cause of action against the procuring agency. Secondly, he must convince the court that, on the balance of convenience, the harm that may be caused to him if relief is refused is greater than the damage to be inflicted upon the respondents (that is, both the winning supplier and the procuring entity) should the requested relief be granted.[37] Thirdly, even if the balance of convenience supports the petitioner's interests, the court will still consider if there are any relevant overriding public policy considerations that weigh against granting the requested relief. Frequently, courts refuse to grant interim orders on public interest grounds.[38] As a matter of fact the vast majority of petitions for interim orders in public tenders are denied. Fourthly, courts will also consider whether perhaps compensation is a more appropriate remedy in the case at hand than a set-aside injunction. This last consideration is often heavily relied upon by the courts in support of a refusal on their part to grant an interim order,[39] thus indicating that the petitioner ought to file an action for damages instead. However, as mentioned, at this interim stage of the proceedings, cross examination of witnesses is extremely limited (if allowed at all) and document disclosure procedures are still not available. It is, therefore, hard to see how, at this condensed stage of trial proceedings, the court can rule on the appropriateness of an action for damages.

Whilst bringing an Administrative Petition is, by no means, inexpensive, chances for success in such legal proceeding are rather small, as most of these petitions are denied. The cumulative effect of the obstacles described above, namely the high legal expenses coupled with a low chance of success, create a deterring effect against the filing of an Administrative Petition. Furthermore, failure to obtain an interim order would under normal circumstances mean that the contract will be awarded to the winner. By the

The bank guarantee can be invoked against the bank if the bidder is declared the winner, but for some reason refuses to sign the contract.

[36] Such as court fees, expert fees etc.

[37] Petition for an Approval to Lodge an Appeal no. 1557/02 Megamart Sport Equipment Ltd. *vs*. The State of Israel – Ministry of Defense Tak-Al 2002(2) 1807, 1808 (2002).

[38] See e.g., An Appeal on an Administrative Action no. 2803/06 Meyer and Sons Ltd. *vs*. HaGichon Water Factory and Drainage Jerusalem Ltd. Tak-Al (2)2006 235.

[39] A Petition for an Approval to Lodge an Appeal no. 7306/07 D.N. Kol Gader Ltd *vs*. Local County Council Eshkol (19.10.2007).

time the court will reach its final decision on the merits of the Administrative Petition (and presumably, even prior to that stage), the project for which the tender was carried out, will be deemed as a "fait accompli". Nevertheless, an aggrieved bidder who as a result of these obstacles chooses not to fully pursue an Administrative Petition for a set-aside relief, even in a case where the contract has already been awarded and performed, runs the risk of being barred from suing damages. Not only that, but also the limitation period which normally applies to ordinary civil claims (7 years) does not apply in respect to Administrative Actions – such action must be brought "in real time"[40] as the Administrative Court of Jerusalem has held lately.[41]

Only very few aggrieved bidders will be convinced to conduct an expensive trial with very low prospects of winning. So much less will they agree to conduct an expensive trial to try to obtain an interim order just for the sake of later being legally entitled to lodge an action for damages, especially considering that the chances of success in such an action are inherently vague, not to mention the poor prospects of obtaining damages for lost profits, and the requirement to take action without delay.

The reason for requiring an aggrieved bidder to seek a set-aside relief prior to bringing an action for damages —.i.e. to avoid the risk of a procuring authority paying more than once for the same project— can indeed be understood on some public policy grounds. There are, however other, more important, public policy considerations, such as the need to ensure prudence and probity in public procurement, that have been compromised as a result of these stringent conditions imposed on the right to sue for damages. We shall therefore propose below a reform of the rules applying to damages in public procurement so as to make them much more effective in providing remedies to aggrieved bidders on the one hand, and in creating positive deterrence against infringements of the procurement rules, on the other hand.

V. General overview of the damages remedy for infringement of the EU public procurement rules

In order to obtain a comparative perspective on the issue at hand, we turn now to the legal situation in the European Union (EU). The rules gov-

[40] I.e., it should be brought in close proximity to the delivery of the arguably wrongful decision by the procuring agency.

[41] Administrative Action (Jerusalem) 202/05 T.V Three Ltd, *vs*. The Second Television and Radio Broadcasting Authority Tak-Mach (1)2007, 9805, 9809.

erning the damages remedy for breach of the EU public procurement rules are governed by the Remedies Directives.[42] Article 2 of Directive 89/665/EEC provides:

> "1. The Member States shall ensure that the measures taken concerning the review procedures specified in Article 1 include provision for powers to:
>
> …
>
> (c) Award damages to persons harmed by an infringement….
>
> …
>
> 5. The Member States may provide that where damages are claimed on the grounds that a decision was taken unlawfully, the contested decision must first be set-aside by a body having the necessary powers".

Similar provisions are found in Article 2 of Directive 92/13/EEC.[43]

Thus, the Remedies Directives provide only very general and superficial guidelines on the rules that are to govern the award of damages for aggrieved bidders. This could be seen to imply that the potential deterring effect of such remedy against infringement of EU public procurement rules has not been given much weight. Indeed, these provisions have been criticized by legal commentators.

Treumer argues that, while the Remedies Directives set the basic rule that review bodies must be able to award damages to persons injured by the infringement of the EU procurement rules, the details of the issues concerning damages are not regulated in detail and their formulation does not contribute to the creation of a clear legal situation.[44] He further argues that it is not even clear from the Directives whether they require the award of

[42] Council Directive 89/665/EEC of 21 December 1989 on the coordination of the laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts (hereinafter the "Public Procurement Remedies Directive") and Council Directive 92/13/EEC of 25 February 1992 coordinating the laws, regulations and administrative provisions relating to the application of Community rules on the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors (hereinafter "Public Utilities Remedies Directive"). On December 11, 2007 the European Parliament adopted a new Directive amending the Public Procurement and Public Utilities Remedies Directives (Directive 2007/66/EC of the European Parliament and of the Council). However, the new Directive did not make any changes to the damages remedy.

[43] The provisions of these two Remedies Directives are not fully identical. However a discussion of the differences between them is outside the scope of this paper.

[44] Steen Treumer "Damages for Breach of the EC Public Procurement Rules – Changes in European Regulation and Practice" P.P.L.R. 2006(4) 159-170, at p.161 (hereinafter "Treumer").

lost profits or not, which is, in Treumer's view, of crucial importance for the efficiency of the remedy of damages.[45] Likewise, Pachnou argues that *Directive 89/665/EEC* does not give any guidelines on the conditions and extent of the damage remedy while such matters are left for the discretion of Member States.[46] It is "not unusual" in Member States, according to Pachnou, to impose a stringent burden of proof on the plaintiff: some Member States require the plaintiff to prove that it would have won the contract in order to be granted compensation for lost profits. Such a requirement, she asserts, is onerous to a degree that it paralyses the operation of the remedy for damages.[47]

Another usual problem, according to Pachnou, is the quantum of damages. While, the recovery of costs is usually covered in most Member States, the question of damages for lost profits is "less certain".[48] A further serious critique of Pachnou relates to the Remedies Directives provisions which

[45] *Ibidem*, p. 170.

[46] Despina Pachnou The Effectiveness of Bidder Remedies for Enforcing the EC Public Procurement Rules: A Case Study of the Public Works Sector in the United Kingdom and Greece. Thesis submitted to the University of Nottingham for the Degree of Doctor of Philosophy, March 2003, p. 84.

[47] *Ibidem*, p. 85. Under the law of England and Wales an aggrieved bidder is required to show high probability, almost a certainty that he would have been successful had the relevant laws not been infringed. See: Despina Pachnou "Bidder Remedies to Enforce the EC Procurement Rules in England and Wales" P.P.P.L.R. 2003(1) 35-64, 57-61. Under German law, apparently, no loss of profit can be claimed for failure to award a contract since as a consequence of the principle of contractual freedom, under normal circumstances no legal obligation lies on a procuring authority to award a contract to a bidder, even if there is no valid reason for not wanting to award the contract to him. Damages for loss of profits can be obtained where an aggrieved bidder can prove that he submitted the most advantageous bid, but the contract was awarded to another bidder. Thus, damages for loss of profits may not be available where the tender was cancelled. The bidder further has to show that the contract would have been awarded to him had it not been for the infringement claimed. See Anne Rubach-Larsen "Damages Under German Law for Infringement of EU Procurement Law" P.P.L.R. 2006 (4) 179-194, 188-190. Under French law, in order to obtain damages for loss of profit an aggrieved bidder must convince the court that he has a very serious or a serious chance of winning the contract. See Francois Lichere "Damages for Violation of the EC Procurement Rules in France" P.P.P.L. 2006(4) 171-178, 174-176. It is to be noted, that despite the relatively difficult level of proof required ("very serious" or "serious" chance), it is claimed that as of 2006 in 30 cases out of 53, French courts concluded that there was a serious chance or a very serious chance of winning. *Ibidem*, p. 173. Under Swedish law, an aggrieved bidder has to prove that there is a proper causal link between the infringement and the loss of profits. She is also required to show that she has made a reasonable effort to minimize her losses: See Michael Slavicek "Damages for Breach of the EC Public Procurement Rules in Sweden" P.P.P.L., 2006(4) 223-240, p. 239-240 (hereinafter: "Slavicek").

[48] Supra note 47, p.85.

enable Member States to require aggrieved bidders to ask for a set-aside remedy before lodging an action for damages[49] (similar to the obiter dictum of the Israeli Broadcasting Authority judgment).[50] This requirement, Pachnou argues, increases the legal expenses incurred by an aggrieved bidder in the process of seeking compensation. Furthermore, it makes the admission of an action in damages dependent on the success of the application to set aside.[51] It is claimed that at least one Member State requires aggrieved bidders to prove some degree of bad faith on behalf of the procuring authority in order to determine the quantum of damages.[52]

In most Member States, compensation tends to be relatively low; only in very few cases have plaintiffs been successful in obtaining damages for lost profits.[53] The rules governing the action for damages in Israel and the corresponding rules in EU Member States, while not identical, share some general common features. Actions for damages are severely restricted by the requirement for a strict causal link, chances for success are not impressive and compensation awards are low. And the requirement that an aggrieved bidder first seek a set-aside order before lodging an action for damages, can be found both in Israel and in at least some of the EU Member States. Generally speaking it may be concluded that the damages remedy in Israel as well as in the EU is hard to obtain, and therefore has no real deterring effect again improprieties in public tenders.

VI. Factors dissuading aggrieved bidders from lodging actions for damages in EU member states

A study conducted by the European Commission, found three main factors that are seen as responsible for discouraging aggrieved bidders from lodging actions for damages in the EU. First, it was found that actions for damages are perceived by EU bidders as remedies lacking real corrective

[49] See above.

[50] Supra, note 23.

[51] Failure to comply with the above procedural requirement will cause the action for damages to be rejected and will preclude the aggrieved bidder from obtaining compensation. Supra note 47, p.87-88.

[52] It would seem that under Swedish law, the quantum of damages is determined in relation to the severity of the infringement by the procuring authority (Slavicek, supra note 48, p. 239). Cf. The European Court of Justice decision in C-275/03, Commission v. Portugal, where it was decided that it was a violation of the Remedies Directive to make damages conditional on proof of intentional or negligent breach (cited in Treumer, supra note 45, p. 161, fn 24.)

[53] Slavicek supra note 48.

effect. That is, even if an action for damages is successful, the bidder will still not be awarded the contract. In the bidders' view this would mean an unwelcome compromise regarding their future business with the procuring authorities. Second, actions for damages are hindered by practical difficulties. Hence chances for winning such an action are viewed as extremely low. These very low chances are attributed to the requirement to prove a causal link as a condition for obtaining lost profits. Third, it was found that, actions for damages tend to be lengthy and costly. Litigation and legal costs are sometimes higher than what can be expected to be awarded for costs incurred in bidding for the contract.[54] A closer look into the consultation papers on which the above study was based, reveals that in addition to the above considerations, aggrieved bidders are also dissuaded from bringing actions for damages because of the obligation under their national legal system "to obtain beforehand the annulment or the declaration of illegality of the contested decision made by the contracting authority".[55] In addition, in another study, conducted by Pachnou, there seems to be strong evidence that bidders are deterred from enforcing their rights against infringing procuring authorities because of fear of being blacklisted by them[56]. No doubt, the combined effect of the practical difficulties inherent in actions for damages, low chances of success, high costs and lengthy processes, coupled with the bidders' fear of retaliation, has a powerful discouraging effect from lodging actions for damages.

VII. Proposals for change

1. *The problems with the current situation*

The situation described above, both in the EU and in Israel, where aggrieved bidders are largely dissuaded from lodging actions for damages even

[54] Commission Staff Working Document *annex to the* proposal for a directive of the European Parliament and of the Council amending Council Directives 89/665/EEC and 92/13/EEC CEE with regard to improving the effectiveness of review procedures concerning the award of public contracts (presented by the Commission COM(2006) 195) Impact Assessment Report – Remedies in the Field of Public Procurement, 12-13. The surveys on which the above Impact Report was based can be found on the EU's website.

[55] The consultation results reveal that this obligation is claimed by the consultees (EU economic operators, lawyers, professional associations and non-governmental organizations) to be one of the causes for their reluctance to bring actions for damages – and where such actions were indeed brought: one of the reasons for their relative lack of success (*idem*).

[56] Despina Pachnou "Bidders' Use of Mechanisms to Enforce EC Procurement Law" P.P.L.R., 2005(5) 256-263, p. 258.

when procurement rules have been violated and where irregularities in the tendering process have occurred, is a troubling one. If one adds to that our observation that often also the alternative remedy of administrative petitions to set-aside wrongful decisions is not an effective remedy —because of the procedural and financial obstacles facing a petitioner and since often the contract is already a "fait accompli"[57]— it would seem that we have here a systemic lack of deterrence against infringements of the procurement rules. In other words, this system of judicial supervision over the procurement process is not a very effective tool in ensuring compliance with the rules. Nor is it doing a good job in ensuring confidence on the part of potential suppliers in the system, as is evident from the EU survey mentioned above.

If these conclusions are correct, we may have here a significant welfare loss resulting mainly from two sources: 1. Abuse of the procurement rules which lead to inefficient use of public funds: government agencies are not getting the best value for our tax dollars; 2. Lack of confidence by potential suppliers in the integrity of the procurement system prevent their participation in public tenders. This means that potential Pareto optimal contracts between such suppliers and the government are lost, competition for government contracts decreases and the arena is left open to those suppliers that know how to manipulate or bribe procurement officers to act in their interest.

2. *The importance of an effective remedy of damages*

We are also not convinced by the argument raised by the courts that to award damages, in particular expectation damages, means to force the pro-

[57] It may be argued that the implementation of the new Remedies Directive (2007/66/EC) by the EU Member States will result in less tenders becoming a "*fait accompli*" since now all EU Member States must allow for a mandatory 10 days "standstill" period after award of a contract, wherein the contract may not be signed. During the "standstill" period aggrieved bidders may seek for review of the award decision and apply for an interim remedy for the duration of the trial, in order to prevent the contract from being concluded. Although, undoubtedly, the "standstill" period may indeed prevent tenders from becoming a "*fait accompli*" before aggrieved bidders manage to bring their legal challenges before the courts, it still does not guarantee a successful application for an interim order. Interim order applications may still be denied on public policy grounds and on other grounds, (such as the balance of convenience test, etcetera). Thus, failing to obtain an interim order may, even under the new regime result in the contracts becoming concluded, which leaves the aggrieved bidder with the sole option of bringing an action for damages.

This suggests therefore, that the action for damages has not lost its importance as a potential deterring tool against infringement of public procurement laws, although, to some extent, it may become less abundant. Israeli Public Procurement Law, however, does not impose a "standstill" period on procuring authorities, as detailed above.

curing agency to "pay twice" for the product. This is in our opinion nothing but rhetoric, because the agency is not really paying twice. It pays only once for the product or service that it has chosen. However, if it has bluntly violated the procurement rules and hence caused damage to bidders who participated in the tender in good faith (expecting the government agency to abide by its own rules), it is only fair and prudent that it should compensate such bidders for the damage it has inflicted.

In fact, payment of damages for infringement of procurement rules serves three main purposes:

1. To compensate the bidder for the losses it has unjustly suffered as a result of the infringement of the procurement rules. This is in essence a deontological corrective justice rationale, based on the moral bindingness of the procuring agency's declared commitment to respect these rules and of its legal obligation to respect the law. This created a legitimate expectation on the part of the bidder that indeed the rules will be respected and this expectation ought to be protected. This rationale is somewhat similar to the moral justification for compensation for torts committed or for contracts breached;[58]

2. To restore the confidence of the aggrieved bidder in the procurement system, so that it and other potential bidders will continue to participate in government tenders. This is a utilitarian rationale similar to those found in the literature on remedies for breach of contracts;[59] and

3. To create a deterrent effect on procuring agencies that will improve future adherence to the rules.[60] This too is a utilitarian rationale similar to those found in the literature on tort law and criminal law in connection with the objective of deterrence.[61] The courts are absolutely right in asserting

[58] See e.g. Fried, *Contract as promise* (1986); Ernest J. Weinrib, *The idea of private law*, 50-53, 136-140 (1995); Izhak Englard, *The philosophy of tort law* (1993), ch. 1-6; Andrew Burrows, *Remedies for torts and breach of contract*, 3rd. ed., 2004, pp. 34-44. For a discussion of the corrective justice rationale in the realm of tort as well as in contract law, see also: Curtis Bridgeman "Notes: Corrective Justice in Contract Law: Is there a case for Punitive Damages?" 56 *Vanderbilt Law Review*, 2003, 237.

[59] Lon L. Fuller and William R. Perdue, "The Reliance Interest in Contract Damages", 46 *Yale Law Journal* 52 and 373, 1936-37; Richard Posner, *Economic analysis of law*, 6th. ed., 2003, ch. 4.

[60] See Arie Reich, *International Public Procurement Law: The Evolution of International Regimes on Public Purchasing* (Kluwer Law International, 1999), pp. 336-340.

[61] See for instance Glanville Williams, "The Aims of the Law of Tort", 4 *Current Legal Problems* 137, 1951, at pp. 144-151; Salmond, *Law of Torts*, 7th. ed., 1928, pp. 11-12. The deterrence objective was adopted and rejuvenated by the Law & Economics movement, such as in the writings of Guido Calabresi, "The Costs of Accidents: A Legal and Economic Analysis",

that government agencies have limited budgets, and that payment of damages are a burden on them. But precisely for that reason such damages will serve as a deterrent against violating the rules and against awarding government contracts to undeserving bidders. Such imposition is also bound to cause a stir in the agency and to prompt it to investigate the actions and motives of the officers that were involved in such ill-fated procurements. One could expect this to help in preventing further infringements in the future.

Having said that, we do however recognize a potential problem where rules are ambivalent or where we deal with technical violations performed in good faith or by mistake. Given the complexity of the procurement rules, a procurement officer may make an error in the handling of a tender without any bad intentions. Also the procuring agency may have been convinced that it took the right decision, but the court may think otherwise. Here the objectives set out above do not necessary mandate the award of high damages. There is less of a need to deter the procuring agency if it did not act in a reprehensible way, and the damage award is less likely to bring about any specific change in future behavior. The corrective justice justification for the award is also less pertinent. Therefore, we can understand why some courts require bad faith on the part of the procuring agency before it awards damages. However, it would not be right to be too stringent on this requirement, since to prove bad faith is not an easy task. To impose on an aggrieved bidder a strict burden of proof in relation to the state of mind of procuring officers whom he may not even know, and on the dealings of which he has very little information, is likely to serve as an insurmountable obstacle for many damages actions. Instead, the courts should decide about the severity of the violations from the objective, not subjective, circumstances of the case, in order to make sure that it imposes expectation damages only in cases of clear and blunt violations of the procurement rules, i.e., such violations that ought to be deterred.

3. *Damages Based on the Aggrieved Bidder's Loss of Chance*

After having established the important functions of the remedy of damages in public procurement and the need to preserve its effectiveness, we need to discuss the question of which type of damages? When should a court award expectation damages, i.e., compensation for loss of expected

Yale University Press, 1970, and Richard Posner's, e.g. William M. Landes and Richard Posner, "The Economic Structure of Tort Law", Cambridge, *Mass. Harvard Univ. Press*, 1987.

profits from the government contract? And when should it limit its award to reliance damages, i.e., compensation for the expenses incurred in connection with the preparation of the bid and participation in the tendering process.

We believe that in order to preserve the deterrent effect of damages, and pursuant to the other objectives of this remedy, an aggrieved bidder should in principle be entitled to expectation damages, whenever she can show that she had a real chance of winning the contract, but for the infringement. However, under the law as it stands now the requirement to prove causation is a major obstacle for the success of any action for damages.[62] To prove a proper causal link between the procuring authority's infringement and lost profits from the contract — i.e., that but for the infringement the plaintiff would most likely have won the contract — is rarely possible.[63] Therefore strict adherence to the causation requirement where an infringement has occurred in the tendering process means a weakened level of private enforcement of public procurement law. Such a situation may lead to underdeterrence, which could in turn, result in a low adherence to public procurement rules by procuring authorities (as well as bidders). Nevertheless, the contrary argument is that loosening the causation requirement may lead to an adverse situation. This may lead to a flood of opportunistic and frivolous actions, which will make the entire public tender process more cumbersome and expensive not only for the relevant procuring authorities but also and particularly for the taxpayer, for whom the public tender is performed.

In the authors' view, a compromise-solution should be adopted between a total relaxation of the causation requirement and between strict adherence to it. Such a compromise may obtain both deterrence and prevent the risk of many frivolous actions. We therefore propose that, an aggrieved bidder will be required to prove only a material infringement of

[62] See for instance J.M. Fernandez, "Recent Cases of the Court of Justice Relevant to Public Procurement", 6 *P.P.L.R.*, Issue 5, CS p.141, 1997, who writes (at pp. CS 149-150): "It is unlikely that complainants can overcome the obstacle of proving a better right to the contract, especially with regard to those contracts awarded pursuant to the most economically advantageous offer, which, according to statistics, by far outweighs the lowest price criterion. As for the bidders, it is a well known fact that the supply of such evidence is an almost insurmountable obstacle in public procurement cases, unless the award is made on the basis of the lowest offer criterion. National experiences and case law on the matter largely supports this conclusion".

[63] This may be attributed to the special particularities of the public tender and also to evidence law as practiced in Israel and in other jurisdictions.

public procurement law in order to be entitled to compensation for lost profits. However, quantification of the damages will depend on an assessment of the plaintiff's chances to have won the contract but for the material infringement of the rules. In other words, under the new regime proposed, the aggrieved bidder will no longer have to prove, that but for the alleged infringement he would have won the competition. Rather, he will have to prove that a material infringement has occurred in the tender process and that in itself ought to make him eligible for damages. The amount of the damages will depend on the chance he had of winning the contract, but for the infringement. If, for instance, the court arrives at the conclusion that he had a 50% chance of winning the contract, instead of the suit being dismissed because of failure to meet the required standard of proof (preponderance of evidence), he will be entitled to damages at the amount of 50% of his expected profits from the contract. Likewise, if he proved a 33% chance, he will be entitled to 33% of these profits, and so on. The quantification of damages will, therefore, rely on the degree of chances lost by the aggrieved bidder as a result of the alleged infringement, multiplied by the amount of her expected profit.[64] A similar approach has been proposed by several scholars in the field of torts[65] and adopted to some extent by the Israeli Supreme Court.[66]

4. *Reversal of the Burden on Proo*

In the authors' view, relaxing the causal link requirement as explained above, is still insufficient to transform the damages remedy to a deterrent one. Proving a loss of a chance to win the tender competition may still be difficult for aggrieved bidders, the reason being that most of the information regarding the tender process is kept in the hands of the procuring authority, making it extremely difficult for an aggrieved bidder to prove the degree of these lost chances. Furthermore, proving the chances lost to a bidder will often require the court to make a thorough study of the winning chances of all the qualified bidders in the same tender. The procuring authority is, in this case, the most efficient party to prove the bidders' chance

64 See also Omer Dekel, *Public Tenders*, 2006, Hebrew, part B., p. 326-328.

65 See for instance, Ariel Porat and Alex Stein, "Tort Liability under Uncertainty", Oxford University Press, 2001.

66 For instance: C.A. 231/84 *Kupat Cholim vs. Fatach* PD 42(3)312; and C.A. 7375/02 *Carmel Hospital vs. Malul* PD 60(1)11. The last decision was lately overturned by a 5-4 majority of the Supreme Court in a reconsideration hearing SCH 4693/05 *Carmel Hospital vs. Malul.*

of winning the competition and to present all the necessary factual background information to the court.[67]

It is, therefore, proposed, that whenever an aggrieved bidder is successful in showing a material breach of the relevant laws, the burden of proof regarding the degree of chance lost by him (which is essential for the damages quantification) will shift to the procuring agency.[68] The point of departure for the court will be that the aggrieved bidder is entitled to 100% of the lost profits, unless the procuring agency discharges its burden of proof and convinces the court that this bidder's chances of winning was lower. In such a case, the bidder will receive the percentage of the expected profits that the court has been convinced better reflects his actual chances of winning.

5. *Damages for bid preparation and participation costs upon proof of a material infringement*

In certain cases the procuring agency will be able to prove that the aggrieved bidder did not have any chance whatsoever to win the contract, or that his chances were so low that the compensation for lost profits will not cover the expenses caused to the bidder in preparing the bid and in participating in the tendering process.

In such a case, we propose that the aggrieved bidder, who has proven a material infringement, will be able to recover, as a minimum, the full costs he incurred in preparation of the bid and in participating in the tender.

VIII. Conclusion

As discussed above, actions for damages in public tenders can serve as an important deterrent against improprieties in the public tendering process and against infringements of public procurement law in general. Nevertheless, Israeli law and some of the EU Member States have failed to fully recognize the importance of the damages remedy and have cre-

[67] This view is particularly true when only one or a few of the qualified bidders in a tender decide to bring an action for damages, whereas others decide to refrain from such an action even though, they may be entitled to damages.

[68] A proposal to shift the burden of proof from aggrieved bidders to procuring authorities was already made in Reich, supra note 61 on p. 338, and is mentioned in the Thesis paper of Despina Pachnou, p. 122, fn. 215, citing Prof. Sue Arrowsmith in her book: *The Law of Public and Utilities Procurement*, 1996. Here we develop the proposal to combine it with the doctrine of proportional damages based on the chances of having won the contract.

ated unnecessary obstacles on aggrieved bidders' track to obtain damages for profit they lost as a result of infringements of the law - possibly out of fear of forcing the taxpayer to pay more than once for the same project.

This paper proposes to transform the damages remedy to a more deterrent instrument that will contribute to the fight against corruption and misconduct in public procurement. The proposal suggests doing so by getting rid of the unnecessary procedural obstacles to actions for damages. An aggrieved bidder should not be required to first submit and exhaust a set-aside petition, before being allowed to sue for damages. In fact, we see no reason to require such a bidder to divide his requested remedies into two separate legal actions. As in most other fields of law, an aggrieved bidder should be allowed to sue in the alternative for an injunction to correct the infringement or damages if such correction is denied for whatever reason.

As for the action for damages, once a material infringement has been proven by the aggrieved bidder, the burden of proof to show that he had no chance of winning the contract should lie with the procuring authority. We further propose that expectation damages be the rule, and that they be calculated on the basis of the degree of chance lost as a result of the infringement. Here too, we propose to place the burden of proof on the procuring entity, which has access to the pertinent information in this regard. In addition to that, in any case of material infringement, damages will not be less than full bid preparation and participation costs.

Arguably, the proposed solution will need to be further elaborated in order for it to adjust to each and every jurisdiction and legal system. However, in the authors' opinion, from a general perspective, the proposed solution presents an improvement to the current rules governing the damages remedy in Israel and in some of the EU Member States, and if adopted will yield more deterrence and adherence to the public tendering rules of the said jurisdictions, provide more just remedies to aggrieved bidders and contribute to the public confidence in the government procurement system..

CESL AND CISG

Ingeborg SCHWENZER*

SUMMARY: I. *Introduction.* II. *Scope of application.* III. *The Tension Between Certainty and Fairness.* IV. *Amended rules.* V. *Filling the gaps.* VI. *Codifying style and techniques.* VII. *Conclusion.*

I. INTRODUCTION

On 11 October 2011, the European Commission published the Proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law. This Common European Sales Law[1] —CESL— is based on the Draft Common Frame of Reference (DCFR),[2] which in turn drew heavily on the Principles of European Contract Law (PECL).[3] CESL contains provisions on contract formation, contract interpretation including unfair contract terms and —as its core part— obligations and remedies of the parties to a sales contract.[4] Furthermore, provisions on damages and interest, restitution as well as prescription can be found. Thus, the sphere of application of the CESL is more or less identical with the UN Convention on

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1 The CESL forms Annex I of the Regulation. After the publication of the Proposal, the European authorities received reasoned opinions from the Austrian Federal Council, the Belgian Senate, the German Bundestag and the United Kingdom House of Commons, respectively, objecting to CESL on the grounds that it infringed the subsidiarity principle. The threshold for an automatic review of the draft was, however, not met (*see http://www.ipex.eu/IPEXL-WEB/dossier/dossier.do?code=COD&year=2011&number=0284&appLng=EN*).

2 Von Bar, C. *et al.* (eds.), *Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference (DCFR)*, Sellier European Law Publishers, Munich, 2009.

3 Principles of European Contract Law (PECL) (1999), available at *http://frontpage.cbs.dk/law/commission_on_european_contract_law/PECL%20engelsk/engelsk_partI_og_II.htm*.

4 For a general overview of CESL *see* D. Staudenmayer, 'Der Kommissionsvorschlag für eine Verordnung zum Gemeinsamen Europäischen Kaufrecht', *NJW*, Vol. 64, 2011, pp. 3491 *et seq*.

Contracts for the International Sale of Goods (CISG) with the exception of unfair contract terms. The CISG now has 78 member states and is by far the most successful[5] international private law convention worldwide along with its sister UN Convention on Limitation.[6]

This paper will first compare the approach and main solutions of the two instruments. It will discuss whether the CESL has improved the solutions already found in the CISG and whether the gaps that still exist in the CISG have been filled in an acceptable way. It will then discuss whether such regional unification alongside the global unification of sales law seems at all desirable and what the prospects of such an optional instrument on the European level might be in practice.

II. Scope of application

Let me first address the scope of application of the two instruments.

1. *Opt in vs. opt out*

The first difference between the CESL and the CISG pertains to the mechanism of how and when the respective instruments apply.

Whereas the CISG automatically applies if the prerequisites of its Art. 1 CISG —both parties having their places of business in Contracting States, or the rules of private international law leading to the application of the law of a Contracting State— are met, the CESL is optional, *i.e.* the choice of the CESL requires an agreement of the parties to that effect. If the parties choose the CESL, the choice covers the CESL as a whole, and not only parts of it.[7] At the same time, the drafters of the CESL consider the choice of CESL as implying an agreement of the contractual parties to exclude the CISG should it otherwise apply.[8] Whether such a disposition can be ordered by the European authorities seems at least very doubtful, as the question whether the parties validly opted out from the CISG is entirely to be decided autonomously under the CISG itself.[9]

5 *See* Schwenzer, I. and Hachem, P., "The CISG – A Story of Worldwide Success", *in* Kleinemann J. (Ed.), *CISG Part II Conference*, Iustus, Uppsala, 2009, p. 140.

6 UN Convention on the Limitation Period in the International Sale of Goods of 14 June 1974.

7 *See* Proposal, Para. 24.

8 *See* Proposal, Para. 25.

9 *See* Schwenzer, I. and Hachem, P., *in* Schwenzer, I. (ed.), *Schlechtriem and Schwenzer, Commentary on the UN Convention on the International Sale of Goods (CISG)*, 3rd ed., Oxford University

2. *Sales of Goods Contracts Defined*

Both instruments govern sales of goods contracts. However, their respective scopes differ substantially.

The CISG does not define the term "goods" itself. Thus, the scope of this notion must be interpreted autonomously. From the very beginning, it has been highly debated whether the sale of software is governed by the CISG or not.[10] The now prevailing view holds that the CISG applies if software is permanently transferred to the buyer, irrespective of the mode in which the software is delivered, *e.g.* via disc or, as usually today, via the internet.[11] Thus, the CISG has been able to easily adjust to ever-changing modern electronic developments.

The CESL, in contrast, still defines goods as "*any tangible movable items*",[12] thus explicitly excluding software. This narrow and rather outdated definition of goods requires that, in addition to "sale of goods", the "supply of digital content" has to be mentioned separately in all relevant provisions.[13]

Another difference relates to so-called mixed contracts. In this respect, the CISG follows a rather pragmatic approach.

According to article 3(2) CISG, the CISG applies to a mixed contract if the supply of labour or other services does not form the preponderant part of the obligations. If the whole contract is governed by the CISG, its provisions also apply to the service part. Thus, a judge or arbitrator does not have to decide whether the fact that the goods do not live up to the contractual requirements results from their own features or from a possible breach of a service obligation.

Again, the approach taken by the CESL is different.[14] It only applies to so-called related services, *i.e.* any service related to the goods or digital con-

Press, Oxford, 2010, article 6, para. 4; *see also* Hesselink, M., "How to Opt into the Common European Sales Law? Brief Comments on the Commission's Proposal for a Regulation", *European Review of Private Law*, Vol. 20, 2012, p. 201.

[10] Schwenzer, I. and Hachem, P., *in* Schwenzer 2010, supra note 9, Art. 1, Para. 18.

[11] *Idem*; see also Kee, C., 'Rethinking the Common Law Definition of Goods', *in* Büchler, A. and Müller-Chen, M. (eds.), *Private Law, national —global— comparative*, *Festschrift für Ingeborg Schwenzer zum 60. Geburtstag*, Stämpfli, Bern, 2011, pp. 930 *et seq*.

[12] See article 2(h) Regulation.

[13] For the definition of digital content see article 2(j) Regulation; see further Feltkamp, R. and Vanbossele, F., "The Optional Common European Sales Law: Better Buyer's Remedies for Seller's Non-performance in Sales of Goods?", *European Review of Private Law*, Vol. 19, 2011, pp. 879 *et seq*.

[14] See *also* Micklitz, H. W. and Reich, N., "The Commission Proposal for a *Regulation on a Common European Sales Law* (*CESL*) – Too Broad or Not Broad Enough?", *in* Micklitz, H. W. and Reich, N. (eds.), *The Commission Proposal for a "Regulation on a Common European Sales*

tent such as installation, maintenance, repair or processing, but explicitly excludes training services[15] that ordinarily play an important role in more complex sales contracts on the international level.[16] Furthermore, even if the mixed contract is covered by the CESL, there is a distinct liability scheme for the breach of a service obligation. Whereas liability for breach of the delivery obligation under the CESL is strict, liability for breach of a service obligation depends on fault.[17] This means that the adjudicator faces the often unresolvable task of exactly attributing the consequences of non-conformity to the goods themselves or the services part of the contract.

3. *B2B and B2C Contracts*

In regard to the personal scope, the CISG is pretty straightforward: it is concerned with international B2B sales contracts, B2C transactions are practically excluded.[18]

Again, the approach taken by the CESL is different. The starting point is the cross-border European B2C sales contract, and indeed the whole instrument exudes the underlying policy of consumer protection, which is one of the main goals of unification of private law at the European level. The Explanatory Memorandum explicitly states that the Proposal "*is consistent with the objective of attaining a high level of consumer protection*"[19] The second aim is to help small or medium-sized enterprises (SME) to benefit more from opportunities offered by the internal market.[20] According to article 7 Regulation, the CESL may be used in B2B contracts only if at least one of the parties is a SME.[21] It remains an open question why the CESL, as an opting-in instrument, cannot be chosen by two commercial entities if neither qualifies as

Law (CESL)" – Too Broad or Not Broad Enough?, EUI Working Paper LAW 2012/04, European University Institute, San Domenico di Fiesole, 2012, pp. 12 *et seq*.

15 *See* article 2(m) Regulation; *see also* article 6 Regulation: exclusion of mixed-purpose contracts.

16 *See further* N. Reich, "An Optional Sales Law Instrument for European Business and Consumers?", *in* Micklitz, H. W. and Reich, N., *supra* note 14, 2012, pp. 85 *et seq*., p. 89: "The scope and content of part V on *Services related to a sales contract* seem to be incomplete, contradictory and will not provide legal certainty of cross-border B2C transactions (…)".

17 Article 148(2) CESL.

18 Article 2(a) CISG; see Schwenzer, I. and Hachem, P., *in* Schwenzer, *supra* note 9, 2010, article 2, paras. 4 *et seq*.

19 P. 6.

20 See Explanatory Memorandum, p. 7.

21 According to Art. 7(2) Regulation, a SME is a trader with less than 250 employees and an annual turnover not exceeding 50 million Euros.

a SME.[22] Furthermore, the CESL seems to assume that, in B2B sales contracts, the SME —like the consumer— is always on the side of the buyer, which certainly is not the case in reality.

4. *Subjects Covered*

As we all know, the CISG is only concerned with the formation of the contract, the rights and duties of the parties and the remedies in case of breach of contract. Issues of limitation of actions are covered by the CISG's sister UN Convention on the Limitation Period in the International Sale of Goods, which, however, has not gained wide approval. There are significant areas not covered by the CISG, especially validity issues.[23]

The CESL, in addition to the areas covered by the CISG and the Limitation Convention, fills some of the open or at least perceived gaps left by the CISG. Apart from the right to withdraw in B2C contracts,[24] it deals with mistake, fraud, threat and exploitation,[25] addresses unfair contract terms,[26] and prolifically regulates pre-contractual information duties.[27] Still, significant areas of general contract law are not covered by the CESL and thus are left to the otherwise applicable domestic law.[28]

III. The Tension Between Certainty and Fairness

One of the major problems each commercial contract law system has to face is the tension between certainty and predictability on the one side and

[22] However, the Member States may open the CESL for other parties than SME; see also Mankowski, P., "Der Vorschlag für ein Gemeinsames Europäisches Kaufrecht (CESL) ", *Internationales Handelsrecht*, Vol. 12, 2012, p. 3; Eidenmüller, H. *et al.*, "Der Vorschlag für eine Verordnung über ein Gemeinsames Europäisches Kaufrecht", *Juristen Zeitung*, Vol. 67, 2012, pp. 273 *et seq*.; Scottish Law Commission, 'An Optional Common European Sales Law: Advantages and Problems', November 2011, available at *http://lawcommission.justice.gov.uk/docs/Common_European_Sales_Law_Advice.pdf*, p. 88.

[23] Article 4, sentence 2(a) CISG; see in detail Schwenzer, I. and Hachem, P., *in* Schwenzer 2010, supra note 9, article 4, paras. 29 *et seq*.

[24] Articles 40-47 CESL.

[25] Articles 48-57 CESL; see on these issues Martens, A. E., "Die Regelung der Willensmängel im Vorschlag für eine Verordnung über ein Gemeinsames Europäisches Kaufrecht", *Archiv für die civilistische Praxis*, Vol. 211, 2011, pp. 845 *et seq*.

[26] Articles 82-86 CESL.

[27] Articles 13-22 CESL; see De Boeck, A., "B2B Information Duties in the Feasibility Study: Analysis of Article 23", *European Review of Private Law*, Vol. 19, 2011, pp. 790 *et seq*.

[28] For further criticism see Eidenmüller *et al.,* supra note 22, 2012, pp. 271 *et seq*.

fairness on the other side. Shall the parties be bound to what they agreed or shall the adjudicator be granted the power to interfere with their agreement on grounds of fairness and conscionability? Already in 1598, Shakespeare put this question in the centre of his play "The merchant of Venice". Is Antonio bound to his promise of "a pound of flesh" in case of not being able to repay the loan or is this an unfair contract term to be disregarded under the circumstances?[29]

It is one of the most salient features of English commercial law that it strongly favours certainty over fairness whereas many civil law legal systems tend to rely on notions of good faith and fair dealing. It was against this background that in the CISG "*the observance of good faith in international trade*" was only inserted in article 7(1) CISG as one criterion among others to be taken into consideration in interpreting the Convention. However, the drafters of the CISG explicitly decided against any provision imposing a duty of good faith on the parties themselves. Thus, in particular, the German notion of *Treu und Glauben* cannot be applied under the CISG although German courts and authors seem to sometimes disregard this fact.[30] By contrast, the CESL explicitly states that each party has a duty to act in accordance with good faith and fair dealing.[31] Any breach of this duty may not only preclude the breaching party from exercising or relying on a right, remedy or defence which it would otherwise have but may in and of itself give rise to liability for any loss thereby caused to the other party.[32] This far reaching principle is hardly reconcilable with the necessity of certainty and predictability in commercial transactions and thus will certainly not be acceptable at least to most Common Law lawyers.[33]

IV. Amended rules

Let us now turn to some core areas of any sales legislation where the CESL chose to deviate from the CISG.

[29] See Scottish Law Commission, *supra* note 22, 2011, p. 106.

[30] See Schwenzer I. and Hachem, P., *in* Schwenzer, supra note 9, 2010, Art. 7, Para. 17.

[31] Article 2(1) CESL.

[32] Article 2(2) CESL.

[33] See Scottish Law Commission, supra note 22, 2011, pp. 106 *et seq.*, p. 113; see further Hofmann, N., "Interpretation Rules and Good Faith as Obstacles to the UK's Ratification of the CISG and to the Harmonization of Contract Law in Europe", *Pace Int'l L. Rev.*, Vol. 22, 2010, pp. 159 *et seq*.

1. *Non-conformity of the Goods*

The litmus test for any sales law are the rules on non-conformity of the goods.[34]

The CISG offers clear and convincing solutions in this regard which have in many instances proven to yield satisfactory results. Consequently, these provisions have served as a role model for domestic[35] as well as the European legislator.[36] The CISG rules emphasise the importance of the contract being the first and foremost reference point for the conformity of the goods.[37] Only if the parties have not made contractual provisions for any specific features of the goods does the CISG establish subsidiary presumptions to decide whether the goods conform to the contract.[38]

Without any obvious necessity, the CESL has deviated from the convincing concept of the CISG.[39] In particular, it should be noted that deviations were not dictated by consumer protection. Firstly, the CESL does not recognise the important distinction between contractual designation of conformity and the statutory default rule.[40] Instead, it requires the goods to comply with contractual requirements as well as the default criteria for non-conformity,[41] thus relying on a mixed subjective/objective approach.[42] This may well lead to absurd results as goods may be perfectly conforming to contractual requirements but not pass the objective test. Foodstuff that is no longer fit for human consumption may well be sold as animal food.

[34] For a comparative overview of the different approaches to non-conformity see Schwenzer, I. *et al.*, *Global Sales and Contract Law*, Oxford University Press, Oxford, 2012, Paras. 31.26 *et seq*.

[35] The approach taken by the CISG has been followed by modern and recently modernized legal systems in Central Europe, the Nordic systems as well as Eastern Europe and Central Asia; see Schwenzer *et al.*, supra note 34, 2012, para. 31.45, with further references.

[36] In particular, article 2 of the Directive 99/44/EC of the European Parliament and of the Council of 25 May 1999 on Certain Aspects of the Sale of Consumer Goods and Associated Guarantees was based on article 35 CISG, which has thus found its way into all domestic legal systems which have implemented the Directive.

[37] See Article 35(1) CISG.

[38] See Article 35(2) CISG.

[39] See also Eidenmüller *et al.*, supra note 22, 2012, p. 280, according to whom the drafters of CESL should have adopted the provisions of article 35 CISG rather than experimenting with the notion of conformity.

[40] This is also evidenced by the very order in article 66 CESL that suggests that the non-mandatory rules of CESL prevail over implied terms of the contract.

[41] See Articles 99, 100 CESL; see also Feltkamp and Vanbossele, supra note 13, 2011, pp. 886 *et seq*.

[42] Feltkamp and Vanbossele, *idem*.

Goods without a CE label that may not be sold in the EU may perfectly be fit for export to other regions in the world.[43] Furthermore, in addition to the long list of subjective and objective criteria, Art. 100(g) CESL contains a catch-all provision requiring the goods to "*possess such qualities and performance capabilities as the buyer may expect*". How these expectations are to be assessed remains largely obscure.[44]

Both the CISG and the CESL require the goods to be free from any right or claim of a third party including those that are based on industrial or other intellectual property.[45] However, whereas under the CISG it is nowadays unanimously held[46] that any claim by a third party triggers the seller's liability, the CESL limits the seller's liability to cases where the claims are not obviously unfounded.[47]

In a B2B contract both under the CISG and under the CESL, the buyer can only rely on any lack of conformity if it gave notice to the seller after a proper examination of the goods.[48] At the Vienna Conference these provisions were highly debated leading to the well-known compromise that if the buyer has an excuse for not having examined the goods or giving proper notice it may still reduce the price or claim damages except for loss of profit.[49] Under the CESL, instead of offering a better protection to SME buyers —as envisaged— the prerequisites for examination and notice are even higher.[50] Examination must be undertaken within a rigid 14 days from the date of delivery of the goods[51] and there is no exception in case of reasonable excuse. A further change for the worse as regards the position of the buyer is the fact that the notice in any case must reach the seller to become effective[52] whereas under the CISG[53] the seller bears the risk that the notice is lost or delayed in transit.

[43] See for the interplay of the CE mark and conformity of the goods Schwenzer, I., supra note 9, article 35, para. 14.

[44] For similar criticism see Feltkamp and Vanbossele, supra note 13, 2011, p. 887.

[45] See article 42 CISG; article 102 CESL.

[46] See Schwenzer, I., supra note 9, article 41, para. 10, article 42, para. 6.

[47] Article 102(1) CESL; see also Feltkamp and Vanbossele, supra note 13, p. 888.

[48] Articles 38, 39, 43 CISG; Articles 121, 122 CESL.

[49] Article 44 CISG.

[50] Articles 121, 122 CESL; see also Feltkamp and Vanbossele, supra note 13, pp. 895 *et seq*.

[51] Article 121(1) CESL.

[52] Article 10(3) CESL.

[53] Article 27 CISG.

2. *Remedies*

The second core area of any sales law codification is the issue of remedies in case of breach of contract.[54] The CISG and CESL agree on the basic structure of remedies, as they apply the remedy-oriented approach rather than the old Roman cause-oriented approach.[55] Upon closer analysis of the remedies, however, remarkable differences appear.

A. *Specific Performance*

The first remedy to discuss is specific performance.[56] It is well known that the CISG has not bridged the gap between Common Law[57] and Civil Law[58] legal systems concerning the general remedy of specific performance. Instead, it leaves it to the court or arbitral tribunal to decide whether it enters a judgment for specific performance.[59] It has to be emphasised that this compromise has not given rise to difficulties in practice.[60] In accord with continental legal thinking, the CESL, from a systematic perspective, instead seems to envisage specific performance as the primary remedy.[61] Thus, the principal provision for the buyer's right to specific performance does not

[54] See Wilhelm, C., "Die Rechtsbehelfe des Käufers bei Nichterfüllung nach dem Vorschlag der Europäischen Kommission für eine Verordnung über ein Gemeinsames Europäisches Kaufrecht (KOM, 2011, 635 endg.)", *Internationales Handelsrecht*, Vol. 11, 2011, p. 226; Eidenmüller *et al.*, supra note 22, 2012, pp. 280 *et seq.*; Feltkamp and Vanbossele, supra note 13, 2011, pp. 897 *et seq.;* Scottish Law Commission, supra note 22, 2011, pp. 59 *et seq.*; see further, for a comparative overview, Schwenzer *et al.*, *supra* note 34, 2012, Paras. 41.01 *et seq*.

[55] See Samoy, I. *et al.*, "Don't Find Fault, Find a Remedy", *European Review of Private Law*, Vol. 19, 2011, pp. 862 *et seq.*; Schwenzer *et al.*, supra note 34, paras. 41.45 *et seq.*; for a comparison of CISG and CESL regarding the seller's right to cure see Kruisinga, S., "The Seller's Right to Cure in the CISG and the Common European Sales Law", *European Review of Private Law*, Vol. 19, 2011, pp. 911 *et seq*.

[56] See generally Schwenzer *et al.*, supra note 34, paras. 43.01 *et seq.*

[57] *Ibidem*, 43.24 *et seq.*

[58] *Ibidem*, paras. 43.11 *et seq.*

[59] See article 28 CISG: "If, in accordance with the provisions of this Convention, one party is entitled to require performance of any obligation by the other party, a court is not bound to enter a judgement for specific performance unless the court would do so under its own law in respect of similar contracts of sale not governed by this Convention".

[60] Müller-Chen, M., in Schwenzer, supra note 10, 2010, article 28, para. 4.

[61] Wilhelm, supra note 54, 2011, p. 226; see also Scottish Law Commission 2011 (*supra* note 22), pp. 65 *et seq.*; Samoy & Dang Vu & Jansen, supra note 55, 2011, p. 869; see further, on the DCFR, De Vries, G., "Right to Specific Performance: Is There a Divergence between Civil- and Common-Law Systems and, If So, How Has It Been Bridged in the DCFR?", *European Review of Private Law*, Vol. 17, 2009, pp. 596 *et seq*.; Stürner, M., "Die Grenzen der

contain any truly relevant restrictions.[62] A reasonable restriction of the remedy of specific performance in cases where the creditor should resort to a substitute transaction is not provided in the context of the buyer's right to specific performance, but only for the respective right of the seller in case of breach of contract by the buyer.[63] It appears doubtful whether such an approach is acceptable to any Common Law lawyer.

A special form of specific performance in case of non-conformity of the goods is repair and replacement.[64] The CISG restricts the seller's obligation to replace non-conforming goods to cases where non-conformity amounts to a fundamental breach of contract in order to avoid costly and unreasonable transportation of the goods.[65] This restriction is not found in the CESL, not even for a B2B contract. It may be questionable whether this makes commercial sense between a Lithuanian seller and a Portuguese buyer. It certainly cannot serve as a model on the global scale.

B. *Avoidance of Contract*

In B2B contracts, both the CISG as well as the CESL in principle allow avoidance of contract in case of a fundamental breach of contract supplemented by the so-called *Nachfrist*-principle.[66] In B2C contracts, however, under the CESL the consumer may avoid the contract for any non-conformity unless the lack of conformity is insignificant.[67]

Primärleistungspflicht im Europäischen Vertragsrecht", *European Review of Private Law*, Vol. 19, 2011, pp. 180 *et seq*.

[62] See article 110(3) CESL: exclusion of specific performance only where it is impossible or unlawful or where the burden to the seller is disproportionate to the benefit for the buyer; see further Feltkamp and Vanbossele, *supra* note 13, 2011, p. 897. For the general exceptions from specific performance in Civil Law legal systems see Schwenzer *et al*., supra note 34, paras. 43.20 *et seq*.

[63] Article 132(2) CESL.

[64] See Feltkamp and Vanbossele, supra note 13, 2011, p. 898; Samoy *et al*., supra note 55, 2011, p. 869.

[65] See article 46(2) CISG; see further Schwenzer *et al*., supra note 34, paras. 49.15 *et seq*.

[66] Buyer: article 49 CISG, articles 114(1), 115 CESL; seller: article 64 CISG, articles 134, 135 CESL; see further Wilhelm, supra note 54, 2011, p. 230; Feltkamp and Vanbossele, supra note 13, 2011, pp. 899 *et seq.*; Schwenzer *et al*., supra note 34, Paras. 47.112 *et seq*.

[67] Article 114(2) CESL; see Eidenmüller *et al.*, supra note 22, 2012, p. 282; Feltkamp and Vanbossele, supra note 13, 2011, p. 901; Wilhelm, supra note 54, 2011, p. 231; see further Scottish Law Commission, supra note 22, 2011, pp. 60 *et seq.*, criticizing that the consumer's right to avoid the contract is too long and too uncertain.

Both sets of rules use an essentially identical definition for the fundamentality of the breach.[68] However, the CESL goes one step further by holding that fundamentality is also given where the breach of contract is of such a nature as to make it clear that the non-performing party's future performance cannot be relied on.[69] Whether such a future breach itself amounts to a fundamental one is immaterial.

C. *Damages*

The rules on damages in the CESL[70] by and large follow those of the CISG.[71] However, the CESL now contains an explicit provision that non-economic loss may only be compensated for as far as it results from pain and suffering. Other non-economic losses are excluded.[72] The CISG, in contrast, does not contain a similar restriction, leaving it to further legal development whether and which non-economic loss may be compensated.[73]

3. *Force Majeure and Hardship*

Both the CISG as well as the CESL provide that the debtor is exempted from liability for damages in case of an impediment beyond its control.[74] The CESL *force majeure* provision can be regarded as being more or less equivalent to that of the CISG. However, the CESL does not discuss *force majeure* in the chapter on damages but rather in a Chapter dealing with "General provisions".[75]

[68] See article 25 CISG; article 87(2)(a) CESL.

[69] Article 87(2)(b) CESL.

[70] Articles 159-165 CESL, supplemented by article 2(c) Regulation; see further Eidenmüller *et al.*, supra note 22, 2012, pp. 282 *et seq.*; Feltkamp and Vanbossele, supra note 13, 2011, p. 903; Wilhelm, supra note 54, 2011, pp. 232 *et seq.*

[71] Articles 74-77 CISG; see generally Schwenzer *et al.*, *supra* note 34, paras. 44.01 *et seq.*

[72] Article 2(c) Regulation; see further Scottish Law Commission, supra note 22, 2011, pp. 64 *et seq.*, criticizing the restriction as a reduction in consumer protection.

[73] See Schwenzer, I., supra note 9, article 74, paras. 18 *et seq.*, para. 39; Schwenzer I. and Hachem, P. "The Scope of the CISG Provisions on Damages", *in* Cunnington, R. and Saidow, D. (eds.), *Contract Damages: Domestic and International Perspectives*, Hart Publishing, Oxford, 2008, p. 100.

[74] Article 79 CISG; article 88(1) CESL; see Wilhelm, *supra* note 54, 2011, pp. 232 *et seq.*; see further Schwenzer *et al.*, *supra* note 34, paras. 45.01 *et seq*.

[75] Chapter 9, articles 87-90 CESL.

Furthermore, it has to be emphasised here once more that, as regards service obligations, the CESL follows the fault-based approach of Roman Law descent. Thus, in these cases, the seller is exempted from liability if there was no fault on its part.

Unlike the CISG, the CESL contains a specific provision on variation or termination by court in case of a change of circumstances commonly referred to as hardship.[76] For various reasons, this provision is not convincing. First, it seems preferable to deal with both *force majeure* and hardship under the same provision as it is done under the CISG.[77] All too often, drawing the line between *force majeure* and hardship is not possible. Most subsequent events do not render performance impossible and thus do not constitute a veritable impediment; they just render performance more onerous for the debtor. The prerequisites as well as the consequences for both cases should be the same. Especially, contrary to what the CESL suggests,[78] there should be no difference between an initial hardship and hardship caused by a change of circumstances subsequent to the conclusion of the contract. Under the CESL, in case of initial hardship, the debtor would have to rescind the contract for mistake. Finally, the consequences of hardship laid down in the CESL are unsatisfactory - at least with regard to sales contracts. The parties' duty to renegotiate[79] as well as a possible adjustment of the contract[80] to the changed circumstances by a court or arbitral tribunal is of practical use only in long-term relationships but usually not in sales contracts. All in all, here again, the results achievable under the CISG are more satisfactory than those under the CESL.[81]

[76] Article 89 CESL; see further Schwenzer *et al.*, supra note 34, paras. 45.10 *et seq.*, 45.76 *et seq*.

[77] The modernised German law of obligations also contains independent rules on impossibility (§ 275 CC) and hardship (§ 313 CC). In particular, the relationship between the provision on impossibility due to performance having become overly onerous for the debtor (§ 275(2) CC) and the provision on adaptation of the contract to changed circumstances rendering performance overly onerous for the debtor (§ 313(1) CC) has now caused considerable debate as regards their delimitation, see Schlechtriem, P. and Schmidt-Kessel, M., *Schuldrecht – Allgemeiner Teil*, 6th ed., Mohr Siebeck, Tübingen, 2005, para. 485.

[78] See article 89(3)(a) CESL: "apply only if: (a) the change of circumstances occurred after the time when the contract was concluded".

[79] Article 89(1) CESL; see further Schwenzer *et al.*, supra note 34, Paras. 45.111 *et seq*.

[80] Schwenzer, *Ibidem*, Paras. 45.113 *et seq.*

[81] See for the solution offered under the CISG Schwenzer, I. *in* Schwenzer 2010 (supra note 9), Art. 79, Para. 54; I. Schwenzer, 'Force Majeure and Hardship in International Sales Contracts', *Victoria University of Wellington Law Review*, Vol. 39, 2009, pp. 721 *et seq.*, p. 724; Schwenzer, I., 'Die clausula und das CISG', *in* Wiegand, W. *et al.* (Eds.), *Tradition mit Weitsicht – Festschrift für Eugen Bucher zum 80. Geburtstag*, pp. 736 *et seq.*; Schwenzer I. and Hachem, P.

4. *Interplay of Different Remedies*

The relationship between different remedies is of great importance.[82] As has been pointed out, remedies laid down under the CESL just as under the CISG in the special part relating to seller's and buyer's obligations are subject to certain restrictions, such as the examination and notice requirement,[83] the fundamentality of the breach in case of avoidance[84] or the foreseeability test in case of damages.[85] Under the CESL, however, other remedies exist that may conflict with these remedies and their underlying concepts.[86] Most notably, non-conformity of the goods may give rise to other remedies. Certainly, any buyer of non-conforming goods is mistaken as to the goods conforming to the contract.[87] Thus, if the prerequisites of Art. 48 CESL are met, the buyer may avoid the contract notwithstanding whether for example it gave timely notice of the non-conformity or whether the breach amounted to a fundamental one.[88] Article 57 CESL explicitly provides that a party may pursue either one of the possible remedies.[89] Further problems arise if the seller has failed to comply with any of its pre-contractual information duties which presumably usually will be alleged by buyers in case of non-conformity of the goods. This not only triggers the remedy of avoidance due to mistake[90] but furthermore entails liability for any loss caused to the other party by such failure which again may be claimed independently from and additionally to any other remedies for breach of contract.[91] Again, this stands in sharp contrast to the solution found under the CISG. As the CISG

'The CISG – Successes and Pitfalls', *American Journal of Comparative Law*, Vol. 57, 2009, pp. 474, 475.

82 See on the lacking hierarchy of remedies under CESL Samoy & Dang Vu & Jansen 2011 (supra note 55), pp. 869 *et seq.*; Feltkamp & Vanbossele 2011 (*supra* note 13), pp. 891 *et seq.*; *see generally* Schwenzer & Hachem & Kee 2012 (supra note 34), Paras. 49.01 *et seq.*

83 Arts. 38, 39 CISG; Arts. 121 *et seq.* CESL.

84 Arts. 25, 49(1)(a) CISG; Arts. 87(2), 114(1) CESL.

85 Art. 74 CISG; Art. 161 CESL.

86 For general criticism on the lack of structure and coherence in the CESL's system of remedies see Samoy & Dang Vu & Jansen 2011 (supra note 55), pp. 861 *et seq.*

87 See for a comparative overview Schwenzer & Hachem & Kee 2012 (*supra* note 34), Paras. 49.15 *et seq.*

88 The CESL thus follows the position found in the PECL and the DCFR; *see* Schwenzer & Hachem & Kee 2012 (supra note 34), Para. 49.24.

89 For an overview of the different approaches that can be taken in this respect *see* Schwenzer & Hachem & Kee 2012 (supra note 34), Paras. 49.11 *et seq.*

90 Art. 48(1)(b)(ii) CESL.

91 Art. 29(1),(3) CESL.

itself governs neither mistake nor pre-contractual duties, it is a question of the possible relationship between CISG remedies and concurrent domestic remedies. In case law[92] and doctrine,[93] it is now unanimously held that the CISG pre-empts all concurrent domestic remedies in this field.

V. Filling the gaps

In order to evaluate the appropriateness of the CESL, it is useful to also have a look at those areas of sales law that do not have a counterpart in the CISG. We shall now discuss how the CESL has filled these gaps. Naturally, only a few select subjects can be discussed here.

1. *Pre-contractual Duties and Liability*

The CISG, in principle, does not contain any rules on pre-contractual duties; a proposition to insert a provision on *culpa in contrahendo* was even rejected at the Vienna Conference.[94]

In contrast, the CESL has devoted a whole chapter to pre-contractual information duties.[95] First of all, a variety of information duties are established which apply to B2C transactions only.[96] But also in a B2B contract, the seller has to give any information concerning the main characteristics of the goods which it has or can be expected to have and which would be contrary to good faith and fair dealing not to disclose to the other party.[97] In B2B contracts, such vague and extensive information duties seem to be

[92] *Cf.* for France: Cass. civ. 1re, 14 May 1996, *Jurisclasseur Périodique*, *Édition Générale*, Vol. 71, 1997, No. I-4009; for Austria: OGH, 13 April 2000, CISG-online 576, with a note by P. Schlechtriem, *IPRax,* Vol. 21, 2001, pp. 161 *et seq*.; *see further* the more recent US case *Electrocraft Arkansas, Inc. v. Super Electric Motors, Ltd.*, US Dist. Ct. E.D. Ark., 23 December 2009, CISG-online 2045.

[93] I. Schwenzer, *in* Schwenzer 2010 (*supra* note 9), Art. 35, Paras. 46 *et seq*., Para. 48 with references.

[94] See U.G. Schroeter, *in* Schwenzer 2010 (*supra* note 9), Intro to Arts. 14-24, Paras. 54 *et seq*.

[95] Chapter 2, Arts. 13-29 CESL; see further C. Cravetto & B. Pasa, 'The 'Non-sense' of Pre-contractual Information Duties in Case of Non-concluded Contracts', *European Review of Private Law*, Vol. 19, 2011, pp. 761 *et seq*.; Eidenmüller *et al.* 2012 (supra note 22), pp. 276 *et seq*.; in regard to the Feasibility Study *see* H. Beale & G. Howells, 'Pre-contractual Information Duties in the Optional Instrument', *in* R. Schulze & J. Stuyck, *Towards a European Contract Law*, Sellier European Law Publishers, Munich, 2011, pp. 51 *et seq.*

[96] Arts. 13-22 CESL.

[97] Art. 23(1) CESL.

inappropriate and must necessarily lead to legal uncertainty that cannot be tolerated in international trade.[98] Further pre-contractual information duties are established for contracts concluded by electronic means, especially via websites.[99]

It has already been pointed out that the possibility to concurrently rely on remedies for breach of pre-contractual information duties is particularly problematic.

2. *Non-negotiated Terms*

The use of non-negotiated terms is, especially in international sales contracts, of great practical importance.

The CISG does not even mention this notion. Now, however, due to more than twenty years of practical experience, it has been possible to carve out the essential solutions pertaining to non-negotiated terms.[100]

By contrast, the CESL even distinguishes between non-negotiated terms and standard contract terms.[101] For the latter it practically copies the German Civil Code[102] and defines standard terms as non-negotiated terms which have been formulated in advance for several transactions involving different parties.[103] The necessity for such a subtle distinction at best remains obscure.[104] The dualism of two distinct concepts in this regard is unknown to any legal system, be it on a domestic or on the European level.[105]

[98] *See* S. Whittaker, 'The 'Draft Common Frame of Reference' – An Assessment', Report commissioned by the Ministry of Justice, United Kingdom, Oxford, 2008, pp. 100 *et seq*.

[99] Art. 24 CESL, applying to B2C and B2B contracts; Art. 25 CESL, unclear whether (3) may also be applied in B2B transactions.

[100] *See* U.G. Schroeter, *in* Schwenzer 2010 (*supra* note 9), Intro to Arts. 14-24, Paras. 5 *et seq*., Art. 14, Paras. 32 *et seq*.

[101] Eidenmüller *et al.* 2012 (*supra* note 22), pp. 278 *et seq*.; H.-W. Micklitz, 'An Optional Law on Off-premises, Distance Sales and Unfair Terms for European Business and Consumers?', *in* Micklitz & Reich 2012 (*supra* note 14), pp. 58 *et seq*.; in regard to the Feasibility Study's provisions on unfairness and non-negotiated terms *see* D. Mazeaud, 'Unfairness and Non-Negotiated Terms', *in* Schulze & Stuyck 2011 (*supra* note 95), pp. 123 *et seq.*; M.W. Hesselink, 'Unfair Terms in Contracts Between Businesses', *in* Schulze & Stuyck 2011 (*supra* note 95), pp. 131 *et seq.*

[102] § 305(1) sentences 1, 3 CC.

[103] Art. 2(d) Regulation.

[104] Art. 7(3) CESL seems to imply the presumption that terms in standard contract terms are non-negotiated terms.

[105] See Art. 3 Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts, which dispenses with the requirement that the terms have been drafted for use in more than one transaction.

The CESL contains a specific regime for non-negotiated terms and standard terms as regards the incorporation of such terms into the contract as well as the judicial control of unfair terms.

a) *Incorporation*

On the level of incorporation, problems arise where non-negotiated terms are to be incorporated by reference. The CESL contents itself with the vague formula that the party supplying the terms must take reasonable steps to draw the other party's attention to them.[106] It remains an open question whether, especially in B2B contracts, a mere reference to standard terms is enough. Furthermore, as the requirement of transparency does not apply in the B2B context,[107] it is unclear what requirements as to language *etc.* exist.

Further difficulties arise with regard to the battle of forms. The provision dealing with this issue only applies to standard terms but not to mere non-negotiated terms.[108] It is hard to see the underlying ratio of this approach. Regardless of this fact, this provision in essence does not add much to what is the prevailing opinion under the CISG.[109]

b) *Substantive Control*

Whereas under the CISG the substantive control of (all) contract terms in principle is a question of validity and thus left to the applicable domestic law,[110] the CESL contains specific provisions for this matter.[111] As regards B2C contracts, in addition to a general clause[112] circumscribing unfairness,

[106] Art. 70(1) CESL.

[107] Art. 82 CESL only refers to B2C contracts.

[108] See the heading and wording of Art. 39 CESL.

[109] Under the Convention, the dispute has narrowed down to two approaches: the so-called last-shot-doctrine and the so-called knock-out-doctrine. Under the first doctrine, the non-negotiated terms which have been sent last become part of the contract. Under the second doctrine, conflicting terms are stricken out and replaced by the default rule. This second view has come to be the prevailing view under the CISG, see Cass. civ. 1re, 16 July 1998, CISG-online 344; BGH, 9 January 2002, CISG-online 651; U.G. Schroeter, *in* Schwenzer 2010 (supra note 9), Art. 19, Para. 36 with numerous references also for domestic laws and uniform projects.

[110] See Art. 4 sentence 2(a) CISG; I. Schwenzer & P. Hachem, *in* Schwenzer 2010 (supra note 9), Art. 4, Para. 30.

[111] For criticism see Eidenmüller *et al.* 2012 (supra note 22), pp. 278 *et seq*.

[112] Art. 83 CESL.

the CESL establishes a so-called black list of contract terms which are always unfair with 11 items[113] and a so-called grey list of terms which are presumed to be unfair with 23 items.[114] As regards B2B contracts, the CESL contains a general clause only.[115] This provision slightly deviates from the concept of unfairness in B2C contracts and only applies to non-negotiated terms.[116] According to this definition, a non-negotiated term is unfair if it grossly deviates from good commercial practice contrary to good faith and fair dealing. This gives rise to scepticism from two perspectives: first, this concept is extremely vague and does not give any orientation on how to draft fair contract terms. Second, this provision insinuates that, in a B2B transaction, an individually negotiated term may never be regarded as being unfair; a solution that would significantly lag behind any domestic and international standard for a control of unfair terms even in B2B contracts.[117]

3. *Interest*

A last lacuna under the CISG which is of great practical importance must be addressed here. Although the CISG provides that interest is due on any sum in arrears,[118] it does not state the applicable interest rate.[119] This has proven to be a real obstacle to achieving uniformity. The CESL contains six provisions on interest on late payments.[120] In essence, it links the interest rate to the one applied by the European Central Bank which is adjusted every six months, or an equivalent rate set by a national central bank.[121] Two percentage points are added to this rate for any delayed payment;[122] eight percentage points are added where a trader delays the payment of the purchase price.[123] All in all, this solution may meet with approval. Still,

[113] Art. 84 CESL.

[114] Art. 85 CESL; see further Micklitz 2012 (supra note 101), pp. 62 *et seq*.

[115] Art. 86 CESL; see Eidenmüller *et al.* 2012 (supra note 22), pp. 278 *et seq*.

[116] Art. 86 CESL.

[117] See Eidenmüller *et al.* 2012 (*supra* note 22), pp. 278 *et seq*., also voicing criticism.

[118] Art. 78 CISG.

[119] See K. Bacher, *in* Schwenzer 2010 (supra note 9), Art. 78, Para. 2 with references.

[120] Arts. 166-171 CESL. See on the provisions of the DCFR A. Fötschl, 'Zinsen auf ausservertragliche Geldforderungen im Rechtsvergleich und eine Analyse der Zinsnormen des Draft Common Frame of Reference (DCFR)', *European Review of Private Law*, Vol. 17, 2009, pp. 106 *et seq*.; see further Eidenmüller *et al.* 2012 (supra note 22), pp. 283 *et seq*.

[121] Art. 166(2) CESL.

[122] Art. 166(2) CESL.

[123] Art. 168(1)(5) CESL.

two points deserve mentioning. First, there is an explicit provision allowing for compensation for recovery costs, be it in the form of a lump sum of 40 Euros or as damages if the recovery costs exceed this sum.[124] Having special regard to the international discussion whether pre-trial attorney's fees should be compensated for,[125] this provision seems highly problematic. Furthermore, all rules on interest are mandatory[126] which heavily impairs freedom of contract in this area.[127]

VI. Codifying style and techniques

As concerns the different codifying style and techniques of the CISG and the CESL, one is first struck by the sheer length of the CESL compared to the relatively short CISG.[128] This is partly due to the approach taken towards definitions. Under the CISG, definitions are a rare exception. Their absence has not led to any problems. Contrary to the CISG, the Regulation itself contains a long list of definitions.[129] While it is laudable that the drafters have attempted to achieve a common understanding of legal terms, it is hardly understandable why the text of the CESL again is packed with sometimes repetitive and sometimes further definitions.[130]

[124] Art. 169 CESL.

[125] *Zapata Hermanons Sucessores, S.A. v. Hearthside Baking Company, Inc.*, US Ct. App. (7th Cir.), 19 November 2002, CISG-online 684; see further Schwenzer & Hachem & Kee 2012 (supra note 34), Paras. 44.166 *et seq*.; I. Schwenzer, *in* Schwenzer 2010 (supra note 9), Art. 74, Paras. 28 *et seq*.; CISG AC Opinion No. 6, 'Calculation of Damages under CISG Article 74', Rapporteur J. Gotanda, 2006, available at *http://www.cisgac.com/default.php?ipkCat=128&ifkCat=148&sid=148*, Comments 5.1 *et seq*.

[126] Art. 171 CESL. There seems to be a contradiction between Art. 170 CESL that deals with unfair terms relating to interest and Art. 171 CESL that prohibits any deviation from the statutory scheme.

[127] *See also* Eidenmüller *et al.* 2012 (supra note 22), pp. 283 *et seq*.

[128] Harsh criticism from U. Huber, 'Modellregeln für ein Europäisches Kaufrecht', *ZEuP*, Vol. 16, 2008, p. 742: "The provisions on sales law have to be completely reformulated. [...] The reader should not be given the impression that the drafters think it to be slow-witted". See also Eidenmüller *et al.*, 'Der Gemeinsame Referenzrahmen für das Europäische Privatrecht - Wertungsfragen und Kodifikationsprobleme', *Juristen Zeitung*, Vol. 63, 2008, p. 549: "Reading the DCFR is tiring, because so much of its content is superfluous and because it contains numerous repetitions".

[129] Art. 2 Regulation.

[130] See for example Art. 7(1) CESL in addition to Art. 2(d) Regulation. See also Eidenmüller *et al.* 2012 (supra note 22), p. 272, with further examples of repetitive clauses.

The sheer length of the CESL does not, however, contribute to clarity.[131] Although, in comparison to the DCFR, the CESL has been shortened considerably, the attempt to include as many scenarios as possible into the wording of the CESL has considerably inflated the text. This prolixity, however, has not prevented the drafters from an exorbitant[132] use of general clauses. The CISG, although using much less general clauses, already has been criticized for its vagueness.[133] The CESL, from this viewpoint, will hardly be acceptable,[134] especially to Common Law lawyers.[135]

Finally, it is regrettable that the CESL does not use the same terminology as the CISG.[136] The drafters of the CISG endeavoured to depart from domestic legal concepts, instead seeking an independent legal language. Indeed, to a large extent, they succeeded. The CESL tries to reinvent the wheel by changing terminology that for almost thirty years now has become the *lingua franca* of international sales law. A prominent example, which is also crucial for trade practice, is the replacement of the term 'avoidance for breach of contract' used by the CISG with the term 'termination' in the CESL. The fact that the very term avoidance is used by the CESL in the context of mistake is hardly helpful to ease communication.[137]

VII. Conclusion

The CESL, as it has been published recently, is hardly an improvement to the CISG that is now in force in 23 states out of the 27 European Union

[131] See Eidenmüller *et al.* 2008 (supra note 128), p. 549; Feltkamp & Vanbossele 2011 (supra note 13), p. 905*;* Huber 2008 (supra note 128), p. 742.

[132] See, in regard to the DCFR, Eidenmüller *et al.* 2008 (supra note 128), p. 536, who provide an impressive account of the excessive use of general clauses in the DCFR; see further Feltkamp & Vanbossele 2011 (supra note 13), p. 905, voicing concern that the use of open-end clauses in CESL will not lead to a sufficient level of legal certainty.

[133] Against this criticism Schwenzer & Hachem 2009 (supra note 81), p. 467.

[134] *See* Feltkamp & Vanbossele 2011 (supra note 13), p. 905, according to whom the CESL is "not ripe for implementation".

[135] *See* for the concerns raised in the United Kingdom the Report issued by the European Union Committee of the House of Lords, *European Contract Law: The Draft Common Frame of Reference - Report with Evidence*, London, House of Lords, Stationary Office, 2009, Paras. 31 *et seq*.

[136] For criticism regarding the wording of the German version of CESL see Eidenmüller *et al.* 2012 (supra note 22), p. 272.

[137] We are aware that PICC and PECL follow the same terminology as the DCFR. However, both sets of rules do not contain specific provisions on sales law and already their departure from the language of the CISG is most unfortunate.

member states.[138] It has been shown that in many areas the differences cannot satisfy the needs of international trade.[139] Many of these changes were highly inspired by the German Civil Code and its underlying 19th century principles as well as a strong desire for consumer protection, both of which do not provide an adequate framework for B2B transactions.[140] This is especially true for the abundant number of general clauses and vague terms.[141] The recurrently emphasized principle of good faith certainly will not be regarded with favour by anyone coming from a Common Law country and does not add much to clarity and predictability - one of the principal necessities in international trade. But this is not at all due to a stronger protection of commercial buyers under the CESL as alleged by the aim of the Regulation. Instead, as has been shown, there are several instances where —with more clarity— the CISG offers buyers better protection than the CESL.[142]

All in all, the CESL does not provide a viable alternative to the CISG.[143] Practice needs a simple uniform law for all international and domestic sales contracts. This is why many modern legislators, especially in Eastern Europe, modelled their domestic sales law according to the CISG.[144] The CESL being only an optional instrument on the European level, it is —at the very

[138] Ireland, Malta, Portugal and the United Kingdom have not ratified the Convention. A continuously updated overview of the Contracting States can be found at *www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG_status.html*.

[139] For similar criticism already on the DCFR see Basedow, J., 'Kodifikationsrausch und kollidierende Konzepte -- Notizen zu Marktbezug, Freiheit und System im Draft Common Frame of Reference', *ZEuP*, Vol. 16, 2008, pp. 673 *et seq*.; see further K. Riesenhuber, 'Information über die Verwendung des Gemeinsamen Europäischen Kaufrechts', *Zeitschrift für Gemeinschaftsprivatrecht*, Vol. 9, 2012, p. 5, raising the question whether CESL can achieve its goal of harmonization.

[140] For similar criticism see also Micklitz & Reich 2012 (supra note 14), p. 31, who conclude that the CESL should be limited to B2C transactions, thus excluding B2B contracting from its scope of application.

[141] See, in regard to the DCFR, L. Antoniolli & F. Fiorentini & J. Gordley, 'A Case-based Assessment of the Draft Common Frame of Reference', *Am. J. Comp. L.*, Vol. 58, 2010, p. 351.

[142] See the references to questions of notice, obviously unfounded claims, seller's general right to cure, non-economic loss etc.

[143] See Eidenmüller *et al.* 2012 (*supra* note 22), p. 285, who come to the same conclusion; see further Scottish Law Commission 2011 (*supra* note 22), p. 102.

[144] See Schlechtriem, P., '25 Years of the CISG: An International lingua franca for Drafting Uniform Laws, Legal Principles, Domestic Legislation and Transnational Contracts', in Flechtner, H. *et al.* (Eds.), *Drafting Contracts Under the CISG*, Oxford University Press, Oxford, 2008, pp. 167, 174, 177; Zoll, F., 'The Impact of CISG on Polish Law', *Rabels Zeitschrift für ausländisches und internationales Privatrecht*, Vol. 71, 2007, pp. 81 *et seq*.

least— doubtful whether any sensible trader will opt for it.[145] In essence, this would mean that sellers and buyers would need to adapt their contracts to three different situations: domestic, European and global. Furthermore, the experiences made with the PICC[146] clearly show that parties do not make use of optional instruments in their choice of law clauses.[147] Whereas about 80% of disputes resolved under the auspices of the ICC contain a choice of law clause, opting-in instruments such as the PICC are chosen in only 0.8% of these contracts, although they may be well appropriate to supplement the CISG.[148] It seems all the more improbable that parties would opt out of the CISG and into the CESL which in itself would have to be supplemented by domestic law.

It is regrettable that the European Union chose such a *Sonderweg* instead of maintaining its leading position in the development of the CISG and raising its voice in the global concert. With the CISG becoming more and more important on the global scale, it is important that any harmonisation or unification of laws in Europe ensures that the CISG remains untouched. Hopefully, however, UNCITRAL will take the lead and develop a set of rules of general contract law supplementing the CISG and thus filling the still existing gaps. Such a global contract law should be modelled on the PICC and the PECL, but certainly not on the CESL.

[145] Lando, O., 'Comments and Questions Relating to the European Commission's Proposal for a Regulation on a Common European Sales Law', *European Review of Private Law*, Vol. 19, 2011, p. 720; *see further* C. Herresthal, 'Ein europäisches Vertragsrecht als Optionales Instrument', *EuZW*, Vol. 22, 2011, p. 8.

[146] UNIDROIT Principles of International Commercial Contracts; *see* the newest version of the PICC published in 2010, available at *http://www.unidroit.org/english/principles/contracts/principles2010/blackletter2010-english.pdf*.

[147] Mankowski, P., 'CFR und Rechtswahl', *in* M. Schmidt-Kessel (Ed.), *Der Gemeinsame Referenzrahmen - Entstehung, Inhalte, Anwendung*, Sellier European Law Publishers, Munich, 2009, p. 401; Lando 2011 (supra note 145), p. 720.

[148] Mankowski 2009 (supra note 147), p. 401.

ORAL LECTURES

THE AUSTRALIAN PPSA AND THE CONFLICT OF LAWS

Anthony DUGGAN

The Personal Property Securities Act 2009 (Cth) ("PPSA"), which came into effect on 30 January 2012, is a wholesale reform of the law governing secured transactions in personal property and it represents a major step in the development of Australian commercial law. The PPSA is based in part on Canadian provincial legislation which, in turn, derives from Article 9 of the United States Uniform Commercial Code.[1] Article 9 is a model statute drafted by the National Conference of Commissioners on Uniform State Laws in collaboration with the American Law Institute and it has been adopted in all States. The result is that United States secured lending law, although primarily a State responsibility, is substantially uniform throughout the country. The same is true in Canada. All the common law provinces and territories have enacted personal property security statutes which, with the exception of the Ontario PPSA,[2] are based substantially on a model statute drafted by the Western Canada Personal Property Security Act Committee (now the Canadian Conference on Personal Property Security Law). The Ontario PPSA shares many common features with the Model Act, but there are quite a number of differences in the details.[3]

New Zealand enacted a personal property securities statute in 1999.[4] The New Zealand PPSA closely follows the text of the Canadian Model PPSA, as enacted in the province of Saskatchewan.[5] Australia has elected to take a more free-wheeling approach. The Australian PPSA takes the Canadian Model statute as its starting point, but it departs from the model in numerous significant respects in terms of both drafting and substance. In con-

1 United States Uniform Commercial Code – Secured Transactions (Article 9).

2 Personal Property Security Act, RSO 1990, c P-10 ('Ontario PPSA').

3 For a fuller account, see Ronald C C Cuming, Catherine Walsh and Roderick J Wood, Personal Property Security Law (Irwin Law, 2005) 8–11.

4 Personal Property Securities Act 1999 (NZ) ('New Zealand PPSA').

5 Personal Property Security Act, RSS 1993, c P-6.2 ('Saskatchewan PPSA').

trast to Article 9 and the Canadian PPSAs, the Australian PPSA is a federal statute. The Australian Commonwealth Parliament has limited powers under the Australian Constitution to enact commercial laws and residual legislative powers are vested in the States. It follows that the Commonwealth could not have enacted a comprehensive secured transactions statute without the co-operation of the States. However, the Australian Constitution provides for the referral of powers from the States to the Commonwealth and, acting pursuant to this provision, each State agreed to pass legislation referring its jurisdiction over PPSA matters to the Commonwealth.[6] As part of the package, the States also agreed to the establishment of a national PPS register, to be run by the Commonwealth, and they undertook to repeal or amend their own secured transactions statutes and to dismantle the numerous specialist registers which had previously operated at the State level.

The Australian PPSA raises a host of interesting issues, particularly when it is read in comparison with Article 9 and the Canadian and New Zealand PPSAs. The topic I have chosen for this paper is the Australian PPSA's conflict of laws provisions. The conflict of laws provisions are interesting because, while they are based in part on similar provisions in the Canadian and New Zealand PPSAs and also in part on the UNCITRAL Legislative Guide to Secured Transactions,[7] there are also some significant differences, some but not all of which reflect deliberate policy choices.[8]

Example 1. Grantor is a company incorporated in Jurisdiction A. Grantor carries on business in Jurisdiction A and Jurisdiction B. Grantor and SP enter into a security agreement in Jurisdiction A under which Grantor gives SP a security interest in factory equipment located in Jurisdiction B. Grantor subsequently sells and delivers the equipment to T in Jurisdiction B without SP's authority. T is unaware of SP's security interest. When SP learns about the sale, it claims the equipment from T.

The first issue in a case like this is to determine whether the dispute between SP and T is governed by the laws of Jurisdiction A or those of Jurisdiction B. The answer to the question may affect the outcome of the case if the rule in Jurisdiction A for dealing with disputes of this nature is different from the rule in Jurisdiction B. In Canada and the United States, conflict of laws issues may arise at the provincial or state level. Assume that in Example 1, Jurisdiction A is Saskatchewan and Jurisdiction B is Ontario. If Saskatchewan law applies, the outcome of the case will depend on whether SP

6 Australian Constitution, s.51(xxxvii).

7 (United Nations, NY, 2010), Chapter X, available at www. uncitral.org/pdf/English/texts/security-leg/e/09-82670_Ebook-Guide_09-04-10.

8 See generally, Parliament of the Commonwealth of Australia, Senate, Replacement Explanatory Memorandum on the Personal Property Securities Bill 2009 (Cth), Chapter 7.

perfected its security interest, in accordance with the Saskatchewan PPSA, by registering a financing statement in the Saskatchewan Personal Property Securities Register. On the other hand, if Ontario law applies, the outcome will depend on whether SP registered in Ontario.[9] By contrast, the Australian PPSA is a federal statute and this forecloses the possibility of conflict of laws issues at the State level. Nevertheless, conflict of laws issues may still arise at the international level (assume, for instance, that in Example 1 Jurisdiction A is Australia and Jurisdiction B is New Zealand) and the Australian PPSA contains provisions addressing conflict of laws issues arising between Australia and other countries.

The main provisions are in PPSA, section 6, which defines the territorial reach of the statute and Part 7.2 (sections 233-241) (the conflict of laws provisions). Other relevant provisions include: section 39, which enacts special rules for the case where the collateral consists of goods or other tangible property and is moved from a foreign jurisdiction into Australia during the currency of the security agreement; section 40, which enacts special rules for the case where the collateral consists of intangible property or financial property and the grantor relocates to Australia or transfers the collateral to a person located in Australia; and section 77, which relates to the case where the applicable law is the law of a foreign jurisdiction which makes no provision for registration of security interests.

Part 2, below, discusses the territorial reach of the PPSA, as provided for in section 6, and the interaction between section 6 and the conflict of laws provisions in Part 7.2. Part 3 deals with the scope of the conflict of laws provisions in Part 7.2. Part 4 discusses the choice of law rules in Part 7.2 relating to security interests in goods and also the rules in section 39 relating to relocation of goods. Part 5 addresses the choice of law rules in Part 7.2 relating to security interests in intangible property and also the rules in section 40 relating to the relocation of the grantor. Part 6 deals with the choice of law rules in Part 7.2 relating to security interests in financial property. Part 7 discusses the choice of law rules in Part 7.2 relating to security interests in proceeds. Part 8 deals with choice of law issues relating to the enforcement of security interests. Part 9 concludes.

[9] If Ontario law applies, T will take the equipment free of SP's security interest if SP's security interest is unperfected in Ontario: Ontario PPSA, s.20(1)(c); if Saskatchewan law applies, T will take the equipment free of SP's security interest if SP's security interest is unperfected in Saskatchewan: Saskatchewan PPSA, s.20(3). Compare Australian PPSA, s.43, discussed in Chapter 10, Part 2, above.

REFLECTIONS ON THE THREE DECADES OF INTERNATIONAL TRADE AND INVESTMENT LAW- AND BEYOND

Mary HISCOCK

SUMMARY: I. *Introduction*. II. *What happened to the trade and investment structures immediately after world war ii?* III. *From diplomacy to law- the wto*. IV. *Why has the WTO had limited succes?* V. *Shift in economic and political power*. VI. *A geographic solution*.

I. INTRODUCTION

In the field of international trade and investment law over the last 30 years, the most outstanding event has been the establishment of the World Trade Organisation (WTO) in 1995. This new legal institution is Janus-like in that it is the actualisation of the last piece of the wartime architecture of the Bretton Woods deliberations. The recent accession of Russia to the WTO membership now means that 97% of world trade is now regulated by the WTO. Bretton Woods also produced the International Bank for Reconstruction and Development (now the World Bank) and the International Monetary Fund (IMF). These three institutions together, as regulators of international commerce, were designed to avoid the policy errors of the first half of the twentieth century, to fortify the chances of avoiding global conflicts or World Wars, and to develop a new jurisprudence of international commercial law. The United Nations at the same time would ensure a new public international law of peace, as well as outlawing war. The WTO can look back over 50 years of incremental development, and forward to a new and expanding field of legal influence through regulation. The second half of the twentieth century, however, modified these expectations dramatically.

The business of the WTO is trade law and practice, not investment. The second half of the 20th century saw a huge increase in the volume of

investment, especially foreign investment in the territory of a sovereign state not that of the investor. Although investment law is a product of domestic law and treaty, as is trade law, the lack of a global institution has meant that there are still no globally agreed rules, and especially that there are no minimum standards. There are significant institutions that have major if partial influence, such as the World Bank and its offshoots, the Convention on the Settlement of Disputes between Investors and host Governments (ICSID), but these do not have the compelling force of WTO membership, and their activities have been even more contentious.

What is interesting is the way in which the institutions created to meet a particular need or objective, have managed to survive and reinvent themselves, even when the need has been fully met. This is particularly true of the IMF and the World Bank, but the WTO itself is the product of survival and reinvention.

Built into the structure of these institutions, there is in every case, a peculiar basis of a blend of law and economic or political theory. Beyond that intrinsic ideology, the last 30 years and the 30 years before that have seen a massive change in external circumstances affecting trade and investment. These challenge the fundamental assumptions that underlay the creation of WTO and the different expectations that exist of investment law and regimes. Looking into the future, what is it that we can expect at the global level of the law of trade and investment? The lawyer's answer, perhaps a limited one, is to say that maybe the answer to the future lies in the past.

II. What happened to the trade and investment structures immediately after world war ii?

First, the rapid emergence of the cold war between the superpowers of the United States (US) and the Union of Soviet Socialist Republics (USSR) destroyed the alliance that was going to underpin the International Trade Organisation (ITO). The ITO, the third institution of the Bretton Woods triumvirate, was designed to regulate the whole field of international commerce, including trade, investment, insurance, taxation, and other financial transactions. What was left was the General Agreement on Tariffs and Trade (GATT) made by 23 nations in 1947 to secure their multilaterally negotiated tariff concessions in the interim until the ITO came into being.

Secondly, the former colonies of the States on both sides of World War II (WWII), demanded and obtained independence through armed conflict or agreement or imperial collapse or withdrawal, beginning with peace ne-

gotiations after WWII and continuing until the end of the century. This unplanned and unexpected series of events seriously disturbed the balance of trade that had existed in the colonial era. It also changed the patterns of resourcing and investment from the pre-war imperial models, aided by the need to pay for the costs of the war. The mood of anti-colonialism which accompanied these changes is still a potent force of suspicion and distrust in international commercial law. Developing and least developed States are now majority stakeholders in all international institutions. This has led to a new jurisprudence quite different from pre-war views.

This last third development is still of uncertain scope. It is the modification of the older international law of peace on the powers of nation States in relation to their own citizens, their own resources, and the persons and property of foreigners within their territory. Whereas it had been the case for several centuries that treaties made by States were binding, these had for the most part, in times of peace, been enabling rather than restrictive. These treaties increased in number from the middle of the nineteenth century with industrialisation and the expansion of imperial trade, frequently conducted by sea. However, the emergence of human rights law, on a global scale, was the beginning of a reorientation, with the result that States were constricted in the exercise of their powers in their own territories by external agreements. The fields of environmental law and labour law were also enlarged internationally. Minimum international standards and procedures were agreed in public health. These were necessitated and accelerated by the increased mobility of persons, and by scientific developments which meant that drugs could alleviate or eliminate diseases that had previously been tolerated. The Black Death that had scourged Europe in medieval times now had twentieth century counterparts that were of global significance.

All these things impacted on international commerce. What had been the province of international diplomacy now became subject to international legal processes.

III. From diplomacy to law- the WTO

The agreements reached to constitute the WTO and its organs and powers are in the form of treaties agreed by each Member as a single undertaking. The WTO constructs the regulatory regime consisting of rules of law governing the conduct of Member States in measures relating to international trade in goods, in services, and in intellectual property rights. It supplies a dispute resolution regime based on arbitration and consulta-

tions, and it has an effective mechanism for enforcement. In this respect, it is unique. It also provides a surveillance mechanism for Member States to see whether they are operating in accordance with their legal obligations. This is a mixture of confession and avoidance, and of exhortation, and occasionally praise.

The rules relating to regulation of trade in goods were built up over 50 years through institutional interpretation of its own rules, the results of disputes between Members, occasional codification, and a joint decision to accept a favourable regime of special and differential treatment for developing countries. This regime established global standards, but gave developing countries time to adopt these standards without undue harm to their economic and social fabric.

The constant objective was the liberalisation of international trade.

This was to be achieved by eliminating trade restrictions on the import of goods, by dealing with trade from every Member state without discrimination both internally and at the borders. The GATT also continued with its original objective of providing a forum for multilateral negotiations for reductions of tariffs. It embodied the economic theory of comparative advantage in its opposition to trade embargoes and quotas, as well as the toleration of tariffs as a transparent instrument but only a temporary one. The validity of the objective was beyond question.

The WTO extended regulation to trade in services as well as goods through the General Agreement on Trade in Services (GATS). This is a novel and open ended concept, and reflects the increasing wealth that now comes from cross-border services delivery as well as from cross-border trade in goods. The instrument is also an interesting development, because the scope of regulation can be increased by a series of protocols to embrace new areas of services not previously agreed. Furthermore, it coincided with an increasing period of privatisation of previously delivered services from government, as well as the sharp decline if not collapse of socialism.

Because the GATS covers the delivery of services by nationals, including corporations, of one Member state in the territory of another Member State, it creates an interesting relationship with investment as opposed to trade. There is no global regulation of investment. The WTO has no powers in this field of law, except where it is directly linked to trade. There are no globally agreed minimum standards, despite the fact that there is a great number of treaties that now regulate cross-border investment as between States, either bilaterally or regionally. There is only one global body for investment dispute resolution, the ICSID, the product of a World Bank initiative in the 1950s. There are many ad hoc arbitrations of investment

disputes. This is a process described by some as the privatisation of public international law, with decisions made by unelected and unaccountable private citizens, enforceable through a network of treaties. It is very controversial whether this can produce a coherent global body of the law relating to investment. Had the ITO come into existence as planned, investment would have been part of its remit.

The scope of coverage of the GATS is determined by the agreement of WTO members in negotiations. It expressly does not cover services delivered by or on behalf of government. But otherwise it is entirely up for decisions by States, and there is a great variance in the range of areas agreed.

The GATS does establish a principle of transparency as a universal obligation. So any measure, whether a law, regulation or policy that affects trade in services, must be published in an accessible form and forum. In addition, and this is a sleeper issue, even where the services are not included in those agreed, each State must ensure that its system of regulation of services is no more restrictive than necessary. The judgment about necessity is not left to the Member State alone.

The last major WTO agreement is Trade Related Intellectual Property Rights (TRIPS). This differs from GATT and GATS, in that it creates minimum international obligations in protecting IP rights, in addition to those arising out of the series of IP Conventions going back to the 19th century. This is not aimed at liberalising trade, but at protecting intellectual and industrial property rights. It was largely negotiated by developed countries with little input from developing countries. It is the most contentious part of the WTO.

IV. Why has the WTO had limited succes?

One might have thought that this logical and negotiated structure would develop to tackle and eliminate problems arising from trade. But it has been buffeted by a number of internal and external pressures which have prevented the WTO from reaching its fulfilment. Considering these issues is ironic, given that, since the accession of Russia to membership of the WTO finally accomplished in 2012, 97% of world trade is regulated by WTO procedures. Russia is also the last of the G20 nations to become a member of the WTO.

The first is timing. What was contemplated in the Uruguay Round negotiations was not trade conducted by electronic means, or telecommunications of the sophistication of the present. The impact of the internet on

trade puts a strain on many of the carefully negotiated agreements, as it has in many areas of international transactions. The rules were not designed to deal with this kind of trade, and the impact on crossborder trade in services in particular is substantial. What always made tariffs an effective and attractive tool of regulation was the existence of a physical territorial border where tariffs could be charged. In the WTO dispute of US Gambling, the US realised all too late that it had entered into an obligation to permit cross border electronic gambling without discrimination, in circumstances where it had power to deal with domestic gambling enterprises in accordance solely with domestic law and policy.

The second change is the loss of persuasive power of the belief in the Washington consensus. This belief that liberalisation of trade was an intrinsic part of achieving democracy was the political counterpart of comparative advantage in terms of WTO ideology. It underlies the whole Trade Policy Review mechanism, because that provided the score card that member states were supposed to meet.

The third aspect is loss of sovereignty. It has always been conceded by States that treaties represented a diminution of sovereignty, but entering into treaties was always a voluntary process, at least in times of peace. The WTO treaties do not merely set up rights and obligations, but also create a complex and organic structure that is not within the control of any member state. Withdrawal is always possible, but is unlikely to occur. So decisions that would normally be within the constitutional power of any State are constrained in ways that would not perhaps have been foreseen. In particular, judgments of State in relation to the health and welfare of their citizens are no longer merely discretionary within political and practical limits but, if restrictive of trade, must be justified by acceptable scientific research. Again this is a matter of necessity.

V. Shift in economic and political power

The processes of international trade have dealt with many examples of unequal power. There has been the dominance of economic power held successively in the 20th century by the UK, the US, and now it is argued that China and India will succeed to this mantle. Since the 1960s, there have been multinational corporations of immense economic power, greater than many nation States. Probably some 75% of world trade is handled by such corporations.

However, in the gap left in relation to investment law, these players have been dominant for most of the 20th century. Because there are no global standards, and the law is negotiated ad hoc, economic power has created a consensus that the object of investment law is protection of the investor. Where that investment is cross-border, then it is protection against a host state and its policies. The latest addition to the ranks of the powerful is the sovereign wealth fund investor. This pits one state against another, and tests out the strength of any system of treaties. The absence of any mitigation through a balance of interests is not there in the treaties. Curiously the other impetus for rethinking the objective of investment law is that many developing countries, fear of which previously caused a call for protection are now investors in their own right seeking protection.

Finally, one needs to consider the demonstrated loss of power of states to show political will to create new solutions to the risks that affect international trade and investment, arising from the global financial crisis of the last few years. This is seen in the failure of the G20, the most powerful economies in the world, to agree to effect solutions to the current situations of sovereign debt. It is an interesting contrast to look to the similar crises of the 80s and 90s, where there was no lack of leadership in suggesting solutions.

The other conspicuous failure of political will is in relation to the failure of the Doha Round of negotiations to agree new trade concessions and amendment of some constitutional aspects of the WTO which have not been effective or acceptable in practice since 1995, or which could not be finally determined during the Uruguay Round. The great challenge facing the WTO is how it deals with a membership that is now largely organised into regional trading blocs rather than single national membership. Those trading blocs are not only extending the WTO rules on trade, but moving into investment activities as well, an impetus largely fuelled by the failure of political will to make changes to the WTO in operation. The result is that much of the convergence reached in the WTO agreements is dissipated by the effect of bilateral and regional trading and investment agreements, leading to the spaghetti or noodle bowl effect of the current law. However much one may like pasta, and however much lawyers earn in fees for advice, this is hardly an acceptable situation.

VI. A GEOGRAPHIC SOLUTION

It may be that the answer lies in moving the problems to a new locale. If the central point of location is the presently the north Atlantic ocean,

what happens if we change this to the Pacific and Indian oceans, and the weight of economic and political power moves out of Europe and North America to China, India, South America and Africa. Alliances such as the BRICS (Brazil, Russia, India, China and South Africa) may begin and finish with different needs, views and objectives. New trade and investment agreements, such as the proposed enlargement of the membership of the Trans-Pacific Partnership, may have a similar effect, or they may just be the last hurrah of the present regime.

UNIFORM LAW: EFFICIENCY PERSPECTIVES

Kono TOSHIYOUKI

The idea of a globally uniform law is not new. In many western countries, the 18th Century had been marked by a transformation from a particular land law to a more homogeneous legal system at the nation state level. As soon as this daunting task gained its momentum, lawyers immediately raised the idea of a 'global law', i.e. law shared by every civilized nation.[1] The fashionable idea of a global uniform law has persisted until today; yet in different economic and cultural settings has prompted the change in methodological approaches as well as the uniform law-making.

This paper is divided into two main parts. The first part provides a historical account of the development of uniform law. This first part outlines the features of the uniform law-making in three periods: the early 20th Century; several decades after the Second World War; and at the turn of the millennia. This evolutionary perspective helps to single out the key features of the uniform law-making process. Further, it is argued that the theory and methodologies of unification of law has changed over time together with the evolving economic and political realities of the time. The second part of the paper aims to contribute to the ongoing debate concerning the goals and methodology of uniform law by applying an economic perspective to uniform law. It seeks to explicate a number of questions that have been left on the sidelines of the discourse. Law and economics calls for the adoption of a different —'efficiency'— criterion as a starting point of analysis. Efficiency renders some of the concepts previously applied by legal scholars obsolete and stimulates the investigation of problems that had only been scantly touched upon in the legal literature. Further, the efficiency criterion offers much stimulus for the investigation of the different possible modes of unification. That is, an efficiency perspective helps to identify the pros and

[1] Zittelmann, E., *Die Moeglichkeit eines Weltrechts* (unchanged reprint of a presentation with an afterword, 1916).

cons of uniform law, as well as to provide guidance in the choice between different methods of unification.

The roots of uniform law could be found in the late 19th Century when the need to establish some common standards promoting international trade became obvious. The need of uniform standards of communication impelled the adoption of, for example, the International Postal Convention (1874).[2] Later, the protection of the results of intellectual activity (books, inventions etc.) resulted in the adoption of the Paris[3] and Berne[4] Conventions dealing with the protection of intellectual property works. The implementation of these international treaties was entrusted to special unions that were created under the same legal framework. The matters related with the maintenance of minimum labor standards were started to regulate by the Association of Labor Legislation (established in 1901), which in 1919 turned the International Labor Organization (ILO).

Simultaneously, a number of international or inter-governmental organizations were established with an intention to further process of unification of laws. The Hague Conference for Private International Law was first convened in 1893. The International Institute for the Unification of Private Law (UNIDROIT) was established in 1926 as an auxiliary organ of the League of Nations. After the Second World War, the task of harmonization and unification of international trade law was entrusted to the UNCITRAL (United Nations Commission for International Trade Law), a special United Nations body. Established in 1966 UNCITRAL adopted a number of international conventions dealing with various aspects of international sales and carriage of goods, commercial instruments, as well as the use of modern communication means in international trade. In addition, a number of non-binding Model Laws were prepared to address such issues as international commercial transactions, financing, insolvency, out-of-state commercial dispute settlement procedures, electronic commerce. Among others, also the Organization for Economic Cooperation and Development (OECD) significantly contributed to the unification process. Established in 1961, OECD provides for a platform to deliberate various economic, political and social issues related to economic development.[5]

[2] 1874 Berne Convention establishing a General Postal Union.

[3] 1883 Paris Convention for the Protection of Industrial Property.

[4] 1886 Berne Convention for the Protection of Literary and Artistic Works.

[5] OECD is well known for its Guidelines for Multinational Enterprises (last time updated in 2011) as well as the Convention on Combatting Bribery of Foreign Public Officials in International Business Transactions (1997).

The last few decades of the 20th Century could be marked by a stark expansion of uniform law-making. A number of various legislative instruments in the area of international trade an private internationa law have been adopted, many of them in the form of international treaties. The work under the auspices of the Hague Conference on Private International Law has also been quite successful. Much more legal certainty as to the jurisdiction and applicable law has been brought to the areas of private, family, commercial and procedural law.

In addition, many more uniform-law-type-instruments have been drafted and put into practice by intergovernmental organizations such has the UNIDROIT as well as non-governmental organizations and trade circles. Suffice here to mention the UNIDROIT Principles of International Commercial Contracts which not only have established a firm ground for general contract-related issues, but also had significant influence in the reform of general contract law at the national law niveau. Besides, a number of uniform-law-type instruments have been drafted by such organizations as International Chamber of Commerce (ICC) which prepared a number of key instruments, such as the INCOTERMS. The ICC also drafted the Uniform Customs and Practice for Documentary Credits and other instruments dealing with the non-state resolution of commercial controversies. Further activities of unification could be identified in other areas related to maritime law and standard setting (eg ISO, accounting, ICANN etc.).

As can be noticed, the initiatives of uniform law-making have gradually shifted from the unification of certain areas of law by international treaties concluded between states towards a 'privatized' setting. This shift from the state towards "quasi-state" or "non-state" unification of law has been driven by increasing complexities associated with the drafting process as well as the political and economic hurdles associated with reaching consensus. Furthermore, it has become more and more difficult to delineate the contours of uniform law. In the wake of such a transformation, a new area of legal scholarship dealing with 'transnational law' has been gaining momentum.[6] The recent paradigm of private uniform law-making has brought about various methodological questions pertaining to the legitimacy of novel regulatory instruments. Further, a number questions arise with regard to the possible and achievable structures of uniform law.

[6] See *e.g.* Calliess, G.P. and Zumbansen, P., *Rough Concensus and Running Code: A Theory of Transnational Private Law* (Hart, 2010); P Kjaer, Between Governing and Governance (Hart, 2010).

The current institutional setting largely influences the levels of uniform law. One of possible approaches to understand uniform law is to see it as comprising three fields of unification: (a) the unification of substantive rules; (b) the unification of rules pertaining to international cases (*internationales Einheitsrecht*); (c) the unification of private international law rules. The key driving forces of unification, as indicated in previous legal scholarship could be summarized as follows. It has been thought that unification of law contributes to simplification, increases legal certainty, facilitates uniformity of court decisions as well as helps to eliminate distortions of competition. In addition, uniform plays a significant role in the courtroom: uniform law reduces the situations where there may be a conflict between norms of/or legal systems, it provides for a solid source for the interpretation of law and filling the gaps in law.

Previous legal scholarship also touched upon the relationship between the uniform substantive law and uniform private international law. It has been argued that these two stand in stark contrast with each other. While unification of substantive, if realized, could eliminate differences among national substantive laws, unification of private international law *can not* achieve such ultimate harmony of substantive laws.[7] Instead, the uniform private international law is based on the premise that substantive laws vary. However, further analysis concerning the relationship of different levels of unification has not been made.

This paper offers to offer a different perspective on uniform law. One of the possible modes of looking at the uniform law is to apply the methods developed by scholars engaged in law and economics. Law and economics takes a rather pragmatic approach to legal problems and considers legal rules from a cost-benefit (efficiency) perspective.[8] It is argued here that an efficiency perspective could provide for some further food for thought and put forward different questions which should be taken into consideration.

In order to support the economic analysis of uniform law, the paper borrows some of the methodologies developed by economics scholars.[9] Namely, an *efficiency* perspective mandates the comparison of costs associated with different kinds of rules: rules that are simple, clear and detailed;

[7] Cf. Kropholler, J., *Internationales Einheitsrecht* (1975).

[8] See eg MJ Whincop and M Keyes, *Policy and Pragmatism in the Conflict of Laws* (Ashgate, 2001); J Basedow, T Kono, G Ruhl (eds), *An Economic Analysis of Private International Law* (Mohr, Tubingen, 2006).

[9] K Kagami, *Kokusai shakai ni okeru shiteki kankei no kiritsu to funsō kaiketsu: kokusai shihō no keizai bunseki – jōsetsu (Regulations and Settlement of Private Disputes in International Community: Introduction to Economic Analysis of Private International Law)* (Tokyo, 2009).

and rules which are abstract (standards). These rules should be also viewed in context and the effects they produce: i.e. legal certainty or flexibility. Furthermore, a law and economics approach calls for the calculation of the costs and benefits associated with the application of different kinds of rules. For instance, the costs associated with clear and simple rules are relatively low. Yet, for the parties clear rules mean a higher degree of legal certainty. On the other hand, abstract rules (e.g. the requirement of 'fair compensation') may lead to relatively high administrative costs as well as offering less certainty for the private parties.

This cost-benefit analysis further prompts weighing of desirable policy goals: legal certainty or flexibility. In the context of current uniform law debate there is no clear consensus as to the desirable outcome. It is generally assumed that uniform law contributes to higher legal certainty and uniformity of decisions. However, legal scholars have not been able to delineate the contours either of legal certainty, nor flexibility. This paper suggests that an efficiency perspective fuels the debate by requiring consider interests of *stakeholders* as well as the factor of *timing, i.e. ex ante and ex post*.

On a more general level, it is argued here that if uniform law is viewed from an efficiency perspective, the costs associated with the uniform lawmaking are to be taken into account. Namely, it may happen that costs associated with uniform law making are unreasonably high. For instance, the Hague Judgments project, the objective of which was to unify grounds of jurisdiction and recognition and enforcement of foreign judgments protracted over a decade and eventually failed. Accordingly, cost-benefit analysis could be also applied to compare under what circumstances the unification of substantive rules is more efficient and should be preferred over the unification of private international law rules. In this constellation, several stages of comparison could be addressed which would include:

- Uniform substantive law versus uniform private international law;
- Uniform substantive law versus national private international law;
- Uniform private international law versus not uniform substantive law;
- National private international law versus uniform private international law.

THE REFORM, APPROXIMATION AND HARMONIZATION OF COMMERCIAL LAWS IN THE MULTI-CULTURAL CONTEXT OF THE EAST AFRICAN COMMUNITY

Agasha MUGASHA

The East African Community comprises of the sovereign states of Kenya, Uganda, Tanzania, Rwanda and Burundi; all of them neighboring countries in the Eastern part of Africa. The five member states aim, ultimately, to form a political federation but as interim steps seek to achieve a customs union, common market, and monetary union. These economic and political ambitions and arrangements are premised on the need for a sound legal system that enables the member states to achieve their objectives of prosperity through regional and international trade and investment. A particularly important suite of laws that have been recently reformed and harmonized are those that relate to commerce and finance, compendiously called commercial laws, which provide the major impetus for the common market protocol.

The large scale reform of the commercial laws in the last thirty years began with a large project for the modernization of commercial laws in Uganda funded by the World Bank in the 1990s. The ideological backdrop had earlier been provided by the dominant economic theory and enforced by the IMF through its development assistance programmes. The theory consisted of several elements: the liberalization of the economies by emphasizing the private sector and significantly reducing the role of the state in commerce and finance; open international trade and foreign investment; capacity building whereby overseas consultants who had the requisite skills were required to partner with local personnel through joint participation in projects; and the realization that commercial laws needed to be supported by wider investments in socio-economic infrastructure. Initially the overwhelming force of globalization was seen as favoring the metropolitan countries because the laws tended to require developing countries to open their markets; in recent years, however, globalization is also seen as benefitting developing countries in the form of increasing direct foreign investment

and other forms of investment *e.g.* joint ventures, franchising and direct sales of goods and services.

The consultants funded by the World Bank submitted their report in 1998 and the project is now in the final stages of implementation by way of enacting the relevant legislation. The first part of this paper assesses the success of this project which mainly imported Western law, predominantly from the United States and to a lesser extent from the UK, to the Ugandan context. The main questions are whether the substance of the laws is suitable for the local circumstances and whether the process achieved the development purpose that was intended.

In 1999 the East African Community was established by Treaty and the regional organization comprising of Kenya, Uganda and Tanzania came into being in 2000 when the treaty come into force. The entry of the two new members in later years complicated the legal landscape because the new entrants traditionally subscribed to the Civil Law tradition in contrast to the founding members that subscribe to the Common Law tradition. The larger regional block also meant that there was greater diversity in the levels of the legal and economic infrastructure, appetite for implementing new laws, and the languages spoken.

There is an on-going exercise for the approximation of municipal laws among the five member states aimed at implementing the common market and facilitating the free movement of goods and services, capital and labor. The approximation exercise is wholly being implemented by local personnel, but one cannot help but notice the hand of foreign consultants and foreign templates in the laws being harmonized or approximated. This leads to the question if the resulting laws are suitable to the local circumstances, if they will serve their intended purpose, and if the lessons from the legal transplants of yesteryear have been learnt.

This paper will test and develop some tentative observations:

- The World-bank funded project in Uganda resulted in a suite of modern laws aligned to the laws in Western countries even though in some instances they were less detailed than their Western counterparts;
- The World-bank funded project focussed on the 'elite' side of commercial and financial law and left behind a large and economically significant informal sector;
- The approximation of municipal laws in the East African Community aims to apply the best principles among the five member states, at a level higher than the highest common denominator, and for that reason the legal tradition of the member state is not very significant;

- The different legal traditions and cultures are still relevant because they create a healthy mutual suspicion and healthy debate before common principles are adopted;
- The mistakes of yesteryear concerning legal transplants have largely been avoided because there is local expertise and strong debate that question the suitability of particular laws and any unnecessary intrusion into local circumstances.

THE COMMISSION PROPOSAL OF A REGULATION FOR AN OPTIONAL "COMMON EUROPEAN SALES LAW" – TOO BROAD OR NOT BROAD ENOUHG?

Norbert REICH
H.W. MICKLITZ

SUMMARY: I. *Concluision too broad – NPT broad enough? instead: a need to readjust the scope of CESL*. II. *Conclusions on modalities of contracting and on unfair terms in B2C transactions*. III. *Conclusions (sales law and related services)*.

I. CONCLUISION TOO BROAD – NPT BROAD ENOUGH? INSTEAD: A NEED TO READJUST THE SCOPE OF CESL

The paper started with the somewhat provocative question of whether the proposal, together with the CESL, could be regarded as being "too broad" or, conversely, "not broad enough". Both readings of the existing material seem to be possible *and must be critically scrutinised under the proportionality criteria*:

- *"Too broad"* by including general rules of contract law and the law of obligations which are not specific to sales law, which do not meet specific problems of cross-border transactions in the internal market, and, therefore, need not be included in the CESL. As a result, this may amount to an "overextension" of its preclusionary effect on national law and may in that respect be contrary to the principles of proportionality.
- On the other hand, it may be "*not broad enough*" in respect of the extremely narrow definition of the "consumer". This will create conflicts with national law under the still existing minimum harmonisation principle. Moreover, the exclusion of financed sales and lease contracts does

not seem to meet the realities of modern marketing. The service sector which takes up about 70 % of the EU-BSP has found very little attention in the CESL, with the exception of the somewhat unfortunate regulation of "linked service contracts".

This paper did not discuss the substantive provisions of the CESL, neither with regard to B2B nor with regard to B2C contracts; this will be done in separate contributions on "modalities" (by Hans-W. Micklitz) and "sales law" (Norbert Reich). While there may be a perceived need to have a specific EU instrument for cross-border B2C contracting, this is not necessarily the case with regard to B2B contracting where already the (somewhat narrower) CISG exists and where hardly any mandatory provisions can be regarded as an impediment to trade. Contracts with SMUs which CESL regards as B2B transactions may well be put under the cover of B2C, at least to a limited extent as far as protective objectives similar to consumer transactions should be pursued. It may also be difficult to clearly distinguish between B2B and B2C contracts, particularly with regard to the applicability of general contract law.

The proposal, as has been shown throughout the analysis in this paper, will raise a *"basket of uncertainties"*, many of which are new to EU law and will require judicial answers by the ECJ in the spirit of uniformity. This need has been provoked by the principle of autonomous interpretation within the scope of the CESL with sometimes difficult borderlines. However, the possibility of uniform interpretation is certainly an advantage of the CESL against other international instruments in contract and commercial law, in particular the CISG, but will create its own *transaction costs* like search costs of traders and consumer —respectively their associations— of finding right and tenable solutions for unsettled questions, length and expenses of proceedings before the ECJ under Art. 267 TFEU, the need to reformulating contract terms, the adaptation of the CESL to new technological and economic developments. Whether the CESL as an optional instrument in whatever form will be an attractive legal model for traders cannot be predicted now; it must still pass its practice test. Whether consumers will be better off if they contract with traders under the CESL, or whether they risk losing familiar protection under national law also waits to be seen.

The authors of this study suggest to rethink the much too broad and to some extent unconvincing approach, as has been shown throughout this paper, of the CESL in a somewhat more narrow and at the same time more realistic direction:

- It should be limited to cross-border B2C transactions, thus excluding B2B contracting where other instruments exist (either freedom of choice under Rome I, or CISG) which do not seem to cause problems to the functioning of the internal market.
- The concept of B2C transactions should be extended in its personal scope as envisaged in Recital 17 of the CRD. Therefore, the definition of "consumer" in Art. 2 (f) of the Proposal should be supplemented by the following paragraph: "*If the contract is concluded for purposes partly within and partly outside the person's trade (dual purpose contracts) and the trade purpose is so limited as not to be predominant in the overall context of the supply, that person should also be considered as a consumer*".
- It requires further discussion on whether and how far transactions with SMEs should also to a limited extent be included. The current concept of customer protection in telecommunication, energy and financial services might serve as the starting point for the development of appropriate concepts.

II. Conclusions on modalities of contracting and on unfair terms in B2C transactions

The results of the study concerning off-premise and distance contracts can be summarised as follows:

1. The Feasibility Study (FS) tries to attain a high level of consumer protection. The contrasting of the FS and the CESL with the recently adopted Consumer Rights Directive 2011/83 (CRD) however remains ambivalent. In some cases, the standards in CESL resp. FS are higher, sometimes lower than in the CRD. Unfortunately, the provisions in CESL and CRD are not always identical. Law application and interpretation thereby become unclear.

2. A general critique must be directed again an individualisation of protective provisions and against an increasing separation of rules which should be regarded as belonging together, as shown with respect to the distance selling directive. The discrepancy of contract law provisions and rules on unfair commercial practices is not in the interest of the consumer. Their combined effects under collective redress requirements should be one of the objectives of an optional instrument.

3. From a consumer point of view it should be regarded as problematic that several consumer friendly decisions of the ECJ have been "overruled". This concerns the reduction of the right of withdrawal to one year after non-information, the introduction of an obligation of the consumer to pay

for the use of a product during the withdrawal period. Also the new provisions on costs for sending back the product are not in the interest of the consumer. One wonders whether this will help cross-border B2C transactions.

4. Another unsettled problem concerns the determination of the language for the transaction. In both the FS and CESL, the trader will be allowed to unilaterally determine the language.

5. There are no provisions on linked contracts in the FS resp. CESL. It seems that only contracts of limited volumes will be governed, financed by using credit cards. But even in these cases it would have been necessary to regulate payment modalities. The FS resp. CESL are silent on that point, will the exception of implementing the *Gysbrechts* judgment of the ECJ (case C-205/07). The authors seem to take the view that the Payment-Directive 2007/64 regulates these questions which is not the case because it does not concern the consequences of payment by card. The chargeback-system as used in the US would have been of help to settle these questions.

The results of the analysis of the parts on the control of unfair terms in the FS resp. CESL show the following results:

1. The FS aimed at a consolidation of the discussion about the control of unfair terms. Therefore relevant new approaches could not be expected when drafting the CESL. Central objectives of consumer protection were left aside, like the increased importance of price clauses, especially in financial markets, the blurred delimitation of individually negotiated from pre-formulated clauses, the limited effects of injunctions against unfair clauses in individual proceedings. One has the impression that the control of unfair clauses works the more "efficiently" the less relevant it is in B2C transactions, and the less it costs to business.

2. It should be remarked positively about the proposals of the FS that the general clause has been reformulated which however was taken back in the CESL. This would have allowed a merger of different legal cultures. An important step would be the introduction of black and grey lists, even if their importance in the EU context remains vague without additional explanations. On the negative side of the CESL the limitation of control to pre-formulated clauses and the exclusion of the control of clauses on the main subject matter and the price must be criticized.

III. CONCLUSIONS (SALES LAW AND RELATED SERVICES)

The following conclusions may be drawn from the discussion of parts IV and V of the CESL based on the FS:

1. As a general observation, it must be stated that the FS and the CESL try to attain a "*high level of consumer protection*", usually closely following the *acquis* where it exists or is in the offing. Certain differences in Member State consumer protection law do not seem to be of such great importance that they actually challenge the entire project of the FS/CESL. However, there are many examples where a discrepancy between the *acquis* and the FS has been found to exist, some achieving a *higher level* of protection, others implying a "lowering" of protective standards without giving a reasonable explanation for that. The reduction of the prescription time from three to two years has not been explained. It must be made sure that the final version of the CRD, and the CESL based on the FS, are made *compatible* with each other and provide for an equally high level of protection. The trader should not be given an incentive to use the CESL in order to lower consumer protection standards, at least in cross-border transactions.

2. As a consequence of this objective, most (but not all) provisions on B2C relations are *mandatory*. If not expressly determined as mandatory, certain terms with an impact on B2C contracts will have to be evaluated by referring to unfair terms legislation, which does not meet the *standard of legal certainty* needed particularly in cross-border transactions. The FS uses a rather inchoate technique as it lists separately each and every provision which is mandatory, instead of providing in its opening articles that all B2C provisions are mandatory as such, unless specifically formulated as default rules.

3. As a more fundamental critique, it has been shown that the scope of application of part IV and even more so part V is simply too *narrow* and will not attain the practical relevance the EU Commission is hoping for, in particular in cross-border transactions, in that:

- The concept of the "consumer" is too restricted, particularly in the (frequent) case of "mixed contracts"; in the CESL setting, it could probably not be extended by Member State law, as has been explained in the Chapeau-paper by Micklitz/Reich;
- The concept of "sales contract" has been shaped by the somewhat dated concept of a single "*spot contract*", while in practice businesses in consumer markets use more and more complex arrangements, e.g. "subscription" type contracts as long-term "open-end" arrangements,

complex "contract packages" containing elements of financing and service, or a combination of both;

- The scope and content of part V on "Services related to a sales contract" seem to be incomplete, contradictory and will not provide legal certainty of cross-border B2C transactions.

4. The special and rather sketchy rules on "*digital content*" which have a broad application must still undergo a test to see to what extent they are compatible with aggressive marketing techniques of right holders which may not conform to consumer choice and needs, in particular with regard to unfair use restrictions by contract clauses seemingly legitimised under copyright reasons. Mere information rights may not suffice to strengthen the rights of the consumer who acquires in good faith digital content. On the other hand, once the professional seller has supplied the information as required, eg on lack of interoperability, the consumer will not have a remedy against the seller. The information requirement *de facto functions as an exclusion clause.*

5. The *technical language* of the FS and the CESL is rather complex by making isolated references to the DCFR. It is regrettable that the terminology of the CRD and the FS/CESL has not been coordinated (for instance the terms "rescission" in the CRD and "termination" in the FS/CESL; the term "reasonable" is frequently used in the FS/CES, but much less in the CRD). Many other ambiguously worded provisions will create additional interpretation problems both for national and finally for EU courts under the requirements of the reference procedure. As an overall assessment, the FS/CES do *not meet the requirements of legal certainty* as a prerequisite of making transactions —whether B2C or B2B— easier and less costly in the internal market.

COMPANY LAW, LAWYERS AND INNOVATION: COMMON LAW VS. CIVIL LAW

Francisco REYES

In this essay we make two major claims. The first is that public legislatures should think seriously about giving maximum effect to the principle of freedom of contract in company law. This would not only give corporate lawyers the tool they need to provide legal services that match the needs of the current global business community, but also encourage legal experimentation and innovation. The second claim is that corporate lawyers in common law systems are more open to legal change and innovation than their civil law colleagues. The difference seems to lie in the more experimental nature of common law compared to civil law systems.

SECURITY OVER MOVABLES IN MEXICO: MEXICO'S NEW *REGISTRO ÚNICO DE GARANTÍAS MOBILIARIAS* ("RUG")

Harry C. SIGMAN*

SUMMARY: I. *Against this background, let us consider the rug, Why do i think the rug is the best registry in latin america?* II. *Some further details about the rug system, particularly inscription of registrations*. III. *Some further details about the rug system, particularly searching the record*.

This paper is presented at the 16th Biennial Conference of the International Academy of Commercial and Consumer Law, generously hosted by the Universidad Nacional Autónoma de México. This provides me the happy opportunity to publicize and praise the achievement by Mexico of the establishment of the RUG, its single nationwide registry for security rights in movables, organized and operated by the Secretaría de Economía and which became operational in October, 2010. The RUG is one of the best movables security registries functioning in the world.

The RUG is one of the two best registries in Latin America, the other being that of Honduras, which became operational effective January, 2011, and is operated by the Chamber of Commerce of Tegucigalpa; see *http://www.garantiasmobiliarias.hn*. It is searchable via the internet, free of charge,

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24/7; registrations bear a small fee; all registrations to date, have been submitted through the Chamber as no member of the public has applied for an electronic user account. I will provide additional comments about the Honduran registry. I also mention, in passing, that Guatemala, Chile and Peru are the three other Latin American countries that have made some reform efforts in the field of security rights in movables during the past decade, subsequent to the promulgation of the OAS Model Law (Org. of Am. States, Model Inter-American Law on Secured Transactions (2002); see *http:/www.oas.org/dil/cidip-vi-secured transactions_eng.htm*. In addition, there is presently pending in Colombia a bill modernizing the substantive law and providing for a modern electronic registry, expected to pass within the next few months.

Most modern efficient secured transactions laws depend on the support of a modern efficient registry. A registry must, of course, be consistent with and implement substantive law rules, but even a conceptually superb body of substantive law is unlikely to be efficient if it is dependent on an unsatisfactory registry. Mexico has been struggling over the modernization of its secured transactions substantive law for two decades. Indeed, much of the credit for the advances that have been made to date belongs to our Academy colleague, Boris Kozolchyk, and his National Law Center for Inter-American Free Trade (see *http:/www.natlaw.com*). I recall coming to Mexico to participate in a conference in Hermosillo (Sonora) in March, 1995, with Boris and Ron Cuming, another Academy colleague. Indeed, much of what has been accomplished in Mexico may be attributed in no small part to Boris' perseverance and dogged efforts.

Although this paper does not include an in-depth study of the development of Mexican substantive law relating to security over movables, some description of that somewhat tortured history is necessary, particularly since the establishment of the RUG has finally made the current underlying substantive law much more usable, more despite that body of law than because of its halting modifications. It is necessary to have a picture of the substantive law to understand what the RUG has accomplished.

Over the past two decades, many efforts were made to modernize Mexico's substantive law. These were vigorously resisted, in particular, by those with vested interests in the status quo, such as the notaries, who, under the pre-existing law and practice, played a key role in drafting and registering commercial documents and effectively functioned (much to their profit) as gatekeepers to secured status and to such registration as existed. They would seem still somewhat to be gatekeepers, not to the RUG but to a creditor's gaining secured status, at least insofar as Ley General de Títulos y Op-

eraciones de Crédito (General Law on Negotiable Instruments and Credit Transactions ("LGTOC") arts. 365 and 404, respectively, require ratification before them of signatures on *prendas sin transmisión de posesión* and *fideicomisos de garantía* when the secured obligation exceeds 250,000 Mexican Pesos [this figure is subject to a daily inflation adjustment, the UDI (*unidad de inversion*); currently that is a multiple of almost 5, so the current figure is a value of approximately US$75.000]. And, naturally, the state level registries were not eager to lose the registrations they serviced prior to the initiation of the RUG. Also, financial leasing companies resisted a requirement that such leases be registered.

A brief comment about *Notarios* (functionaries appointed by the states who perform the roles traditional for notaries in the civil law world; see http:/www.notarios.com.mx) and *corredores públicos* (generally translated as public brokers, these are federally appointed persons who, although dating back to decree of Emperor Carlos V of Spain, today function under the Federal Law of Public Brokerage in force since 1993; they provide public faith and play various roles in the commercial marketplace; see *http:/www.correduríapública.gob.mx*).There are about 5,000 *notarios* and 370 *corredores*.

Significant modernization of Mexican substantive law proved difficult also, or at least so it was argued by opponents, because modern substantive secured transactions law seemed impossibly inconsistent with historic concepts of incompatibility of security rights without dispossession of the debtor and "notice filing" seemed unacceptable in light of the historic operation of registries, which served to validate the underlying legal document itself, to constitute the transaction embodied in the document, to give the arrangement "public faith", and to provide publicity vis-à-vis third parties. This traditional function involved the participation of notaries as well as the *análisis y calificación* by registry officials (rigorous screening examination to assure completeness and validity of documents submitted for registration), for which services both the notaries and the registrars charged fees. It is important to note, however, that the OAS Model Law, designed for use in countries with legal traditions similar to those of Mexico, demonstrates that these are not insurmountable obstacles; Honduras did a fine job of adopting a comprehensive modern movables security law based largely on the OAS Model Law. It should also be noted that Mexican delegates to the OAS played a significant role in the OAS deliberations. Indeed, the diplomatic conference that approved the 2009 OAS Model Registry Regulations was chaired by a Mexican, Rodrigo Labardini, who also is the current chair of Uncitral Working Group VI's effort to produce a Technical Legislative Guide on the Implementation of a Security Rights Registry Guide intended

to assist countries wishing to implement the U.N. Comm'n on Int'l Trade Law, UNCITRAL Legislative Guide on Secured Transactions, U.N. Sales No. E.09.V.12 (2010) herein "Uncitral Legislative Guide".

Unlike the Uniform Commercial Code, in the states of the United States of America, and the Personal Property Security Acts, in the Canadian provinces, and unlike the OAS Model Law and the Uncitral Legislative Guide, Mexican substantive law, to this day, has not adopted a unitary security interest based on a functional approach. Rather, it embraces a variety of different security devices, which were developed over time, under Mexican federal or state law, to provide modes of financing particular activities, and which had/have different rules concerning not only collateral coverage but whether a public registration was required; where it was to take place (even registrations with respect to a particular device that were required under the federal Commercial Code, were filed in a state-run registry pursuant to a Coordination and Cooperation Agreement between the Mexican Ministry of the Economy and each individual state); and what was achieved by such registration (including priority vis-à-vis competing creditors). For example, there was no specific statutory purchase-money super priority similar to the that found in the North American laws; the need to facilitate purchase-money credit, first introduced legislatively in a very rudimentary form by the Mexican 2000 legislation, was theretofore managed either in a "secret lien" form, in that registration was not required, or by using title-based devices such as conditional sales, title reservation or financial leases, or by specific priority rules inhering in particular security devices that functioned, at least in part, as purchase money transactions (*créditos refaccionarios*, *avíos* or *habilitación* are essentially production credit vehicles, although not strictly confined to pure purchase money transactions).

Mexican substantive and registry law moved forward in a poorly-coordinated series of major and minor legislative and regulatory actions during the first decade of this century, primarily in 2000 and 2003, until finally the actions establishing the RUG were taken during 2009. These actions are identified in fn. 1 of Dale Beck Furnish, Mexico's Emergent New Law of Secured Transactions: Recent Developments 2000-2010, 28 Ariz. J. of Int. and Comp. Law 143 (2011).

The reforms in the actions of 2000 did produce a few modernizations. For example, they added two new statutory security devices, the *prenda sin transmisión de posesión* (pledge without transfer of possession) and the *fideicomiso de garantía* (security trust), the latter of which featured a form of summary execution that was extremely attractive when compared with the expensive and lengthy enforcement procedures available in the case of other security

devices. These two new devices and the other modifications were placed in the LGTOC, the Commercial Code and other related statutes.

By means of the *Reglamento del Registro Público de Comercio* issued in 2003, there was instituted a national *Sistema Integral de Gestion Registral* ("SIGER'). This did not create a new registry but in essence provided a national electronic data transmission and storage system, replacing paper and producing a national uniformity. While this did not constitute a single national registry, it was a first step towards "notice filing", by providing for a simple "pre-codified" form for electronic registration; this form, however, was applicable only with respect to the new statutory *prenda* and the new rules did not require such registration for all forms of security devices. Moreover, the form was in addition to, not in lieu of, submission of the underlying documentation for *calificación* by the registrar.

Registration with respect to the new security trust device required the submission of the entire trust document (eventually, a pre-codified form was added for this device). This contrast illustrates the difficulty Mexico had to depart from the traditional registration. On the other hand, the legislation declared explicitly that the new *prenda*, a nonpossessory right in movables, was a "real right." While the new law required registration of the new *prenda* in order to achieve effectiveness against third parties, it did not award priority over the other security devices then in use. The trust (*fideicomiso*) had long been known in Mexican law and was used, *inter alia*, for security purposes. The 2000 act introduced a statutory version of this device, better tailored specifically for security purposes and making it a more reliable device. Although it became commonly used, it was expensive to create (among other things, only financial institutions and warehouse operators are eligible to act as such trustees, allowing them to charge monopolistic fees), making it to a great extent unavailable for widespread use to support credit to sme's. The trust document was to be registered under the name of the debtor/trustor, with the creditors who were the beneficiaries being designated by the trustor to the trustee but not necessarily being identified in the trust document (and creditors were eligible to be trustees).

Under the reforms enacted during the first decade of this century, a financial lease (*arrendamiento financiero*), a device theretofore not required to be registered, was required to be registered in the *Registro Público de Comercio* or another "applicable registry." Now, that device must be registered in the RUG. Also, during that time, in 2007, Mexico ratified the Cape Town Convention, accepting the notion of registration of title retention and financial leases of aircraft.

Thus, even after almost a decade of reform efforts, Mexico lacks a coherent clear structure of one or more security devices, with a clear system of priorities, and, until the establishment of the RUG, lacked a single registry covering all such devices.

Finally, three actions during September and October, 2010 (*Decreto*, *Acuerda* and *Aclaración al Acuerda*) resulted in the RUG as it is operational today. The final Regulations that established the RUG specify a list of security and security-like devices, under the general heading of *garantías mobiliarias*, which continue to be available and are not superseded by a unitary security interest, but are required to be registered in the RUG in order to be effective against third parties. Thus, a single national registry was established in which one would find substantially all types of effective competing security rights over movables and in which registration would itself render the creditor's security right, regardless of type, effective against third parties.

The enumerated list of security devices covered by registration in the RUG is specified by a drop-down element on the mandatory "pre-codified" form (a form that, in the RUG, exists only electronically), the last of which is a catch-all of "other special privileges" (although it is not clear to what this refers, possibly to some privileges that appear to exist under Mexican insolvency law, but it is clearly an expansive element, not a limiting one). The list comprises: *prenda sin transmisión de posesión* (nonpossessory pledge); *la derivada de un crédito refaccionario o de habilitación o avio* (the derivative of [rights arising under] types of production credit agreements); *la derivada de una hipoteca industrial* (the derivative of an industrial mortgage [this device is available only to banks]); *la constituida sobre una aeronave o embarcación* (rights in airplanes or vessels); *la derivada de un arrendamiento financiero* (rights arising under financial leases); *cláusula de reserva de dominio en una compraventa mercantil de bienes muebles que sean susceptibles de identificarse de manera indubitable* (title reservation clause in a commercial purchase and sale agreement covering movable goods which are capable of being indubitably identified); and *la derivada de un fideicomiso de garantía, derechos de retención, y otros privilegios especiales conforme al Código de Comercio o las demás leyes mercantiles* (rights arising under guaranty trust agreements, rights of retention [possessory liens] and other special privileges in accordance with the Code of Commerce and the other commercial laws". These devices do not appear to be inapplicable to any particular type of personal property. Registration in the RUG constitutes "public notice" for purposes of the RUG legislation and "other legal regimes."

Moreover, there is currently pending further legislation, prepared by the Ministry of Economy, to improve certain elements. For example, the cur-

rent draft of the legislation adds a requirement of registration of sales of accounts (n.b., the statement of motives refers to "*cesión de créditos (derechos de cobro) incluyendo al factoraje financiero*", while the operative statutory text refers only to such financial factoring. Current Mexican law, art. 426 of LGTOC, provides that "transmisión de derechos de crédito" done with the purpose of financial factoring becomes effective against third persons upon notification to the account debtor, without the need for a registration in any registry or a grant made before a *fedatario público*. Also, the proposed legislation may provide for registration against non-Mexican entities that are not matriculated under Mexican law. The RUG is not presently well-suited to deal with U. S. cross-border financing of *maquiladora* production, as the entity that ships the goods south and then receives the goods after processing in Mexico is the owner, and, if a legal person, is not an acceptable grantor. It is anticipated that this legislation will be adopted this coming December.

I. Against this background, let us consider the RUG, Why do I think the RUG is the best registry in Latin America?

1. *The RUG is an all-electronic system.*

This avoids delays, costs and risk of data entry or other error and other intervention by registry staff that inhere in systems involving paper registrations. This feature makes possible the speed, low-cost and other advantages of the RUG. Registrations are immediately effective and immediately indexed and searchable. Experience in North America indicates that users migrate toward electronic filing when that is offered if the system design is user-friendly and efficient. Honduras has a well-designed electronic system but is also designed to accept paper registrations.

2. *The RUG is available 24/7 for both searching and registering.*

It provides registrants, immediately upon registration, with a certificate of registration bearing a time stamp and electronic signatures of both the registrant and the RUG in a form admissible in court, and a registration is immediately automatically indexed so as to become searchable immediately upon registration. This speeds up credit decisions and funding in the marketplace. In Honduras, the registration is also immediately indexed and becomes immediately searchable. The registrant obtains an acknowledgment

of the registration which includes the registered data, the date and time of registration and the registration number assigned by the registry.

3. *The RUG provides a single nationwide secured transactions database.*

[único is sometimes mistranslated as "unique", suggesting it is different from all others; in this context, it means "sole" or "single", the only one.] This feature avoids all the legal, logistical and other issues which would otherwise result from having multiple registries (by geographic subdivisions or otherwise). This was no mean feat—prior to the initiation of the RUG, there were 269 local registration databases and the average time for achievement of registration was 17 days. These registration offices still exist and may, inter alia, provide assistance to would-be registrants at the RUG. Honduras has a single registry operated by the Chamber of Commerce of Tegucigalpa, which has an office open to the public in Tegucigalpa. While there continues to be only one database, the Chamber of Commerce of San Pedro Sula (the second largest but primary commercial city in Honduras), now functions as an ancillary office for receiving registration data on paper. Neither office retains paper; once the data is entered into the database electronically, the paper is returned to the registrant. Thus, in Honduras, the database is fully electronic and intake can be transmitted from account holders electronically (although to date there has been no application for an account by anyone and all registrations to date have been made via the Chamber, so effectively the system provides a data entry service to those wishing to submit the data on paper).

4. *Accessibility to the RUG, both for registering a security right and for searching, is available to all.*

Statistics indicate that by June 30, 2012, over 85% of registrations had been transmitted directly to the RUG by creditors themselves, with the remainder being transmissions by a notary, a *corredor*, other federal and state officials and the judiciary (who are empowered to cancel or modify registrations, *e.g.*, upon determination that the grantor is entitled to cancellation, by means of an electronically transmitted *Anotación*). The Honduras system deals with the latter situation in a slightly different manner. The judiciary does not have such a direct access to the system; it is the debtor, having obtained a cancellation order from a judge, who submits the cancellation form.

With respect to searching the RUG, there is no requirement that a searcher establish a legitimate interest in order to gain access to the RUG data, as is the case in many land and other "traditional" registries (including some recently established movables security registries, *e.g.*, New Zealand and Australia).

5. *Searching and registering at the RUG are both FREE OF COST.*

The government agency responsible for government revenues and for determination of fees charged for government services in Mexico (in the registry context, it is wise not to leave this matter to the registry itself, so as to discourage empire-building), conducted a study that indicated that, based on an all-electronic system, with minimal need for employees other than monitoring operations and occasional IT work and a few clerks to answer telephone calls, the incremental cost of a registration transaction was less than US$0.05. This left the capital cost of the software and hardware to create and operate the system, which effectively the government decided to subsidize in order to achieve the goal of facilitating credit for sme's. Previously, fees were set by each Mexican State and were typically based on a percentage of the registered amount of the secured debt (averaging 2%) —essentially imposing a tax on secured credit, inconsistent with the goal of the reform to reduce the cost of credit. Not charging a fee has the added benefit of eliminating the need to deal with collections and avoids the cost of building a financial element into the software for the system. Charging a high amount, whether as a flat fee or a percentage of the credit, is likely to thwart the goal of increased availability of credit at lower cost, as it often results in either the failure to register (which then reduces the revenue anticipated by the government), forcing the secured party to either deny or reduce the desired credit, or to go forward on an unsecured basis. Not charging a fee based on the secured amount also removes a justification for including a field in the registration data for the maximum secured amount-whether mandatory or, as in Mexico, voluntary— inclusion of which then requires provisions in the law regarding the consequences of inclusion or failure to include this data.

In contrast, Guatemala imposes very high registration fees, fixed to produce revenue for the government; this clearly has made the registry far less useful and is clearly counterproductive to the underlying goal of making more credit available to sme's. In 2009, Guatemala had only 566 registrations. Honduras avoided the temptation to emulate Guatemala; it charges a

fee of only the equivalent of approximately US$12.00, not enough to deter use of the system; and searches in Honduras are free. As of August 1, 2012, Honduras had over 6,500 registrations.

6. *Substantially all-inclusive scope of security rights required to be registered at the RUG.*

Registration at the RUG covers substantially all types of de facto security rights and substantially all types of collateral, including motor vehicles (although in Mexico, creditors claiming cars as collateral often utilize a technique of blank endorsement of transfer documents to enhance enforcement in the event of default; Honduras has a car registry that issues license plates and collects taxes, but this does not appear to be a registry for owners or secured parties). I must say substantially because there are still some items not included in the RUG's coverage (*e.g.*, financial factoring).

The electronic registration screen calls for a designation of not only the type of security right but also of collateral type (selected by the registrant from a drop-down menu; gathered by the RUG for statistical purposes) and a description of the collateral. RUG statistics re types of collateral subject of registrations through June 30, 2012, indicate the following distribution: about 50% agricultural products, about 25% machinery and equipment, 13% motor vehicles, 4% livestock, 2% rights and receivables, 1% inventory and 1% consumer products. [N.b., some of these categories might be overlapping.] The User Guide recommends that registrants copy and paste the collateral description from the underlying document on which the registration is based. This advice may not only be prudent to prevent unintentional discrepancy, but also provides assurance that the registrant will not be accused of providing misleading data-an issue raised by certain Mexican lawyers, though not a likely issue in the North American systems.

7. *The RUG is very user-friendly.*

A *Guía del Usuario para el uso del sitio* (a user's guide, in Spanish, of course) is accessible at the RUG website. In addition, items on various screens have a question mark, which, when clicked, provide examples and explanations and cite to the Reglamento. The Honduras system is likewise very user-friendly—each screen has instructions, as do the backs of the paper forms.

II. Some further details about the RUG system, particularly inscription of registrations

The registration requires identification by name (*nombre, denominación o razor social*), as well as by the *folio electrónico* of the *otorgante (*the grantor of the security right) and, if the *otorgante* is not also the *deudor* (the person who owes the secured obligation), identification of the *deudor*. The RUG creates an id# for individuals —for RUG purposes— if they don't have one. In contrast, in Honduras, the only official search, and the only one with legal consequences, is by the id# (although a search by name is possible for informational purposes). [In the U.S., UCC Article 9 also distinguishes between an obligor and a debtor; the latter is defined as "*A person having an interest…in the collateral, whether or not the person is an obligor.*", i.e. the grantor of the security interest; there is no separate identification of the obligor on the UCC financing statement and U.S. citizens do not have official national id#'s (thus, for searchers and filers, the weight on the debtor's name is much greater).]

Multiple creditors may be identified on a single registration (*fideicomisos*, for example, often involve more than one creditor).

Duration of the registration's effectiveness (*vigencia*) is designated by the registrant (*e.g.*, 60 months). The system accommodates designation of up to 9999 months (surely the need for such a lengthy duration is highly improbable and might be subject to attack, at least by the grantor, as false information). The period initially designated by the registrant is modifiable by the subsequent registration of a renewal or decrease. In the absence of a designation by the registrant, the registration is nevertheless processed, and the RUG automatically assigns one-year duration.

III. Some further details about the RUG system, particularly searching the record

In the course of preparing this paper, a search was run via the internet from a personal computer in the U.S. It was fast, simple and cost-free, and, apparently, comprehensive; indeed, it offered a complete image of each discovered registration for immediate viewing and/or downloading. All that was required —a one-time procedure— was becoming a Registered User; this required only an e-address and designation of a password created by the prospective user. An account was authorized within seconds by return e-mail, conferring Registered User status. This enabled proceeding with a search, and no electronic signature or other requirements were imposed.

To become a user eligible to submit registrations, an electronic signature is required. I was advised that obtaining an electronic signature is easy and inexpensive, and that the Tax Office has issued thousands of digital keys that people can easily carry on a USB in their pockets, and that there are also five companies that issue these privately. In Honduras, searches can be done directly on the website without any previously established account (but to submit registrations electronically a user account must first be established).

Available search criteria are: the grantor's name, the grantor's *folio electrónico* (id#; for individual Mexican nationals, this is usually that person's CURP [Social Security] #), collateral description, and the number assigned by the RUG to a particular registration (*número de garantía o asiento*). A search request can include more than one criterion. This feature is especially useful if a response to an initial inquiry by grantor's name or by collateral description produces a large number of potential hits, since it results in a narrower more focused search. Submission of a grantor name consisting of only a given name and a surname (patronymic), produced a report indicating results found for three persons with those same names but also an additional name element (most likely matronymics). This suggests that the search logic is not a literally 'exact match' (as is the case in some U.S. filing offices) but responded with at least some matches that include the requested name but have at least certain additions. The three additional registrations reported were identified by: the number assigned by the RUG to the registered security right (*número de garantía o asiento*), the transaction number assigned by the RUG to that filing (*número de operación*), the type of the transaction (*e.g.*, an initial registration (*inscripción*)), the name of the grantor, the grantor's id# (or when the grantor does not have one, the number assigned by the RUG to the grantor for RUG purposes), the date and time of the reported transaction and the collateral type (to see the collateral description would require calling up a copy of the registration). This data might allow disregard of any or all of the three discovered registrations, and, alternatively, it enables the searcher to extend the search by calling up a copy of one or more of the indicated filings showing all of its information, including an identification of the specific security right that is the subject of the registration. Other search logic information derived from that computer session is that a search request that submitted only a surname was not rejected, and, as to be expected, the report identified many potential hits (in this case, a fairly common name produced thirteen potential hits). Thus, in virtually a matter of seconds, or at most minutes, much useful data could be obtained at no cost. Also learned was that the system does not strip out accents, *i.e.*,

a search of Sanchez without an accent will produce different, non-overlapping, results from a search of Sánchez. The system is not case-sensitive.

A printout can be generated of any of the screens referred to above. However, a prudent searcher will take the further step of requesting a *Certificación*, obtainable without delay and at no cost. This produces a pdf, displayed on the screen and available for download by the searcher, which constitutes legal evidence of the registration in the RUG's records; certifications issued by the RUG facilitate presentation of documentary evidence in legal proceedings. The *Certificación* will be needed, at the very least, in the event of litigation, judicial enforcement or bankruptcy.

Some additional comments on the RUG:

It should be noted that registration in the RUG relates to a particular document/legal act (*acto o contrato*) which creates a particular type of security right, identifying the type of right, the date of the underlying document, the details concerning the *Instrumento Público* (number and identity of the notary or corredor) who formalized the document (required if the secured amount exceeds a statutory minimum), and, at the option of the registrant, the terms and conditions of the document. The document and its details are neither submitted to nor examined by the RUG; it is the registrant who supplies this data to the public record (without verification by the RUG). This feature is consistent with Mexico's preservation, at the substantive law level, of different types of security rights rather than put them all into one functionally-defined "security interest" (along the lines of UCC Article 9 and the Canadian PPSA's). This is consistent with the traditional notion of the registry as a place where an existing legal right is being registered, rather than using the registry as a notice board or warning flag that a right may exist now or may come into existence in the future which will enjoy a priority based on the date of the filing. This feature also precludes the submission to the RUG for inscription of a registration until the right has been legally created by the specified legal *acto* or *contrato*. To facilitate the possibility of a pre-creation warning flag, often valuable for legitimate business reasons, the RUG permits the registration of an *aviso preventivo*, a preventive notice that warns searchers of the intention to register a right shortly which will have a priority dating back to the time of the registration of the *aviso*. The *aviso* is effective for only a short period. As is apparent, this arrangement is less flexible than that of the North American systems.

On the other hand, the RUG system provides more information to searchers and more certainty concerning the particular secured transaction, but these benefits come at the price of the flexibility provided by the North American systems, where the filing is effective to perfect with respect to one or more transactions, limited not to a single underlying document but only by the collateral description.

The RUG registration provides a field for a statement of the maximum amount secured (and currency). The value of this field is far from clear, and it may well function as a trap for the unwary secured creditor. This is not a mandatory item, and its voluntary nature is clearly labeled as such. Moreover, the form also calls for an indication whether or not the underlying document foresees "*incrementos, reducciones o sustituciones*" of the collateral or the secured amount. Such an indication should suffice to put the world on notice that any stated amount cannot be relied on. Unless clarified by legislation, the effect of including an amount that turns out to be less than the actual debt will have to await judicial development. Moreover, as noted above, in some other countries, unfortunately, this item, by reason of traditional practice in real property registries (in which context it is often useful), is mandatory, and, regrettably, often becomes the base for calculating the registration fee.

LA REGULACIÓN FRENTE A LA INESTABILIDAD FINANCIERA

Juan Manuel Ugarte Chávez

Frente a situaciones de inestabilidad y crisis financiera, desde hace más de dos siglos la respuesta inmediata ha sido mayor regulación y el perfeccionamiento de la regulación existente. Ejemplos de ello se encuentran desde el Bullion Report hasta la Ley Dodd-Frank, y la gran generación de medidas regulatorias sugeridas por el G20 y la Junta de Estabilidad Financiera (FSB) en los últimos cinco años. Sin embargo, la crisis actual, iniciada en 2007, ha puesto en evidencia no solamente la incapacidad de la regulación para alcanzar el objetivo de estabilidad financiera y económica mundial, sino también la crisis de las teorías existentes para explicar la realidad y transmitir la información correcta a los gobernantes para la toma de decisiones. El diseño y ejecución de medidas regulatorias en los ámbitos económico y financiero refleja nuevas formas de operación de la arquitectura de regulación y supervisión en el sistema mundial, y cada vez menores grados de libertad de los gobiernos de los países para diseñar y ejecutar sus políticas económicas y financieras de acuerdo a las condiciones prevalecientes en sus economías. Frente a ello, y a los mayores retos que plantean los riesgos globales se encuentra la necesidad de profundizar en nuevos desarrollos teóricos que expliquen las nuevas condiciones de las relaciones económicas y financieras entre los países, orientando la regulación al cumplimiento de los principios fundamentales del ser humano reflejados en mayores niveles de bienestar. Las nuevas formas de regulación deben estrechar los vínculos entre el sector financiero y el sector real de la economía, así como también generar los vehículos de expresión y perfeccionar los mecanismos de ejecución que permitan materializar mejores condiciones de convivencia entre los países. Estos son requisitos indispensables en la búsqueda de la estabilidad mundial que le dan congruencia con las aspiraciones legítimas de las sociedades de cada economía, individualmente.

BANKRUPTCY TOURISM IN EUROPE AND THE UNITED STATES

Jay Lawrence WESTBROOK

Although we have made great progress in recent years in overcoming parochialism in cases involving the bankruptcy of multinational corporations, that progress has inevitably created some new problems. The availability of increased recognition and cooperation in such cases has tempted debtor corporations to file their principal bankruptcy cases in jurisdictions outside their home countries. Not only do such proceedings often disappoint the legitimate expectations of their creditors and other stakeholders, but they create pressures to attract the substantial revenues involved in administration of cases of that sort, especially for professionals. A further consequence is the specter of bankruptcy "havens," often in the same countries which are regarded as havens for tax and bank secrecy purposes. Even where jurisdictions have a legitimate interest in the outcome of these proceedings, this sort of forum shopping tends to produce a race to the bottom in important respects and to undermine support for international cooperation generally. The solutions to these problems are still to be fully worked out, but this paper analyses the strengths and weaknesses of some possible approaches.

The Evolution of the Global Trade Over the Last Thirty Years, editado por el Instituto de Investigaciones Jurídicas de la UNAM, se terminó de imprimir el 10 de abril de 2014 en Formación Gráfica, S. A. C. V., Matamoros 112, col. Raúl Romero, Ciudad Nezahualcóyotl, 57630, Estado de México. Se utilizó tipo *Baskerville* de 9, 10 y 11 puntos. En esta edición se empleó papel cultura ahuesado de 70 x 95 de 50 kilos y cartulina sulfatada de 14 puntos para los forros; consta de 100 ejemplares (impresión *offset*).